FEDERAL DEPOSIT INSURANCE CORPORATION
Washington, D.C. 20429

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, 2019

FDIC Insurance Certificate Number: 35095

TOWNEBANK

(Exact name of registrant as specified in its charter)

VIRGINIA	**54-1910608**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
5716 High Street, Portsmouth, VA	**23703**
(Address of principal executive offices)	(Zip Code)

(757) 638-7500

(Registrant's telephone number, including area code)

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

Title of each class	**Trading Symbol(s)**	**Name of each exchange on which registered**
Common Stock, par value $1.667 per share	TOWN	The Nasdaq Global Select Market

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** [X]

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** [X]

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). **YES** [ ] **NO** [ ]

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

Large accelerated filer ☒	Accelerated filer ☐
Non-accelerated filer ☐	Smaller reporting company ☐
	Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). **YES** [ ] **NO** [X]

The aggregate market value of the common equity held by non-affiliates computed by reference to the price at which the common equity was last sold as of the last business day of the registrant's most recently completed second fiscal quarter was approximately $1.80 billion.

Number of shares of common stock outstanding at February 21, 2020: 72,624,475 shares

DOCUMENTS INCORPORATED BY REFERENCE

(1) Portions of the Registrant's 2019 Annual Report to Shareholders are incorporated by reference into Parts I, II, and IV; and

(2) Portions of the Registrant's 2020 Proxy Statement for its Annual Meeting of Shareholders to be held May 20, 2020 are incorporated by reference into Part III.

TOWNEBANK

Cross Reference Index

FORM 10-K

Part I

Part II

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PART I

Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements within the meaning of U.S. federal securities laws. These forward-looking statements speak only as of the date of this report, are based on current expectations, and involve a number of assumptions. These include statements regarding future economic performance, financial condition, prospects, growth, strategies and expectations, and objectives of management, and are generally identified by the use of words such as "believe," "expect," "intend," "anticipate," "estimate," or "project," or similar expressions. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 and we are including this statement for purposes of these safe harbor provisions. You should not place undue reliance on forward-looking statements, which are subject to assumptions that are subject to change. Our ability to predict results, or the actual effect of future plans or strategies, is inherently uncertain. These forward-looking statements are subject to a number of factors and uncertainties that could cause actual results to differ from those indicated or implied in the forward-looking statements and such differences may be material. Factors that could have a material effect on our operations and future prospects include but are not limited to: changes in interest rates, general economic and business conditions; legislative/regulatory changes; the monetary and fiscal policies of the U.S. government, including policies of the U.S. Department of the Treasury and the Board of Governors of the Federal Reserve System; the quality and composition of the loan and securities portfolios; demand for loan products; deposit flows; competition; demand for financial services in our market area; implementation of new technologies and the ability to develop and maintain secure and reliable electronic systems; changes in the securities markets; changes in accounting principles, policies and guidelines; the ability to identify attractive acquisition targets, complete acquisitions at a reasonable cost, and integrate the operations of acquired businesses; and other risk factors detailed from time to time in filings we make with the Federal Deposit Insurance Corporation. We undertake no obligation to update or clarify these forward-looking statements, whether as a result of new information, future events, or otherwise. For additional information on factors that could materially influence forward-looking statements included in this report, see the risk factors in "Item 1A. Risk Factors" in this report.

Item 1. BUSINESS

Overview

TowneBank began operations as a Virginia chartered bank in April 1999. We offer retail and commercial banking services to numerous markets in Virginia and North Carolina. We place special emphasis on serving the financial needs of individuals, commercial enterprises, and professionals.

Our foundation was built on providing banking services and, since inception, we have expanded to provide our members with complete residential real estate services, mortgage, personal and commercial insurance services, title-related services for both residential and commercial transactions, employee benefit services, and investment services. We offer a diversified range of financial services through our banking and non-banking subsidiaries. Additionally, through two controlled divisions, we provide investment and asset management services and originate mortgage loans, the majority of which are sold to investors on the national secondary market. Unless indicated otherwise, the terms “Company,” “we,” “us,” and “our” refer to TowneBank and our consolidated subsidiaries.

Our common stock is listed on the Nasdaq Global Select Market under the symbol TOWN. Our bank’s main office is located at 5716 High Street, Portsmouth, Virginia 23703 (telephone number 757-638-7500), and our Corporate Administration and Member Service Center is located at 6001 Harbour View Boulevard, Suffolk, Virginia 23435 (telephone number 757-638-6700). We have established banking offices in Chesapeake, Chesterfield County, Glen Allen, Hampton, James City County, Mechanicsville, Newport News, Norfolk, Portsmouth, Richmond, Suffolk, Virginia Beach, Williamsburg, and York County in Virginia, along with Raleigh, Cary, Charlotte, Greensboro, Greenville, Moyock, Grandy, Camden County, Southern Shores, Corolla and Nags Head in North Carolina. These locations are centrally located in core areas of each community, providing convenient access for both individual and business members.

A list of our subsidiaries is filed as Exhibit 21, and additional information relating to our business and our subsidiaries is included in the 2019 Annual Report to Shareholders (“Annual Report”) filed as Exhibit 13 and incorporated herein by reference.

Organization

We were organized and incorporated under the laws of the Commonwealth of Virginia on September 3, 1998, and commenced operations on April 8, 1999. We have three reportable segments: Banking, Realty, and Insurance.

Banking Segment. The Banking segment provides loan and deposit services to retail and commercial customers. We also provide commercial mortgage brokerage services and a variety of investment and asset management services.

Realty Segment. The Realty segment provides residential real estate services and originations of a variety of mortgage loans. We also provide resort property management and residential and commercial title insurance.

Insurance Segment. The Insurance segment provides individual and business members with a wide array of insurance products, including life, property, casualty, travel, and vehicle insurance, as well as employee and group benefits.

Operating Philosophy

Our operating philosophy emphasizes the making of marketing and member decisions at the local level (within centrally mandated and monitored control standards) with administrative and operational decisions at the central Company level. In order to accomplish this, we have established a “TowneBanking Group” (“Banking Group”) for each of our targeted markets.

We maintain a “hometown” banking image by providing each Banking Group with its own president, commercial loan officers, and local board of directors who are active and visible in their respective communities. It is the responsibility of each local board, acting under delegated authority of the Company’s Board of Directors, to direct our overall development in their respective markets. The separate Banking Groups, with local decision-making authority, allow us to more effectively identify and respond to the financial needs of our members.

The Board of Directors believes the separate Banking Groups strategy facilitates member service by ensuring senior management is actively involved in each community and is available on a day-to-day basis to respond to the needs of the members in each community. From a member perspective, each TowneBanking Group is positioned as a separate bank headquartered in its respective community.

Our strategic plan places increased emphasis on developing and generating noninterest, or fee, income. Such development involves looking for opportunities to grow that income source, including acquisitions of non-bank financial service providers. Noninterest income includes income generated by our subsidiaries and divisions, as well as service charges on deposit accounts and other fee income.

Services

We provide our members with high-quality, responsive, and technologically advanced services. Members have easy access to our decision-makers and enjoy continuity in service relationships, allowing a fast response to meet their needs. We plan to continue to pursue economically advantageous acquisitions and other strategic opportunities to grow our businesses.

Banking and Other Financial Services. The foundation of our banking services is built on being a reliable and consistent source of credit with loans that are priced based upon the overall banking relationship. Our capitalization provides a lending capacity to meet the credit needs of our targeted market segment. Further, we have various loan participation agreements with other financial institutions should the need arise to meet the additional credit needs of our members.

Through our Banking segment, we offer a full range of deposit products, including checking accounts, savings accounts, and various types of time deposit services, which range from daily money market accounts to long-term certificates of deposit. The transaction accounts and certificates of deposit are tailored by market area at rates competitive to those offered in the area. In addition, we offer retirement account services, such as Individual Retirement Accounts. All deposit accounts are insured by the Deposit Insurance Fund of the Federal Deposit Insurance Corporation ("FDIC") up to the maximum amount allowed by law and are solicited from individuals, businesses, associations and organizations, and governmental authorities.

Other services offered include safe deposit boxes, treasury management services, direct deposit of payroll and Social Security checks, and automatic drafts for various accounts. In addition, services to facilitate access to banking information and transactions, such as online banking, mobile banking, and on-call banking, are offered.

We also offer a full range of short- to medium-term personal and commercial loans. Personal loans include secured and unsecured loans for financing automobiles, home improvements, education, and personal investments. Commercial loans include secured and unsecured loans for working capital (including inventory and receivables), business expansion (including acquisition of real estate and improvements), and equipment and machinery purchases. Additionally, we originate fixed- and floating-rate mortgage loans, as well as real estate acquisition, development, and construction loans. Through TowneBank Commercial Mortgage, LLC, we broker larger commercial loans that are not intended to remain in our portfolio.

Through Towne 1031 Exchange, LLC, we offer the ability to serve as a qualified intermediary assisting investors with tax-deferred exchanges under Section 1031 of the Internal Revenue Code. We provide all necessary documentation to accomplish tax deferral while the investors' proceeds are safely held in accounts established at TowneBank awaiting reinvestment as required by Internal Revenue Service regulations.

Through Towne Investment Group and Towne Wealth Management, we offer other financial services, such as financial, retirement, and estate planning. We also offer assistance on a variety of investment options, including alternative investments, annuities, margin accounts, convertible bonds, and pension and profit-sharing plans. Towne Investment Group and Towne Wealth Management employ full-service financial advisors supported by an affiliation with Raymond James Financial, Inc., a full-service broker-dealer.

Realty Services. The full spectrum of services offered in our Realty segment allows us to realize certain operational synergies in providing quality residential real estate services, originations of a variety of residential mortgages, and title services for residential and commercial title transactions.

We assist customers with the process of buying or selling a home. Additionally, we also provide other realty-related services, including relocation services for individuals and families, including those in the military; and property management services for single-family homes, condominiums, townhomes, apartments, offices, vacation rentals, and retail establishments. Our vacation rentals business specializes in resort property management, offering vacation rentals with many of the most distinctive resort properties in Hilton Head, South Carolina; McHenry, Maryland; and Oak Island, North Carolina.

TowneBank Mortgage processes residential mortgage loans, from application acceptance to loan closing and funds disbursement. Once finalized, they are packaged and sold principally in the secondary market through purchase commitments from investors that subject us to only *de minimis* market risk. In addition to relocation and property management services, we offer title and settlement services, perform real estate closings for residential properties, and issue title insurance policies for both residential and commercial transactions.

Insurance Services. The Insurance segment provides individual and business members with a wide array of insurance products, including life, property, casualty, travel, and health insurance. Through Towne Insurance, we offer a full line of commercial and consumer insurance products and financial services. Through Towne Benefits, we offer individual and group life and health insurance. Through Red Sky, we offer travel, medical, and baggage protection insurance for travelers via vacation property management companies.

Competition

Because we offer a wide variety of financial services, we compete with other financial institutions as well as other financial service providers, real estate companies, mortgage loan originators, and insurance companies. Competition is generally based on pricing and quality of products and services offered, level of service, convenience, availability of services, and the degree of expertise and personal manner in which services are offered.

There is significant competition within the banking and financial services industry in our market areas. We face competition from other banks, savings institutions, credit unions, consumer finance companies, insurance companies, real estate companies, and other financial institutions in our targeted market areas. Many of our larger competitors have broader geographic markets and substantially greater resources and can offer more diversified products and services. Increasingly, we compete with other companies based on financial technology and capabilities. Competition among providers of financial products and services continues to increase as technology advances have lowered the barriers to entry for financial technology companies, with customers having the opportunity to select from a growing variety of traditional and nontraditional alternatives, including crowdfunding, digital wallets and money transfer services. The ability of non-banking financial institutions to provide services previously limited to commercial banks has intensified competition. Because nonbank financial institutions are not subject to the same regulatory restrictions as banks and bank holding companies, they can often operate with greater flexibility and lower cost structures.

Despite the intense level of competition, we believe the existing and future banking and financial services market in our market areas represents excellent opportunities for a locally owned and managed financial services company with a strong community philanthropic philosophy, such as Towne. Among other factors, the economic outlook for the areas and the size and growth potential of the existing markets for banking and other financial services point to a growing demand for such services. Further, in view of the continuing trend in the financial services industry toward consolidations into larger, sometimes impersonal, national institutions, our company fulfills a market demand for the personal and customized financial services an independent, locally run company can offer.

Market Area

Our primary service area is Richmond, Virginia, the Greater Hampton Roads region in southeastern Virginia, northeastern North Carolina, and the Raleigh, Charlotte, Greenville and Greensboro metropolitan areas in North Carolina. In Virginia, our service area encompasses the Virginia Beach-Norfolk-Newport News, VA-NC ("Hampton Roads") Metropolitan Statistical Area ("MSA"), the 37th largest metropolitan area in the United States, with a population of approximately 1.73 million as of July 2018, and the Richmond, VA ("Richmond") MSA, the 44th largest metropolitan area in the United States, with a population of approximately 1.31 million as of July 2018. In North Carolina, our service area now encompasses the Raleigh, NC ("Raleigh") MSA, the 42nd largest metropolitan area in the United States, with a population of approximately 1.36 million as of July 2018, and the Charlotte, NC ("Charlotte") MSA, the 23rd largest metropolitan area in the United States, with a population of approximately 2.57 million as of July 2018.

We also offer residential mortgages in Charlottesville, Virginia; Wilmington, North Carolina, in the Washington-Arlington-Alexandria, DC-VA-MD-WV MSA; in the Baltimore-Columbia-Towson, MD MSA; in Frederick, Maryland; and in Lancaster, Pennsylvania. Additionally, we have insurance offices located in Charlotte, Greenville and Raleigh, North Carolina; Rock Hill, Lancaster, and Spartanburg, South Carolina; and the counties of Essex, Gloucester, Northumberland, Prince William, and Richmond in Virginia.

Concentrations

The majority of our depositors are located and doing business in our targeted market areas, and we lend a substantial portion of our capital and deposits to individual and business borrowers in these market areas. Any factors adversely affecting the economy of our targeted market areas could, in turn, adversely affect our performance. A geographic concentration exists with our loan portfolio, as most of our business activity is with members in our targeted market areas. There were no significant concentrations in any one customer; however, we have a concentration in commercial real estate loans.

Governmental Monetary Policies

Our earnings and growth are affected not only by general economic conditions, but also by the monetary policies of various governmental regulatory authorities, particularly the Board of Governors of the Federal Reserve System ("Federal Reserve"). The Federal Reserve implements national monetary policy through its open market operations in United States government securities, control of the discount rate, and establishment of reserve requirements against both member and nonmember financial institutions' deposits.

These actions have a significant effect on the overall growth and distribution of loans, investments, and deposits, as well as rates earned on loans or paid on deposits. Federal Reserve monetary policies have had a significant effect on the operating results of commercial banks in the past and are expected to do so in the future. Management is unable to predict the effect of possible changes in monetary policies upon our future operating results.

Part I

Development of Business

The following is a summary of developments in our business since January 1, 2019:

- Effective January 1, 2019, the Company acquired Straus, Itzkowitz & LeCompte Insurance Agency, Inc., an independent insurance agency, which was merged into the operations of Towne Insurance Agency, LLC.

- Effective September 1, 2019, the Company acquired Angel Insurance and Financial Services, Inc., an independent insurance agency, which was also merged into the operations of Towne Insurance Agency, LLC.

- Effective February 19, 2019, we opened a banking office in Greenville, North Carolina and on November 12, 2019 we opened a banking office in Greensboro, North Carolina.

- TowneBank remained in first place in the latest Hampton Roads Annual Deposit Market Share Report released by the FDIC. The report ranks institutions by share of FDIC-insured deposits in the Hampton Roads MSA as of June 30, 2019. TowneBank had a 23.92% share of deposits in Hampton Roads and was the only community bank with a share greater than 5%. TowneBank was in seventh place in the Richmond MSA in the FDIC's Annual Deposit Market Share Report with $1.10 billion in deposits as of June 30, 2019. In our North Carolina markets, TowneBank ranked seventh in the Raleigh MSA with a 4.73% market share and eighth in the Charlotte MSA with a 0.30% market share.

Prior to 2019, our most significant acquisitions included the following:

- On January 26, 2018, the Company acquired Paragon and its wholly owned bank subsidiary, Paragon Commercial Bank, a Raleigh, North Carolina-based bank with three banking offices servicing Raleigh, Cary, and Charlotte, North Carolina. The acquisition added approximately $1.43 billion in loans and assumed approximately $1.25 billion in deposits.

- On June 24, 2016, TowneBank acquired Monarch Financial Holdings, Inc. and its wholly owned bank subsidiary, Monarch Bank, headquartered in Chesapeake, Virginia. The acquisition added approximately $808.14 million in loans and \ approximately $1.06 billion in deposits.

- On January 2, 2015, TowneBank acquired Franklin Financial Corporation and its wholly owned subsidiary, Franklin Federal Savings Bank, based in Richmond, Virginia. The acquisition added eight office locations, approximately $491.96 million in loans and approximately $682.95 million in deposits.

We anticipate concentrating on the further development of our markets by seeking mergers and acquisitions opportunities or opening additional banking offices as business and other conditions warrant, and by expanding into new markets as opportunities arise. The regulatory approval process for the opening of additional banking offices takes into account a number of factors, including, among others, a determination that we have capital in an amount deemed necessary to warrant additional expansion, and a finding that the public interest will be served. Additionally, we will continue to place a focus on the development of noninterest income sources and will look for growth opportunities, which could include additional acquisitions of non-bank financial service providers.

Supervision and Regulation

We are regulated extensively under both federal and state law. The following is a brief summary of the material statutes, acts, rules, and regulations that affect us. This summary is qualified in its entirety by reference to the full text of the statutes, acts, rules, regulations, and policies referenced below. Changes in statutes, acts, rules, regulations, or regulatory policies could have a material effect on our business.

General. We are organized as a Virginia chartered banking corporation and are regulated and supervised by the Bureau of Financial Institutions of the Virginia State Corporation Commission ("Bureau of Financial Institutions"). In addition, we are regulated and supervised by the FDIC, which serves as our primary federal regulator. The Bureau of Financial Institutions and the FDIC conduct regular examinations of us, reviewing the adequacy of our loan loss reserves, the quality of our loans and investments, the appropriateness of management practices, compliance with laws and regulations, and other aspects of our operations. In addition to these regular examinations, we must furnish to the FDIC quarterly and annual reports containing detailed financial statements and schedules. Federal and Virginia banking laws and regulations govern all areas of our operations, including reserves, loans, mortgages, capital, issuance of securities, payment of dividends, and establishment of branches. The FDIC and the Bureau of Financial Institutions have authority to impose penalties, initiate civil and administrative actions, and take other steps intended to prevent us from engaging in unsafe or unsound practices. In this regard, the FDIC has adopted capital adequacy requirements.

We are also subject to the enforcement and rule-making authority of the Consumer Financial Protection Bureau ("CFPB") regarding consumer financial products. The CFPB has the authority to create and enforce consumer protection rules and regulations and has the power to examine us for compliance with such rules and regulations. The CFPB also has the authority to prohibit "unfair, deceptive or abusive" acts and practices. The CFPB has examination and enforcement authority over all banks and their affiliates with more than $10 billion in assets, which we exceeded following the Paragon acquisition that was effective January 26, 2018.

Capital Requirements. Federal bank regulatory agencies have adopted risk-based capital requirements for assessing bank capital adequacy. Virginia chartered banks must also satisfy the capital requirements adopted by the Bureau of Financial Institutions. The federal capital standards define capital and establish minimum capital requirements in relation to assets and off-balance-sheet exposure as adjusted for credit risk.

In July 2013, the FDIC and other federal bank regulatory agencies approved final rules known as the "Basel III Capital Rules," which substantially revised the risk-based capital and leverage capital requirements applicable to bank holding companies and depository institutions, including the Company. The Basel III Capital Rules went into effect for the Company on January 1, 2015 (subject to a phase-in period that ended on January 1, 2019).

The Basel III Capital Rules, among other things, (i) introduced as a new capital measure "Common Equity Tier 1" ("CET1"), (ii) specified that Tier 1 capital consists of CET1 and "Additional Tier 1 capital" instruments meeting specified requirements, (iii) defined CET1 narrowly by requiring that most adjustments to regulatory capital measures be made to CET1 and not to the other components of capital, and (iv) expanded the scope of the adjustments as compared to existing regulations. CET1 capital consists of common stock instruments that meet eligibility criteria in the final rules, retained earnings, and common equity Tier 1 minority interest. The capital rules require banks to include accumulated other comprehensive income ("AOCI") into CET1 unless the bank used a one-time election to exclude AOCI from its regulatory capital metrics. We elected to exclude AOCI from CET1.

The Basel III Capital Rules require banking organizations to maintain (i) a minimum ratio of CET1 to risk-weighted assets of at least 4.5%, plus a 2.5% "capital conservation buffer" (which is added to the 4.5% CET1 ratio, effectively resulting in a minimum ratio of CET1 to risk-weighted assets of at least 7.0%); (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0%, plus the capital conservation buffer (which is added to the 6.0% Tier 1 capital ratio, effectively resulting in a minimum Tier 1 capital ratio of 8.5%); (iii) a minimum ratio of total capital (that is, Tier 1 plus Tier 2 capital) to risk-weighted assets of at least 8.0%, plus the capital conservation buffer (which is added to the 8.0% total capital ratio, effectively resulting in a minimum total capital ratio of 10.5%); and (iv) a minimum leverage ratio of 4.0%, calculated as the ratio of Tier 1 capital to adjusted average quarterly assets.

The aforementioned capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions that fail to meet the effective minimum ratios once the capital conservation buffer is taken into account, as detailed above, will face limitations on the payment of dividends, common stock repurchases, and discretionary cash payments to executive officers based on the amount of the shortfall and the institution's "eligible retained income" (four quarter trailing net income, net of distributions and tax effects not reflected in net income).

The Basel III Capital Rules provide for a number of deductions from and adjustments to CET1. In July 2019, the federal banking agencies adopted final rules (the "Capital Simplification Rules") that, among other things, revised these deductions and adjustments. Following the adoption of the Capital Simplification Rules, certain deferred tax assets and significant investments in non-consolidated financial entities must be deducted from CET1 to the extent that any one such category exceeds 25% of CET1. Prior to the adoption of the Capital Simplification Rules, amounts were deducted from CET1 to the extent that any one such category exceeded 10% of CET1 or all such items, in the aggregate, exceeded 15% of CET1. The Capital Simplification Rules took effect for the Company as of January 1, 2020. These limitations did not impact our regulatory capital during any of the reported periods.

The Basel III Capital Rules prescribe a standardized approach for risk weightings that expanded the risk-weighting categories from the general risk-based capital rules 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 and agency securities, to 600% for certain equity exposures (and higher percentages for certain other types of interests), and resulting in higher risk weights for a variety of asset categories. In November 2019, the federal banking agencies adopted a rule revising the scope of commercial real estate mortgages subject to a 150% risk weight.

In December 2017, the Basel Committee on Banking Supervision (the "Basel Committee") published standards that it described as the finalization of the Basel III post-crisis regulatory reforms (the standards are commonly referred to as "Basel IV"). Among other things, these standards revise the Basel Committee's standardized approach for credit risk (including by recalibrating risk weights and introducing new capital requirements for certain "unconditionally cancellable commitments," such as unused credit card lines of credit) and provides a new standardized approach for operational risk capital. Under the Basel framework, these standards will generally be effective on January 1, 2022, with an aggregate output floor phasing in through January 1, 2027. Under the current U.S. capital rules, operational risk capital requirements and a capital floor apply only to advanced approaches institutions, and not to the Company. The impact of Basel IV on us will depend on the manner in which it is implemented by the federal bank regulatory agencies.

Prompt Corrective Action. The Federal Deposit Insurance Act, as amended ("FDIA"), requires among other things, the federal bank regulatory agencies to take "prompt corrective action" against depository institutions that do not meet minimum capital requirements. The FDIA includes the following five capital tiers: "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized."

In order to be adequately capitalized for purposes of the prompt corrective action rules, a banking organization is required to have at least an 8% total risk-based capital ratio, a 6% Tier 1 risk-based capital ratio, a 4.5% CET1 risk-based capital ratio, and a 4% Tier 1 leverage ratio. To be well-capitalized, a banking organization is required to have at least a 10% total risk-based capital ratio, an 8% Tier 1 risk-based capital ratio, a 6.5% CET1 risk-based capital ratio, and a 5% Tier 1 leverage ratio. An institution may be downgraded to, or deemed to be in, a capital category that is lower than indicated by its capital ratios if it is determined to be in an unsafe or unsound condition or if it receives an unsatisfactory examination rating with respect to certain matters. A bank's capital category is determined solely for the purpose of applying prompt corrective action regulations, and the capital category may not constitute an accurate representation of the bank's overall financial condition or prospects for other purposes.

At December 31, 2019, we had the following risk-based capital and leverage ratios relative to regulatory minimums.

Ratio	TowneBank	Minimum	Well Capitalized
Common equity Tier 1	11.46%	4.50%	6.50%
Tier 1 risk-based capital	11.49%	6.00%	8.00%
Total risk-based capital	14.58%	8.00%	10.00%
Tier 1 leverage	9.95%	4.00%	5.00%

The FDIC is authorized by federal legislation and regulations to take various enforcement actions against any undercapitalized insured depository institution and any insured depository institution that fails to submit an acceptable capital restoration plan or fails to implement a plan accepted by the FDIC. These powers include, among other things, requiring a bank to be recapitalized, prohibiting asset growth, restricting interest rates paid, requiring prior approval of capital distributions, requiring divestiture by the institution of its subsidiaries, requiring new election of directors, and requiring the dismissal of directors and officers.

Dividends. The amount of dividends payable depends upon our earnings and capital position and is limited by federal and state laws, regulations, and policies. In addition, under Virginia law, the Bureau of Financial Institutions may limit the ability of the bank to pay dividends. No dividend may be declared or paid that would impair a bank's paid-in capital.

The Bureau of Financial Institutions and the FDIC have the general authority to limit dividends paid if such payments are deemed to constitute an unsafe and unsound practice. In particular, Section 38 of the Federal Deposit Insurance Act would prohibit us from making a dividend if we were "undercapitalized" or if such dividend would result in us becoming "undercapitalized."

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). On July 21, 2010, the Dodd-Frank Act was signed into law. The Dodd-Frank Act implemented significant changes to the regulation of the financial services industry and affected the lending, investment, trading, and operating activities of financial institutions. The legislation directed federal bank regulatory agencies to implement new leverage and capital requirements. These requirements take into account off-balance sheet activities and other risks, including risks relating to securitized products and derivatives. The Dodd-Frank Act created a new Financial Stability Oversight Council to identify systemic risks in the financial system and gives federal regulators new authority to take control of and liquidate financial firms. In addition, the Dodd-Frank Act contains a wide variety of provisions affecting the regulation of depository institutions, including restrictions related to mortgage originations, risk retention requirements as to securitized loans, establishment of the CFPB, and restrictions on proprietary trading.

Because our assets exceed $10 billion, we are subject to the Durbin Amendment promulgated under the Dodd-Frank Act. Under the rule, the maximum permissible interchange fee for an electronic debit transaction is the sum of 21 cents per transaction and five basis points multiplied by the value of the transaction. The rules also allow for an upward adjustment of no more than one cent to an issuer's debit card interchange fee if the issuer develops and implements policies and procedures reasonably designed to achieve certain fraud-prevention standards. This limitation on interchange fees began impacting our noninterest income in the third quarter of 2019. The impact was a reduction in noninterest income service charges of approximately $1.90 million in the second half of 2019.

The Dodd-Frank Act created the CFPB, an independent federal agency, with broad rule-making, supervisory, and enforcement powers under various federal consumer financial protection laws. The CFPB has examination and primary enforcement authority with respect to depository institutions with $10 billion or more in assets, such as the

Company. Smaller institutions are subject to rules promulgated by the CFPB, but are examined and supervised by federal banking regulatory agencies for consumer compliance purposes.

The Economic Growth, Regulatory Relief and Consumer Protection Act of 2018, which was signed into law on May 24, 2018 (the “EGRRCPA”), amended the Dodd-Frank Act to provide regulatory relief for certain smaller and regional financial institutions. The EGRRCPA, among other things, exempted banks with less than $250 billion in total consolidated assets, such as the Company, from the enhanced prudential standards and the company-run and supervisory stress tests previously required under the Dodd-Frank Act. The amendments to the Dodd-Frank Act were effective for the Company in November 2019.

The Dodd-Frank Act has had, and may in the future have, a material impact on the Company’s operations, particularly through increased compliance costs resulting from new and possible future consumer and fair lending regulations. See Part I, Item 1A, “Risk Factors” for additional discussion of this topic.

FDIC Insurance Assessments. Substantially all of our members’ deposit accounts are insured up to applicable limits by the Deposit Insurance Fund (the “DIF”) of the FDIC and are subject to deposit insurance assessments to maintain the DIF.

The Dodd-Frank Act permanently increased the maximum deposit insurance amount for banks, savings institutions, and credit unions to $250,000 per depositor, per insured depository institution, for each account ownership category.

The Dodd-Frank Act also broadened the base for FDIC insurance assessments. Assessments are now based on average consolidated total assets less tangible equity capital of a financial institution. The Dodd-Frank Act required the FDIC to increase the reserve ratio of the DIF from 1.15% to 1.35% of insured deposits by 2020, and eliminates the requirement that the FDIC pay dividends to insured depository institutions when the reserve ratio exceeds certain thresholds. On September 30, 2018, the DIF reserve ratio reached 1.36%, exceeding the statutorily required minimum reserve ratio of 1.35% ahead of the 2020 deadline, which ended surcharges on insured depository institutions with assets greater than $10 billion. Banks with assets of less than $10 billion were awarded assessment credits for their portion of their assessments that contributed to the growth in the reserve ratio from 1.15% to 1.35%. Because our assessments contributing to the growth in the reserve ratio occurred prior to our total assets exceeding $10 billion, when the reserve ratio exceeded 1.38% in June 2019, the FDIC applied these credits to TowneBank's assessment invoices beginning in the second quarter assessment period of 2019. The Company's total assessment credit was $2.53 million.

FDIC insurance expense totaled $0.85 million, $2.89 million, and $2.45 million in 2019, 2018, and 2017. FDIC insurance expense previously included deposit insurance assessments and Financing Corporation (“FICO”) assessments related to outstanding FICO bonds. These assessments have ceased as all FICO bonds matured in 2019.

Because our total consolidated assets exceed $10 billion, the FDIC uses a performance score and a loss-severity score to calculate our assessment rate. In calculating these scores, the FDIC uses a bank’s capital level and regulatory supervisory ratings and certain financial measures to assess an institution’s ability to withstand asset-related stress and funding-related stress. The FDIC also has the ability to make discretionary adjustments to the total score based upon significant risk factors that are not adequately captured in the calculations. In addition to ordinary assessments described above, the FDIC has the ability to impose special assessments in certain instances.

Historically, deposit insurance premiums we have paid to the FDIC have been deductible for federal income tax purposes; however, the Tax Cuts and Jobs Act of 2017 disallowed the deduction of such premium payments for banking organizations with total consolidated assets of $50 billion or more. For banks with less than $50 billion in total consolidated assets, such as the Company, the premium deduction is being phased out based on the proportion of a bank's assets exceeding $10 billion. The premium expense disallowed in 2019 was insignificant.

Community Reinvestment Act. Banks are subject to the provisions of the Community Reinvestment Act of 1977 ("CRA") that requires the appropriate federal bank regulatory agency, the FDIC in our case, to assess our record in meeting the credit needs of the communities we serve.

The CRA assessment is required by any bank that has applied to, among other things, establish a new branch office that will accept deposits; relocate an existing office; or merge, consolidate with, acquire the assets of, or assume the liabilities of a federally-regulated financial institution. We received an "Outstanding" rating in our last CRA examination.

In December 2019, the FDIC and the Office of the Comptroller of the Currency jointly proposed rules that would significantly change existing CRA regulations. The proposed rules are intended to increase bank activity in low- and moderate-income communities where there is significant need for credit, more responsible lending, greater access to banking services, and improvements to critical infrastructure. The proposals change four key areas: (i) clarifying what activities qualify for CRA credit; (ii) updating where activities count for CRA credit; (iii) providing a more transparent and objective method for measuring CRA performance; and (iv) revising CRA-related data collection, record keeping, and reporting. We are evaluating what impact this proposed rule, if implemented, may have on the Company.

Federal Deposit Insurance Corporation Improvement Act. The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") became effective July 2, 1993. FDICIA requires insured institutions with $500 million or more in total assets at the beginning of their fiscal year to submit independently audited annual reports to the FDIC and the appropriate agency.

These publicly available reports must include: (i) annual financial statements prepared in accordance with accounting principles generally accepted in the United States and such other disclosure requirements as required by the FDIC or the appropriate agency, and (ii) a management report signed by the Chief Executive Officer and the Chief Financial Officer or Chief Accounting Officer of the institution that contains a statement of management's responsibilities for: (a) preparing the annual financial statements, (b) establishing and maintaining an adequate internal control structure and procedures for financial reporting, and (c) complying with the laws and regulations designated by the FDIC relating to safety and soundness, and an assessment of: (1) the effectiveness of the system of internal control and procedures for financial reporting as of the end of the fiscal year, and (2) the institution's compliance during the fiscal year with applicable laws and regulations designated by the FDIC relating to safety and soundness.

With respect to any internal control report, the institution's independent public accountants must attest to, and report separately on, certain assertions of the institution's management contained in such report for institutions with $1 billion or more in total assets.

Privacy Legislation. Several laws, including the Privacy of Consumer Financial Information (Part V of the Gramm-Leach-Bliley Act) and related regulations issued by federal bank regulatory agencies, provide protections against the transfer and use of customer information by financial institutions. A financial institution must provide to its customers information regarding its policies and procedures with respect to the handling of customers' personal information. Each institution must conduct an internal risk assessment of its ability to protect customer information. These privacy provisions generally prohibit a financial institution from providing a customer's personal financial information to unaffiliated parties without prior notice and approval from the customer.

Bank Secrecy Act. The Bank Secrecy Act ("BSA"), which is intended to require financial institutions to develop policies, procedures, and practices to prevent and deter money laundering, mandates that every bank have a written, board-approved program that is reasonably designed to assure and monitor compliance with the BSA. The program must, at a minimum: (i) provide for a system of internal controls to assure ongoing compliance; (ii) provide for independent testing for compliance; (iii) designate an individual responsible for coordinating and monitoring day-to-day compliance; and (iv) provide training for appropriate personnel. In addition, a bank is required to adopt a customer identification program as part of its BSA compliance program. Financial institutions are generally required to report cash transactions involving more than $10,000 to the U.S. Department of the Treasury. In addition, financial institutions are required to file suspicious activity reports for transactions that involve more than $5,000 and which the financial institution knows, suspects or has reason to suspect involves illegal funds, is designed to evade the requirements of the BSA, or has no lawful purpose. The USA PATRIOT Act of 2001, enacted in response to the September 11, 2001, terrorist attacks, requires bank regulators to consider a financial institution's compliance with the BSA when reviewing applications from a financial institution. In May 2016, the regulations implementing the BSA were amended to explicitly include risk-based procedures for conducting ongoing customer due diligence, to include understanding the nature and purpose of customer relationships for the purpose of developing a customer risk profile. In addition, banks must identify and verify the identity of the beneficial owners of all legal entity customers (other than those that are excluded) at the time a new account is opened (other than accounts that are exempted).

Incentive Compensation. In June 2010, the federal bank regulatory agencies issued comprehensive final guidance on incentive compensation policies 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 *Interagency Guidance on Sound Incentive Compensation Policies*, which covers all employees who have the ability to materially affect the risk profile of a financial 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's 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 financial institution's board of directors.

Section 956 of the Dodd-Frank Act requires the federal bank regulatory agencies and the Securities and Exchange Commission to establish joint regulations or guidelines prohibiting incentive-based payment arrangements at specified regulated entities that encourage inappropriate risk-taking by providing an executive officer, employee, director or principal shareholder with excessive compensation, fees, or benefits or that could lead to material financial loss to the entity. The federal bank regulatory agencies issued such proposed rules in March 2011 and issued a revised proposed rule in June 2016 implementing the requirements and prohibitions set forth in Section 956. The revised proposed rule would apply to all banks, among other institutions, with at least $1 billion in average total consolidated assets, for which it would go beyond the existing *Interagency Guidance on Sound Incentive Compensation Policies* to (i) prohibit certain types and features of incentive-based compensation arrangements for senior executive officers, (ii) require incentive-based compensation arrangements to adhere to certain basic principles to avoid a presumption of encouraging inappropriate risk, (iii) require appropriate board or committee oversight, (iv) establish minimum recordkeeping, and (v) mandate disclosures to the appropriate federal bank regulatory agency. These proposed rules have not yet been finalized.

Consumer Financial Protection. We are subject to a number of federal and state consumer protection laws that extensively govern our relationship with our customers. These laws include the Equal Credit Opportunity Act, the Fair Credit Reporting Act, the Truth in Lending Act, the Truth in Savings Act, the Electronic Fund Transfer Act, the Expedited Funds Availability Act, the Home Mortgage Disclosure Act, the Fair Housing Act, the Real Estate Settlement Procedures Act, the Fair Debt Collection Practices Act, the Service Members Civil Relief Act, laws governing flood insurance, federal and state laws prohibiting unfair and deceptive business practices, foreclosure laws, and various regulations that implement some or all of the foregoing. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits, making loans, collecting loans, and providing other services. If we fail to comply with these laws and regulations, we may be subject to various penalties. Failure to comply with consumer protection requirements may also result in failure to obtain any required bank regulatory approval for merger or acquisition transactions we may wish to pursue, or being prohibited from engaging in such transactions even if approval is not required.

The Dodd-Frank Act centralized responsibility for consumer financial protection by creating a new agency, the CFPB, and giving it responsibility for implementing, examining, and enforcing compliance with federal consumer protection laws. The CFPB focuses on (i) risks to consumers and compliance with federal consumer financial laws, (ii) the markets in which firms operate and risks to consumers posed by activities in those markets, (iii) depository institutions that offer a wide variety of consumer financial products and services, and (iv) non-depository companies that offer one or more consumer financial products or services.

The CFPB has broad rule-making authority for a wide range of consumer financial laws that apply to all banks, including, among other things, the authority to prohibit “unfair, deceptive or abusive” acts and practices. Abusive acts or practices are defined as those that materially interfere with a consumer’s ability to understand a term or condition of a consumer financial product or service or take unreasonable advantage of a consumer’s (i) lack of financial savvy, (ii) inability to protect himself in the selection or use of consumer financial products or services, or (iii) reasonable reliance on a covered entity to act in the consumer’s interests. The CFPB can issue cease-and-desist orders against banks and other entities that violate consumer financial laws. The CFPB may also institute a civil action against an entity in violation of federal consumer financial law in order to impose a civil penalty or injunction.

Ability-to-Repay and Qualified Mortgage Rule. Pursuant to the Dodd-Frank Act, the CFPB issued a final rule, amending Regulation Z as implemented by the Truth in Lending Act, requiring mortgage lenders to make a reasonable and good faith determination based on verified and documented information that a consumer applying for a mortgage loan has a reasonable ability to repay the loan according to its terms. Mortgage lenders are required to determine consumers’ ability to repay in one of two ways. The first alternative requires the mortgage lender to consider the following eight underwriting factors when making the credit decision: (i) current or reasonably expected income or assets; (ii) current employment status; (iii) the monthly payment on the covered transaction; (iv) the monthly payment on any simultaneous loan; (v) the monthly payment for mortgage-related obligations; (vi) current debt obligations, alimony, and child support; (vii) the monthly debt-to-income ratio or residual income; and (viii) credit history. Alternatively, the mortgage lender can originate “qualified mortgages,” which are entitled to a presumption that the creditor making the loan satisfied the ability-to-repay requirements. In general, a “qualified mortgage” is a mortgage loan without negative amortization, interest-only payments, balloon payments, or terms exceeding 30 years. In addition, to be a qualified mortgage the points and fees paid by a consumer cannot exceed 3% of the total loan amount. Qualified mortgages that are “higher-priced” (e.g., subprime loans) garner a rebuttable presumption of compliance with the ability-to-repay rules, while qualified mortgages that are not “higher-priced” (e.g., prime loans) are given a safe harbor of compliance. The Company is predominantly an originator of compliant qualified mortgages.

Tax Reform. On December 22, 2017, the President of the United States signed into law the Tax Cuts and Jobs Act of 2017 "TCJA". The legislation made key changes to the U.S. tax law, including the reduction of the U.S. federal corporate tax rate from 35% to 21%, effective January 1, 2018. As a result of the reduction in the U.S. corporate income tax rate from 35% to 21% under the TCJA, the Company revalued its ending net deferred tax assets at December 31, 2017 and recognized a provisional $10.11 million tax expense in the Company’s consolidated statement of income for the year ended December 31, 2017. An additional expense of $0.70 million was recognized in 2018 due to the finalization of the provisional component of the TCJA.

Cybersecurity. In March 2015, federal regulators issued two related statements regarding cybersecurity. One statement indicates that financial institutions should design multiple layers of security controls to establish lines of defense and to ensure that their risk management processes also address the risk posed by compromised customer credentials, including security measures to reliably authenticate customers accessing internet-based services of the financial institution. The other statement indicates that a financial institution's management is expected to maintain sufficient business continuity planning processes to ensure the rapid recovery, resumption and maintenance of the institution's operations after a cyber-attack involving destructive malware. A financial institution is also expected to develop appropriate processes to enable recovery of data and business operations and address rebuilding network capabilities and restoring data if the institution or its critical service providers fall victim to this type of cyber-attack. If the Company fails to observe the regulatory guidance, it could be subject to various regulatory sanctions, including financial penalties.

Reporting Obligation Under Securities Laws. We are subject to the periodic reporting requirements of the Securities Exchange Act of 1934 ("Exchange Act") as adopted by the FDIC, including the filing of annual, quarterly, and other reports with the FDIC. As an Exchange Act reporting bank with over $500 million in assets, we are directly affected by the Sarbanes-Oxley Act of 2002 and regulations promulgated thereunder, which are aimed at improving corporate governance and reporting procedures. We are also subject to the rules and listing standards adopted by The Nasdaq Stock Market, LLC. We are complying with the rules and regulations implemented pursuant to the Sarbanes-Oxley Act and by The Nasdaq Stock Market, LLC, and intend to comply with any applicable rules and regulations implemented in the future.

Future Legislation and Regulation. Congress may enact legislation from time to time that affects the regulation of the financial services industry, and state legislatures may enact legislation from time to time affecting the regulation of financial institutions chartered by or operating in those states. Federal and state regulatory agencies also periodically propose and adopt changes to their regulations or change the manner in which existing regulations are applied. The substance or impact of pending or future legislation or regulation, or the application thereof, cannot be predicted, although enactment of the proposed legislation could impact the regulatory structure under which we operate and may significantly increase costs, impede the efficiency of internal business processes, require an increase in regulatory capital, require modifications to business strategy, and limit the ability to pursue business opportunities in an efficient manner.

Employees

As of December 31, 2019, we had 2,446 full-time equivalent employees, excluding real estate sales agents. There were 407 real estate sales agents at December 31, 2019. Our real estate agents are independent contractors and not included as our employees. None of our employees are represented by any collective bargaining agreements, and relations with employees are considered good.

Available Information

Our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports are filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act and are accessible at no cost on our website, www.townebank.com, as soon as reasonably practicable after those reports have been filed with or furnished to the FDIC. These materials are available free of charge in print to stockholders who request them by writing to: TowneBank, 6001 Harbour View Boulevard, Suffolk, Virginia 23435. A copy of the statements of beneficial ownership of our equity securities filed by our directors, officers, and 10% or greater shareholders under Section 16 of the Exchange Act may also be obtained through our website. The information contained on our website is not a part of or included in this Form 10-K.

The public may read and copy any of the reports filed with the FDIC at the FDIC's Accounting and Securities Disclosure Section, Division of Risk Management Supervision, 550 17th Street, N.W., Washington, D.C. 20429. The public may contact the FDIC at 202-898-8913 should they require a copy of a filing be sent directly to them.

Item 1A. RISK FACTORS

In addition to the other information contained in this report, the following risks may affect us. This listing should not be considered all-inclusive. Additional risks and uncertainties, including those not presently known to us or that we currently consider immaterial, may also impair our business, financial condition, or operating results.

Dependence on uncontrollable economic conditions could have a material adverse impact on our financial condition and results of operations.

Like all financial institutions, we are subject to the effects of any economic downturn. During the past decade, the U.S. economy faced a severe economic crisis, including a major recession. Business activity across a wide range of industries and regions in the U.S. was reduced, and local governments and many businesses experienced financial difficulty. Our business is concentrated in the Richmond, Virginia region, the Greater Hampton Roads region in southeastern Virginia, northeastern North Carolina, and the Raleigh and Charlotte metropolitan areas in North Carolina. As a result, the financial condition and results of operations may be affected by changes in the economies of these regions. Adverse changes in economic conditions in our market areas would likely impair the ability to collect loans and could otherwise have a material adverse effect on our financial condition and results of operations. While conditions have improved since the recession, there can be no assurance that this improvement will be sustained, and any declines may have a negative effect on our financial conditions and results of operations.

Changes in defense spending by the federal government as a result of congressional budget cuts could adversely impact the economy in Greater Hampton Roads, which could have an adverse effect on our results of operations and financial condition.

The U.S. military has a major presence in Greater Hampton Roads. As a result, the U.S. military is an important aspect of the Greater Hampton Roads economy in which we operate. Actual and proposed cuts to defense and other security spending could have an adverse impact on the Greater Hampton Roads economy, which could adversely affect our business, financial condition, and results of operations.

Changes in interest rates could have a negative impact on our results of operations.

Our profitability is dependent to a large extent on our net interest income, which is the difference between interest income on interest-earning assets and interest expense on interest-bearing liabilities. Our net interest income is impacted by changes in market rates of interest, changes in credit spreads, changes in the shape of the yield curve, the interest rate sensitivity of our assets and liabilities, prepayments on our loans and investments, and the mix of our funding sources and assets.

Our interest-earning assets and interest-bearing liabilities may react in different degrees to changes in market interest rates. Interest rates on some types of assets and liabilities may fluctuate prior to changes in broader market interest rates, while rates on other types may lag behind. The result of these changes to rates may cause differing spreads on interest-earning assets and interest-bearing liabilities. Any substantial, unexpected, or prolonged change in market interest rates could have a material adverse effect on our business, financial condition, and results of operations. While we take measures, such as hedging our mortgage loans held for sale, intended to manage risks from changes in market interest rates, we cannot control or accurately predict changes in the rates of interest or be sure our protective measures are adequate.

Transition away from the benchmark rate London Interbank Offered Rate to another benchmark rate could adversely affect operations.

In 2017, the United Kingdom's Financial Conduct Authority announced that after 2021 it would no longer compel banks to submit the rates required to calculate LIBOR. As a result, the continuation of LIBOR on the current basis cannot and will not be guaranteed after 2021. At this time, it is impossible to predict whether and to what extent banks will continue to provide submissions for the calculation of LIBOR. Similarly, it is impossible to predict whether LIBOR will continue to be viewed as an acceptable market benchmark, what rate or rates may become accepted alternatives to LIBOR, or what effects any such changes in views or alternatives may have on the markets for LIBOR-indexed financial instruments.

Regulators, industry groups, and others have, among other things, published recommended replacement language for LIBOR-linked financial instruments, identified recommended alternatives for certain LIBOR rates (e.g., the Secured Overnight Financing Rate), and proposed implementations of the recommended alternatives in floating rate instruments. There is not yet any consensus on what recommendations and proposals will be broadly accepted.

We have a significant number of loans, borrowings and other financial instruments with attributes that are either directly or indirectly dependent on LIBOR. The transition from LIBOR could create considerable costs and additional risk. Since proposed alternative rates are calculated differently, payments under contracts referencing new rates will differ from those referencing LIBOR. The transition will change our market risk profiles, requiring changes to risk and pricing models, valuation tools, product design and hedging strategies. Furthermore, failure to adequately manage this transition process with our customers could adversely impact our reputation. Although we are currently unable to assess what the ultimate impact of the transition from LIBOR will be, failure to adequately manage the transition could have a material adverse effect on our business, financial condition and results of operations.

Economic and other conditions may cause volatility in the price of our common stock.

In the current economic environment, the prices of publicly traded stocks in the financial services sector have been volatile. However, even in a more stable economic environment, the price of our common stock can be affected by a variety of factors, such as expected or actual results of operations, changes in analysts' recommendations or projections, announcements of developments related to our businesses, operating and stock performance of other companies deemed to be peers, news or expectations based on the performance of others in the financial services industry, and expected impacts of a changing regulatory environment. These factors not only impact the price of our common stock but could also affect the liquidity of the stock, given the Company's size, geographical footprint, and industry. The price for shares of our common stock may fluctuate significantly in the future, and these fluctuations may be unrelated to the Company's performance. General market price declines or market volatility in the future could adversely affect the price for shares of our common stock, and the current market price of such shares may not be indicative of future market prices.

The value of our goodwill and other intangible assets may decline in the future.

As of December 31, 2019, we had $501.22 million of goodwill and other intangible assets. A significant decline in our expected future cash flows, a significant adverse change in the business climate, slower growth rates, or a significant and sustained decline in the price of our common stock may necessitate taking charges in the future related to the impairment of our goodwill and other intangible assets. If we were to conclude that a future write-down of goodwill and other intangible assets is necessary, we would record the appropriate charge, which could have a material adverse effect on our financial condition and results of operations.

Loss of any of our key personnel could disrupt our operations and result in reduced revenues.

We are a relationship-driven organization. A key aspect of our business strategy is for our senior officers to have primary contact with our customers. Our growth and development to date have been, in large part, a result of these personalized relationships with our customer base. The success of our acquisitions also often depends on our ability to retain and integrate the senior officers of acquired businesses.

Our senior officers have considerable experience in the banking industry and related financial services and are extremely valuable and would be difficult to replace. The loss of the services of these officers could have a material adverse effect upon future prospects. Although we have entered into employment contracts with our Executive Chairman, Chief Executive Officer, and our other senior executive officers, and purchased key man life insurance policies to mitigate the risk of an unforeseen departure or death of certain of our senior executive officers, we cannot offer any assurance that they and other key employees will remain employed by us. The unexpected loss of services of one or more of these key employees could have a material adverse effect on operations and possibly result in reduced revenues.

Reliance on certain external vendors could adversely affect our operations.

We are reliant upon certain external vendors to provide products and services necessary to maintain our day-to-day operations. Accordingly, our operations are exposed to risk that these vendors will not perform in accordance with the contracted arrangements under service-level agreements. We maintain a system of comprehensive policies and a control framework designed to monitor vendor risks including, among other things, (i) changes in the vendor's financial condition, (ii) changes in the vendor's support for existing products and services, and (ii) changes in the vendor's strategic focus. While we believe these policies and procedures help to mitigate risk, the failure of an external vendor to perform in accordance with contracted arrangements under service-level agreements could be disruptive to our operations, which could have a material adverse impact on our business and, in turn, our financial condition and results of operations.

We may not be able to successfully implement our planned core system conversion, which could cause us to experience compliance and operational problems or lose customers, or incur additional expenditures beyond current projections, any one of which could adversely affect our financial results.

We are planning a system conversion for our core banking platform during the second quarter of 2020 with the goal of becoming more efficient and providing better products and services to our customers, thereby strengthening our controls and processes and improving overall results. Successfully implementing this conversion and achieving these goals will require communicating these changes to our customers in a positive fashion, and integrating our systems and operating procedures. If we are unable to successfully implement the core banking system conversion, we may lose customers, experience compliance and operational problems, or incur additional expenditures beyond current projections, any one of which could adversely affect our financial results.

We are subject to environmental liability risk associated with our lending activities.

A significant portion of our loan portfolio is secured by real property. During the ordinary course of business, we may foreclose on and take title to properties securing certain loans. In doing so, there is a risk that hazardous or toxic substances could be found on these properties. If hazardous or toxic substances are found, we may be liable for remediation costs, as well as for personal injury and property damage. Environmental laws may require us to incur substantial expenses and may materially reduce the affected property's value or limit our ability to use or sell the affected property. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability. Environmental reviews of real property before initiating foreclosure actions may not be sufficient to detect all potential environmental hazards.

Remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on our financial condition and results of operations.

Severe weather, natural disasters, sea level rise, acts of war or terrorism, and other external events could significantly impact our business.

Severe weather, natural disasters, sea level rise and other environmental risks, acts of war or terrorism, and other adverse external events could have a significant impact on our ability to conduct business. In addition, such events could affect the stability of our deposit base, impair the ability of borrowers to repay outstanding loans, impair the value of collateral securing loans, cause significant property damage, result in loss of revenue, and/or cause us to incur additional expenses. The occurrence of any such event in the future could have a material adverse effect on our business, which, in turn, could have a material adverse effect on our financial condition and results of operations.

The operational functions of business counterparties over which we may have limited or no control may experience disruptions that could adversely impact our operations.

Every year, retailers and service providers are the target of data systems incursions which result in the thefts of credit and debit card information, online account information, and other financial data of tens of millions of their customers and users. These incursions affect cards issued and deposit accounts maintained by many banks, including the Company. Although our systems are not breached in such incursions, these events can cause us to reissue a significant number of cards and take other costly steps to avoid significant theft loss to us and our customers. In some cases, we may be required to reimburse customers for the losses they incur. Other possible points of intrusion or disruption not within our control include internet service providers, electronic mail portal providers, social media portals, distant-server ("cloud") service providers, electronic data security providers, telecommunications companies, and smart phone manufacturers.

Security breaches and other disruptions could compromise our information and expose us to liability or result in the loss of money, which could damage our reputation and our business.

We rely on the secure processing, storage, and transmission of confidential and other information in our computer systems and networks. While we have policies and procedures designed to prevent or limit the effect of a possible security breach, our computer systems, software, and networks may be vulnerable to unauthorized access, computer viruses, or other malicious code, and other events that could have a security impact. If one or more such events occur, this potentially could jeopardize our or our customers' confidential and other information processed and stored in, and transmitted through, our computer systems and networks, or otherwise cause interruptions or malfunctions in our or our customers' operations, or result in the loss of money. We may be required to expend significant additional resources to modify our protective measures or to investigate and remediate vulnerabilities or other exposures, and we may be subject to litigation and financial losses that are either not insured against or not fully covered through any insurance maintained by us.

Security breaches in our internet banking activities could further expose us to possible liability, financial loss, and damage to our reputation. Any compromise of our security also could deter customers from using our internet banking services that involve the transmission of confidential information. We have implemented security systems to provide the security and authentication necessary to effect secure transmission of data. These precautions may not protect our systems from compromises or breaches of our security measures, which could result in damage to our reputation and our business.

Our risk-management framework may not be effective in mitigating risk and loss.

We maintain an enterprise risk management program that is designed to identify, quantify, monitor, report, and control the risks that we face. These risks include: strategic, reputational, credit, liquidity, interest rate, operational, compliance, pricing, legal and cybersecurity. While we assess and improve this program on an ongoing basis, there can be no assurance that our approach and framework for risk management and related controls will effectively mitigate all risk and limit losses in our business. If conditions or circumstances arise that expose flaws or gaps in our risk-management program, or if our controls break down, our results of operations and financial condition may be adversely affected.

Failure of our internal and disclosure controls and procedures could have a material adverse effect on our results of operations and financial condition.

Effective internal and disclosure controls and procedures are necessary to provide reliable financial reports and effectively prevent fraud and to operate successfully as a public company. Our management regularly reviews and updates our internal controls, disclosure controls and procedures, and corporate governance policies and procedures. Any system of controls, no matter how well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Any failure or circumvention of our controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on our results of operations and financial condition.

Negative perception of the Company through media may adversely affect our reputation and business.

The Company's reputation is critical to the success of its business. We believe that our brand image has been well received by customers, reflecting the fact that the brand image, like our business, is based in part on trust and confidence. Our reputation and brand image could be negatively affected by rapid and widespread distribution of publicity through social and traditional media channels. Our reputation could also be affected by our association with clients affected negatively through media distribution, or other third parties, or by circumstances outside of our control. Negative publicity, whether true or untrue, could affect our ability to attract or retain customers, or cause us to incur additional liabilities or costs, or result in additional regulatory scrutiny.

Restrictions relating to the acquisition of our common stock may discourage an acquisition.

Certain provisions of our articles of incorporation and bylaws could delay or frustrate the removal of incumbent directors and could make a merger, tender offer, or proxy contest more difficult, even in instances where shareholders deem the proposed transaction to be beneficial to their interests. These provisions, among others, provide for staggered terms for the Board of Directors and that a plan of merger, share exchange, sale of all or substantially all of our assets, or similar transaction must be approved and recommended by the affirmative vote of at least two-thirds of the directors in office or, if not so approved and recommended, by the affirmative vote of the holders of 80% of our outstanding shares, and limit the ability of shareholders to call a special meeting. In addition, certain provisions of state and federal law may also have the effect of discouraging or prohibiting a future takeover attempt in which our shareholders might otherwise receive a substantial premium for their shares over then-current market prices. To the extent that these provisions discourage or prevent takeover attempts, they may tend to reduce the market price for our common stock and the notes.

Liquidity could be impaired by an inability to access the capital markets or an unforeseen outflow of cash.

Liquidity is essential to our businesses. Due to circumstances that we may be unable to control, such as a general market disruption or an operational problem that affects third parties or the Company, our liquidity could be impaired by an inability to access the capital markets or an unforeseen outflow of cash or deposits which could constrain our ability to make new loans or meet our existing lending commitments and could ultimately jeopardize our overall liquidity and capitalization.

Our credit ratings are also important to our liquidity. These ratings are based on a number of factors, including our overall financial strength, as well as factors not entirely within our control, such as conditions affecting the financial services industry generally. As a result, there can be no assurance that we will maintain our current ratings. A reduction in our credit ratings could adversely affect our liquidity and competitive position, increase our borrowing costs or limit our access to the capital markets.

Continued growth may require raising additional capital, which may dilute current shareholders' ownership percentage.

In order to meet applicable regulatory capital requirements, we may, from time to time, need to raise additional capital to support continued growth. If we sell our equity securities to raise additional funds, the relative ownership interests of our existing shareholders would likely be diluted.

Risks associated with acquisitions and the resulting integrations may affect costs and revenue.

A component of our business strategy includes growth through acquisitions. Costs or difficulties related to integrating the acquired business with the Company might be greater than expected. Further, expected revenue and/or operational synergies and cost savings associated with pending or recently completed acquisitions may not be fully realized or realized within the expected time frame. We cannot provide assurance that we will be successful in overcoming these risks or any other issues encountered in connection with acquisitions.

Attractive acquisition or expansion opportunities may not be available to us in the future.

We may consider acquiring other businesses or expanding into new product lines or markets that we believe will help us fulfill our strategic objectives. We expect that other banking and financial companies, some of which have significantly greater resources, will compete with us to acquire financial services businesses. Our target base of attractive candidates may be limited and competition could increase prices for potential acquisitions that we believe are attractive. Acquisitions may also be subject to various regulatory approvals. If we fail to receive the appropriate regulatory approvals, we will not be able to consummate acquisitions that we believe are in our best interests.

Focus on commercial loans may increase the risk of substantial credit losses.

We offer a variety of loan products, including residential mortgage, consumer, construction, and commercial loans. At December 31, 2019, approximately 60.42% of loans were commercial and industrial loans, and commercial loans secured by commercial real estate. It is expected that, as we grow, this percentage will remain fairly constant.

Commercial lending generally involves more risk than mortgage and consumer lending because loan balances are greater, and the borrower's ability to repay is contingent on the successful operation of a business. Risk of loan defaults is unavoidable in the banking industry. We attempt to limit exposure to this risk by monitoring carefully the amount of loans in specific industries and by exercising prudent lending practices. However, the risk that substantial credit losses could result in reduced earnings or losses cannot be eliminated.

The Company's focus on lending to small to mid-sized community-based businesses may increase its credit risk.

Most of our commercial business and commercial real estate loans are made to small business or middle-market customers. These businesses generally have fewer financial resources in terms of capital or borrowing capacity than larger entities and have a heightened vulnerability to economic conditions. Additionally, these loans may increase concentration risk as to industry or collateral securing our loans. If general economic conditions in the market areas in which we operate negatively impact this important customer sector, our results of operations and financial condition may be adversely affected. Moreover, a portion of these loans have been made by the Company recently, and the borrowers may not have experienced a complete business or economic cycle. The deterioration of the borrowers' businesses may hinder their ability to repay their loans with the Company, which could have a material adverse effect on our financial condition and results of operations.

Our allowance for loan losses may prove to be insufficient to absorb potential losses in the loan portfolio.

We maintain an allowance for loan losses that we believe is adequate to provide for any potential losses in our loan portfolio. Our management determines the amount of this allowance through a periodic review and consideration of several factors, including:

- an ongoing review of the quality, size, and diversity of the loan portfolio;
- an evaluation of present economic, political, and regulatory conditions;
- an evaluation of performing and nonperforming loans;
- our historical loan loss experience; and
- the amount and quality of collateral, including guarantees securing the loans.

Although we believe our loan loss allowance is adequate to absorb probable losses in the loan portfolio, we cannot predict such losses or that our allowance will be adequate. The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material changes. Deterioration in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans, and other factors, both within and outside the Company's control, may require an increase in the allowance for loan losses.

The adoption of ASU 2016-13, as amended, on January 1, 2020 could result in an increase in the allowance for loan losses as a result of changing from an "incurred loss" model, which encompasses allowances for current known and inherent losses within the portfolio, to an "expected loss" model, which encompasses allowances for losses expected to be incurred over the life of the portfolio. Furthermore, ASU 2016-13 will necessitate that we establish an allowance for expected credit losses for certain debt securities and other financial assets. We expect our allowance to increase up to 10% upon full adoption of this ASU, due to the change mentioned previously, significantly influenced by the composition, characteristics and quality of our loan and securities portfolios as well as the prevailing economic conditions and forecasts as of the adoption date. In December 2018, the federal banking regulators issued a final rule that would provide an optional three-year phase-in period for the day-one regulatory capital effects of the adoption of ASU 2016-13. See "Recent accounting pronouncements" contained in Note 1 of the Consolidated Financial Statements for additional information.

Our credit standards and ongoing credit assessment processes might not protect us from significant credit losses.

We take credit risk by virtue of making loans and leases and extending loan commitments and letters of credit. We manage credit risk through a program of underwriting standards, the review of certain credit decisions, and an ongoing process of assessment of the quality of the credit already extended. Our exposure to credit risk is managed through the use of consistent underwriting standards that emphasize local lending while avoiding highly leveraged transactions as well as excessive industry and other concentrations. Our credit administration function employs risk management techniques to help ensure that problem loans and leases are promptly identified. While these procedures are designed to provide us with the information needed to implement policy adjustments where necessary and to take appropriate corrective actions, there can be no assurance that such measures will be effective in avoiding undue credit risk.

We rely upon independent appraisals to determine the value of real estate that secures a significant portion of our loans, and the values indicated by such appraisals may not be realizable if we are forced to foreclose upon such loans.

A significant portion of our loan portfolio consists of loans secured by real estate. We rely upon independent appraisers to estimate the value of such real estate. Appraisals are only estimates of value, and the independent appraisers may make mistakes of fact or judgment that adversely affect the reliability of their appraisals. In addition, events occurring after the initial appraisal may cause the value of the real estate to increase or decrease. As a result of any of these factors, the real estate securing some of our loans may be more or less valuable than anticipated at the time the loans were made. If a default occurs on a loan secured by real estate that is less valuable than originally estimated, we may not be able recover the outstanding balance of the loan.

We depend on the accuracy and completeness of information about clients and counterparties, and our financial condition could be adversely affected if we rely on misleading information.

In deciding whether to extend credit or to enter into other transactions with clients and counterparties, we may rely on information furnished to us by or on behalf of clients and counterparties, including financial statements and other financial information, which the Company does not independently verify. We also may rely on representations of clients and counterparties as to the accuracy and completeness of that information and, with respect to financial statements, on reports of independent auditors. For example, in deciding whether to extend credit to clients, we may assume that a customer's audited financial statements conform with accounting principles generally accepted in the United States and present fairly, in all material respects, the financial condition, results of operations, and cash flows of the customer. Our financial condition and results of operations could be negatively impacted to the extent we rely on financial statements that do not comply with GAAP or are materially misleading.

Our quarterly financial results may fluctuate as a result of seasonality, which may make it difficult to predict our future performance and may adversely affect our common stock price.

We engage in certain lines of business that are historically subject to seasonal trends. These include mortgage banking and real estate brokerage services that reflect the general patterns of housing sales, which typically peak in the spring and summer seasons. Our non-mortgage and real estate related businesses have various seasonality trends that may create further fluctuations in our quarterly operating results. Any of these seasonal trends, or the combination of them, may negatively impact the price of our common stock.

Our mortgage revenue is cyclical and sensitive to the level of interest rates, changes in economic conditions, decreased economic activity, and slowdowns in the housing market, any of which could adversely impact our profits.

The success of our mortgage business is dependent upon our ability to originate loans and sell them to investors at or near current volumes. Loan production levels are sensitive to changes in the level of interest rates, product availability, and changes in economic conditions. Loan production levels may suffer if we experience a slowdown in the housing markets in the regions in which we do business, or tightening credit conditions. Any sustained period of decreased activity caused by fewer home sales or refinancing transactions, higher interest rates, housing price pressure, or loan underwriting restrictions would adversely affect our mortgage originations and, consequently, could significantly reduce our income from mortgage activities. As a result, these conditions would also adversely affect our results of operations.

We may be required to repurchase residential mortgage loans or reimburse investors and others as a result of breaches in contractual representations and warranties.

We sell residential mortgage loans to various parties, which may include government sponsored entities and other bank and non-bank financial institutions that purchase residential mortgage loans for investment or private label securitization. We may be required to repurchase residential mortgage loans, indemnify the securitization trust, investor or insurer, or reimburse the securitization trust, investor or insurer for credit losses incurred on loans in the event of a breach of contractual representations or warranties that is not remedied within a specified period (usually 60 days or less) after we receive notice of the breach. Contracts for residential mortgage loan sales to these entities include various types of specific remedies and penalties that could be applied to inadequate responses to repurchase requests. If economic conditions and the housing market deteriorate or future investor repurchase demand and our success at appealing repurchase requests differ from past experience, we could have increased repurchase obligations and increased loss severity on repurchases, that could adversely affect operations.

Strong competition in our primary market area and from non-traditional financial institutions may limit asset growth and profitability.

We encounter strong competition from other financial institutions in our primary market area. In addition, established financial institutions not already operating in our primary market area may open branches at future dates. In the conduct of certain aspects of our business, we also compete with savings institutions, credit unions, mortgage banking companies, consumer finance companies, insurance companies, real estate companies, and other institutions, some of which are not subject to the same degree of regulation or restrictions as are imposed upon us. Also, technology and other changes have lowered barriers to entry and made it possible for non-banks to offer products and services traditionally provided by banks. In particular, the activity of financial technology ("fintech") companies has grown significantly over recent years and is expected to continue to grow. Fintech companies have and may continue to offer bank or bank-like products and a some fintech companies have applied for bank charters. In addition, other fintech companies have partnered with existing banks to allow them to offer deposit products to their customers. Many of these competitors have substantially greater resources and lending limits than we have and offer services that we do not provide. In addition, many of these competitors have numerous branch offices located throughout their extended market areas that provide them with a competitive advantage. Finally, these institutions may have differing pricing and underwriting standards, which may adversely affect our company through the loss of business or causing a misalignment in our risk-return relationship. No assurance can be given that such competition will not have an adverse impact on the financial condition and results of operations.

Legislative reforms, such as the Dodd-Frank Act, can result in our business becoming subject to significant and extensive additional regulations, which could adversely affect our results of operations and financial condition.

The Dodd-Frank Act may continue to result in significant changes in the regulation of financial institutions. As disclosed earlier in this Form 10-K, the act contains numerous provisions that affect all banks and bank holding companies. Some of these provisions under the Dodd-Frank Act have the consequence of increasing our expenses, decreasing our revenues, and changing the activities in which we choose to engage. Other legislative and regulatory changes affecting capital, liquidity, taxes, supervision, permissible activities, corporate governance and compensation, fiscal policy, and steps to eliminate government support for banking organizations may have long-term effects on the business model and profitability of banking organizations that cannot now be foreseen. The specific impact of the Dodd-Frank Act on our current activities or new financial activities we may consider in the future, our financial performance, and the markets in which we operate will depend on the manner in which the relevant agencies develop and implement required rules and the reaction of market participants to these regulatory developments.

Increased capital standards may have an adverse effect on our profitability, lending, and ability to pay dividends on our securities.

In July 2013, the FDIC released its interim final rules that implement in the United States the Basel III regulatory capital reforms from the Basel Committee and certain changes required by the Dodd-Frank Act. Under the Basel III Capital Rules, minimum requirements have increased for both the quality and quantity of capital held by banking organizations. The rules became effective January 1, 2015 and were fully phased in on January 1, 2019. The potential impact of the Basel III Capital Rules includes, but is not limited to, reduced lending and negative pressure on profitability and return on equity due to higher capital requirements. To the extent the Company is required to increase capital in the future to comply with the Basel III Capital Rules, our ability to pay dividends may be reduced.

In December 2017, the Basel Committee published standards that it described as the finalization of the Basel III post-crisis regulatory reforms (the standards are commonly referred to as “Basel IV”). Among other things, these standards revise the Basel Committee’s standardized approach for credit risk (including by recalibrating risk weights and introducing new capital requirements for certain “unconditionally cancellable commitments,” such as unused credit card lines of credit) and provides a new standardized approach for operational risk capital. Under the Basel framework, these standards will generally be effective on January 1, 2022, with an aggregate output floor phasing in through January 1, 2027. Under the current U.S. capital rules, operational risk capital requirements and a capital floor apply only to advanced approaches institutions, and not to the Company. The impact of Basel IV on us will depend on the manner in which it is implemented by the federal bank regulatory agencies.

Regulations issued by the Consumer Financial Protection Bureau could adversely affect our earnings.

The CFPB has broad rule-making authority to administer and carry out the provisions of the Dodd-Frank Act with respect to financial institutions that offer covered financial products and services to consumers. Pursuant to the Dodd-Frank Act, the CFPB has established a rule effective January 10, 2014, requiring mortgage lenders to make a reasonable and good-faith determination based on verified and documented information that a consumer applying for a mortgage loan has a reasonable ability to repay the loan according to its terms, or to originate “qualified mortgages” that meet specific requirements with respect to terms, pricing, and fees. The rule also contains disclosure requirements at mortgage loan origination and in monthly statements. These requirements could limit our ability to make certain types of loans or loans to certain borrowers, or could make it more expensive and/or time-consuming to make these loans, which could adversely impact our profitability

Extensive government regulation and monetary policy could adversely affect operations.

As part of the financial services industry, we are subject to extensive governmental supervision, regulation, and control that have materially affected the business of financial institutions in the past and are likely to do so in the future. Regulations affecting the financial services industry and, therefore, us may be changed at any time, and the interpretation of those regulations by examining authorities of the financial services industry is also subject to change. There can be no assurance that future changes in legislation, administrative regulations, or governmental policy will not adversely affect the financial services industry and our business.

We are subject to additional regulatory scrutiny because our total assets exceed $10 billion.

As of December 31, 2019, we had $11.95 billion in total consolidated assets. The Dodd-Frank Act and its implementing regulations impose various additional requirements on banks with $10 billion or more in total assets, including examination by the CFPB with respect to various federal consumer financial protection laws and regulations. Until 2018, we were subject to regulations adopted by the CFPB, but the FDIC was primarily responsible for examining our compliance with consumer protection laws and those CFPB regulations.

In addition, because our assets exceed $10 billion, we are subject to the Durbin Amendment promulgated under the Dodd-Frank Act. Under the Durbin Amendment, the maximum permissible interchange fee for an electronic debit transaction is the sum of 21 cents per transaction and five basis points multiplied by the value of the transaction. The rules also allow for an upward adjustment of no more than one cent to an issuer's debit card interchange fee if the issuer develops and implements policies and procedures reasonably designed to achieve certain fraud-prevention standards. This limitation on interchange fees will adversely impact our results of operations.

Compliance with these and other requirements may necessitate that we hire additional compliance or other personnel, design and implement additional internal controls, or incur other significant expenses, any of which could have a material adverse effect on our business, financial condition or results of operations.

Changes in the federal, state or local tax laws may negatively impact our financial performance.

Changes in tax law could increase our effective tax rates. Such changes may be retroactive to previous periods and as a result could negatively affect our current and future financial performance. Similarly, our customers are likely to experience varying effects from both the individual and business tax provisions of new tax laws and such effects, whether positive or negative, may have a corresponding impact on our business and the economy as a whole.

Potential downgrades of U.S. government securities by one or more of the credit ratings agencies could have a material adverse effect on our operations, earnings and financial condition.

A possible future downgrade of the sovereign credit ratings of the U.S. government and/or a decline in the perceived creditworthiness of U.S. government-related obligations could impact our ability to obtain funding that is collateralized by affected instruments, as well as affect the pricing of that funding when it is available. A downgrade may also adversely affect the market value of such instruments. We cannot predict if, when or how any changes to the credit ratings or perceived creditworthiness of these obligations will affect economic conditions. A downgrade of the sovereign credit ratings of the U.S. government or the credit ratings of related institutions, agencies or instruments could have a material adverse effect our business, financial condition and results of operations.

Loss of deposits or a change in deposit mix could increase our funding costs.

Deposits are a low cost and stable source of funding. We compete with banks and other financial institutions for deposits. Funding costs may increase because we may lose deposits and replace them with more expensive sources of funding, clients may shift their deposits into higher cost products or we may need to raise interest rates to avoid losing deposits. Higher funding costs reduce our net interest margin, net interest income and net income.

There are risks resulting from the use of models in our business.

We rely on quantitative models to measure risks and to estimate certain financial values. Models may be used in such processes as determining the pricing of various products, grading loans and extending credit, measuring interest rate and other market risks, predicting or estimating losses, assessing capital adequacy and calculating economic and regulatory capital levels, as well as to estimate the value of financial instruments and balance sheet items. Poorly designed or implemented models present the risk that our business decisions based on information incorporating model output would be adversely affected due to the inadequacy of that information. Also, information we provide to the public or to our regulators based on poorly designed or implemented models could be inaccurate or misleading.

Item 1B. UNRESOLVED STAFF COMMENTS

None.

Item 2. PROPERTIES

Our bank's main office is located in Portsmouth, Virginia, and our Corporate Administration and Member Service Center is located in Suffolk, Virginia; we own both of these locations. As of December 31, 2019, we occupied an additional 146 properties, of which we own 43, in the cities and counties in which we operate. We consider our properties to be suitable and adequate for our present needs. Additional information with respect to the amounts at which company premises and equipment are carried and commitments under long-term leases is set forth in Note 6 - Premises, Equipment, and Leases and Note 7 - Leases in the Annual Report and incorporated herein.

Item 3. LEGAL PROCEEDINGS

In the ordinary course of operations, we are a party to various legal proceedings. Based upon information currently available, management believes that such legal proceedings, in the aggregate, will not have a material adverse effect on our business, financial condition, or results of operations.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

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

Market Information

Our common stock is listed on the Nasdaq Global Select Market under the symbol TOWN.

Holders

As of December 31, 2019, we had issued and outstanding 72,649,682 shares of common stock. These shares were held by approximately 12,038 shareholders of record.

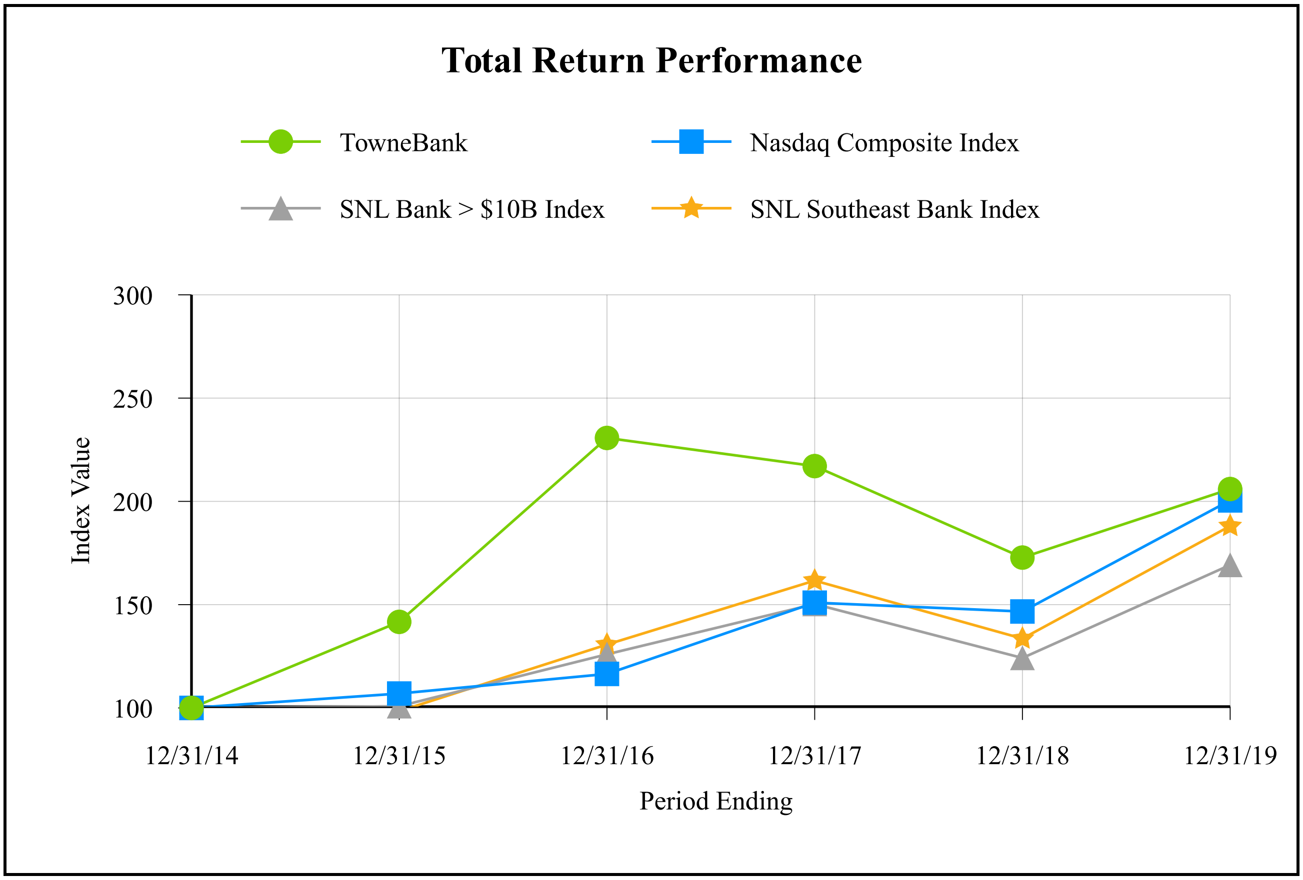
Dividends

In the first quarter of 2019, we declared a quarterly cash dividend of $0.16 per common share. Beginning in the second quarter of 2019 through the first quarter of 2020, we declared cash dividends of $0.18 per common share. In the first quarter of 2018, the Company declared a quarterly cash dividend of $0.14 per common share. In May, August, and November 2018, the Company declared quarterly cash dividends of $0.16 per common share. All dividends paid are limited by the requirement to meet capital guidelines issued by regulatory authorities, and future declarations are subject to financial performance and regulatory guidelines.

Our future dividend policy is subject to the discretion of the Board of Directors and will depend upon a number of factors, including future earnings, financial condition, cash requirements, and general business conditions. We are also subject to certain restrictions imposed by the reserve and capital requirements of federal and Virginia banking statutes and regulations. See "Part I, Item 1. Business - Supervision and Regulation," for information on regulatory restrictions on dividends.

Stock Performance Graph

The following stock performance graph presents the cumulative total return comparison through December 31, 2019, of stock appreciation for our common stock, the Nasdaq Composite Index measuring all Nasdaq domestic and international-based common type stocks listed on the Nasdaq Stock Market ("Nasdaq Composite"), the SNL Securities Index including banks greater than $10 billion in total assets ("SNL Bank > $10B Index"), and the SNL Securities Index including only banks in the Southeast ("SNL Southeast Bank Index"). Returns assume an initial investment of $100 at the market close of December 31, 2014, and reinvestment of dividends.



Index	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018	12/31/2019
TowneBank	$ 100.00	$ 141.67	$ 230.71	$ 217.08	$ 172.79	$ 205.98
Nasdaq Composite Index	100.00	106.96	116.45	150.96	146.67	200.49
SNL Bank > $10B Index	100.00	100.83	125.96	150.29	124.18	169.22
SNL Southeast Bank Index	100.00	98.44	130.68	161.65	133.56	188.08

Item 6. SELECTED FINANCIAL DATA

Reference is made to the information in the section entitled, "Selected Financial Highlights," of our Annual Report for the year ended December 31, 2019, which is incorporated herein by reference.

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

Reference is made to the information in the section entitled, "Management's Discussion and Analysis," of our Annual Report, which is incorporated herein by reference.

Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Reference is made to the information in the section entitled, "Management's Discussion and Analysis," under subsections "Interest Sensitivity," "Market Risk Management," "Earnings Simulation Analysis," "Market Value Simulation," and "Credit Risk Elements," of our Annual Report, which is incorporated herein by reference.

Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Reference is made to the information in the sections entitled, "Management's Report on Internal Control," "Report of Independent Registered Public Accounting Firm," and "Consolidated Financial Statements and Notes," of our Annual Report, which is incorporated herein by reference.

Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES

None.

Item 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures. An evaluation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) was carried out as of December 31, 2019, under the supervision and with the participation of our Chief Executive Officer, Chief Financial Officer, and several other members of our senior management. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective as of the end of the period covered by this report.

Management's Report on Internal Control Over Financial Reporting. The annual report of management on the effectiveness of our internal control over financial reporting and the attestation report thereon issued by our independent registered public accounting firm are set forth under "Management's Report on Internal Control" and "Report of Independent Registered Public Accounting Firm" of our Annual Report, which is incorporated herein by reference.

Changes in Internal Control Over Financial Reporting. There were no changes in our internal controls over financial reporting that occurred during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. OTHER INFORMATION

None.

PART III

Item 10. DIRECTORS, EXECUTIVE OFFICERS, AND CORPORATE GOVERNANCE

Reference is made to the information in the sections entitled, “Election of Directors,” “Section 16(a) Beneficial Ownership Reporting Compliance,” and “Board of Directors and Committees: *Audit Committee,”* of our definitive Proxy Statement for the Annual Meeting of Stockholders to be held May 20, 2020 (“2020 Proxy Statement”), which sections are incorporated herein by reference. The following information is provided, as of February 28, 2020, for those executive officers who are not directors.

Name (Age)	Principal Occupation During Past Five Years
Matt Davis (52)	Chief Strategy and Risk Officer since September 2019; President, NC Region of TowneBank from February 2019 to August 2019; Chief Operating Officer Paragon Bank from December 2012 to January 2019; Chief Credit Officer Paragon Bank from June 2002 to November 2012.
Kevin L. Fly (54)	Senior Executive Vice President and Chief Accounting Officer since May 2018; Executive Vice President - Financial Reporting, Tax, and Policy from June 2013 to May 2018; Senior Vice President and Director of Financial Reporting from December 2007 to June 2013.
Dawn Glynn (52)	President, Retail and Private Banking since January 2019; President and Regional Executive Officer for Portsmouth/ Chesapeake/Suffolk from 2016 to 2018; President for Portsmouth/Chesapeake/Suffolk from 2013 to 2016; President for Chesapeake from 2010 to 2013.
William B. Littreal (49)	Senior Executive Vice President and Chief Financial Officer since March 2018; Senior Executive Vice President and Chief Strategy Officer and Director of Investor Relations since June 2016; Senior Executive Vice President and Chief Operating Officer from April 2011 to June 2016; Executive Vice President and Director of Finance from April 2008 to April 2011.
Brian Skinner (49)	Chief Banking Officer since January 2019; Regional Executive Officer of Peninsula/Williamsburg from 2007 to 2018.
George P. Whitley (67)	Senior Executive Vice President and Chief Legal Officer since October 2016; Partner, LeClairRyan, Richmond, Virginia, from May 1994 to September 2016.

Code of Ethical Conduct

We have adopted a Code of Ethical Conduct that applies to our Chief Executive Officer and other executive and senior financial officers, including our Chief Financial Officer, Chief Accounting Officer, Corporate Treasurer, Internal Audit members, any person Assistant Vice President and above in an Accounting/Financial position, Senior Financial Analyst, any Regulation O executive officers along with any person serving in an equivalent position regardless of whether or not they are designated as executive officers for Regulation O purposes, or any persons serving in equivalent positions within the Company. The Code of Ethical Conduct is included as Exhibit 14. Any changes in or waivers from our Code of Ethical Conduct applicable to the Chief Executive Officer and any other executive or senior financial officer shall be promptly disclosed through a filing with the FDIC on Form 8-K.

Part III

A written copy of our Code of Ethical Conduct is available free of charge to stockholders who request it by writing to: TowneBank, 6001 Harbour View Boulevard, Suffolk, Virginia 23435. We also provide this information on our website, www.townebank.com, under Investor Relations, Governance Documents, Code of Conduct.

Item 11. EXECUTIVE COMPENSATION

The information required by this item is incorporated herein by reference to our 2020 Proxy Statement to be filed with the FDIC within 120 days of the end of our fiscal year.

Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information concerning security ownership of certain beneficial owners and management required by this item is incorporated herein by reference to our 2020 Proxy Statement to be filed with the FDIC within 120 days of the end of our fiscal year.

The following table summarizes information, as of December 31, 2019, relating to our stock incentive plans, pursuant to which grants of options to acquire shares of common stock may be awarded from time to time.

	Number of securities to be issued upon exercise of outstanding options, warrants, and rights	Weighted average exercise price of outstanding options, warrants, and rights	Number of securities remaining available for future issuance under equity compensation plans (1)
	(A)	(B)	(C)
Equity compensation plans approved by security holders	11,197	$14.59	1,951,375
Equity compensation plans not approved by security holders	—	—	—
Total	11,197	$14.59	1,951,375

(1) Consists of shares available for future issuance under TowneBank's equity compensation plans.

Item 13. CERTAIN RELATIONSHIPS, RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Reference is made to the information in the sections entitled, "Related Party Transactions," "Election of Directors," and "Board of Directors and Committees," of the 2020 Proxy Statement, which sections are incorporated herein by reference.

Item 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

Reference is made to the information in the section entitled, "Accounting Firm Fees," of the 2020 Proxy Statement, which section is incorporated herein by reference.

PART IV

Item 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

a) The following documents are filed as part of this report.

(1) Financial Statements

The following documents are included in the 2019 Annual Report to Shareholders and are incorporated by reference in this report:

Report of Independent Registered Public Accounting Firm
Management's Report on Internal Control
Consolidated Balance Sheets
Consolidated Statements of Income
Consolidated Statements of Comprehensive Income
Consolidated Statements of Equity
Consolidated Statements of Cash Flows
Notes to Consolidated Financial Statements

(2) Financial Statement Schedules

All financial statement schedules as required by Item 8 and Item 15 of Form 10-K have been omitted because the information requested is not required, not applicable, or is shown in the Consolidated Financial Statements or Notes thereto.

(3) Exhibits

The following exhibits are filed as part of this Form 10-K and this list includes the Exhibit Index.

Exhibit No.	Description
1.1	Purchase Agreement, dated July 12, 2017, by and between TowneBank and Sandler O'Neill + Partners, L.P. (incorporated herein by reference to Exhibit 1.1 to our Form 8-K, previously filed with the FDIC on July 14, 2017).
2.1	Agreement and Plan of Reorganization, dated April 26, 2017, by and among TowneBank, TB Acquisition, LLC, Paragon Commercial Corporation and Paragon Commercial Bank (incorporated herein by reference to Exhibit 2.1 to our Form 8-K, previously filed with the FDIC on May 2, 2017).
3.1	Articles of Incorporation, as amended (incorporated herein by reference to Exhibit 3.1 to our Form 10-Q, previously filed with the FDIC on August 6, 2014).
3.2	Articles of Amendment to the Articles of Incorporation (incorporated herein by reference to Exhibit 3.1 to our Form 8-K, previously filed with the FDIC on December 14, 2018).
3.3	Bylaws, as amended (incorporated herein by reference to Exhibit 3.2 to our Form 8-K, previously filed with the FDIC on January 31, 2018).

PART IV

Exhibits continued

4.1	Form of Global 4.50% Subordinated Note due 2027 (incorporated herein by reference to Exhibit 4.1 to our Form 8-K, previously filed with the FDIC on July 17, 2017).
4.2	Description of TowneBank's Securities
10.1	Employment Agreement, dated October 1, 2005, between TowneBank and Jacqueline B. Amato (incorporated herein by reference to Exhibit 10 to our Form 8-K, previously filed with the FDIC on February 15, 2006).
10.2	Form of Employment Agreement entered into between TowneBank and each of G. Robert Aston, Jr., J. Morgan Davis, and Philip M. Rudisill (incorporated herein by reference to Exhibit 10.5 to our 2002 Form 10-K, previously filed with the FDIC on March 26, 2003).
10.3	Form of Employment Agreement entered into between TowneBank and each of William I. Foster, III, Thomas L. Hasty, III, and Keith D. Horton, (incorporated herein by reference to Exhibit 10.4 to our 2002 Form 10-K, previously filed with the FDIC on March 26, 2003).
10.4	Form of Change in Control Agreement entered into between TowneBank and each of G. Robert Aston, Jr., J. Morgan Davis, and Philip M. Rudisill (incorporated herein by reference to Exhibit 10.4 to our 2003 Form 10-K, previously filed with the FDIC on February 25, 2004).
10.5	First Amendment to the Amended and Restated Change in Control Employment Agreement, dated May 15, 2019, between TowneBank and G. Robert Aston, Jr. (incorporated herein by reference to Exhibit 10.1 to our Form 8-K, previously filed with the FDIC on May 15, 2019).
10.6	First Amendment to the Amended and Restated Change in Control Employment Agreement, dated May 15, 2019, between TowneBank and J. Morgan Davis (incorporated herein by reference to Exhibit 10.2 to our Form 8-K, previously filed with the FDIC on May 15, 2019).
10.7	Form of Change in Control Agreement entered into between TowneBank and each of William I. Foster, III, Thomas L. Hasty, III, and Keith D. Horton (incorporated herein by reference to Exhibit 10.5 to our 2004 Form 10-K, previously filed with the FDIC on February 23, 2005).
10.8	Amended and Restated Employment Agreement, dated November 27, 2019, between TowneBank and William B. Littreal (incorporated herein by reference to Exhibit 10.1 to our Form 8-K, previously filed with the FDIC on November 27, 2019).
10.9	Change in Control Employment Agreement, dated November 27, 2019, by and between TowneBank and William B. Littreal (incorporated herein by reference to Exhibit 10.2 to our Form 10-Q, previously filed with the FDIC on November 27, 2019).
10.10	Form of Supplemental Executive Retirement Plan (incorporated herein by reference to Exhibit 10.7 to our 2008 Form 10-K, previously filed with the FDIC on March 13, 2009).
10.11	TowneBank 2008 Stock Incentive Plan (incorporated herein by reference to Exhibit 10.8 to our 2008 Form 10-K, previously filed with the FDIC on March 13, 2009).

Part IV

Exhibits continued

10.12	TowneBank 2017 Stock Incentive Plan (incorporated herein by reference to Appendix A to the Proxy Statement for the 2017 Annual Meeting of Stockholders on Schedule 14A, previously filed with the FDIC on April 21, 2017).
10.13	TowneBank Annual Incentive Compensation Plan (incorporated herein by reference to Appendix B to the Proxy Statement for the 2017 Annual Meeting of Stockholders on Schedule 14A, previously filed with the FDIC on April 21, 2017).
10.14	Amended and Restated Split Dollar Life Insurance Agreement, dated as of August 24, 2016, entered into between TowneBank and the trustees of two separate irrevocable life insurance trusts established by G. Robert Aston, Jr., for the benefit of certain family members (incorporated herein by reference to Exhibit 10.1 to our Form 8-K, previously filed with the FDIC on August 30, 2016).
10.15	Transition and Consulting Agreement, dated as of November 9, 2016, entered into between TowneBank and Jacqueline B. Amato (incorporated herein by reference to Exhibit 10.1 to our Form 8-K, previously filed with the FDIC on November 15, 2016).
10.16	Employment Agreement, dated December 16, 2015, by and between TowneBank and Brad E. Schwartz (incorporated herein by reference to Exhibit 10.1 to our Form 10-Q, previously filed with the FDIC on August 9, 2016).
10.17	Employment Agreement, dated December 16, 2015, by and between TowneBank and William T. Morrison (incorporated herein by reference to Exhibit 10.3 to our Form 10-Q, previously filed with the FDIC on August 9, 2016).
10.18	Change in Control Employment Agreement, dated December 16, 2015, by and between TowneBank and Brad E. Schwartz (incorporated herein by reference to Exhibit 10.4 to our Form 10-Q, previously filed with the FDIC on August 9, 2016).
10.19	Change in Control Employment Agreement, dated December 16, 2015, by and between TowneBank and William T. Morrison (incorporated herein by reference to Exhibit 10.6 to our Form 10-Q, previously filed with the FDIC on August 9, 2016).
10.20	Retirement Agreement, dated February 5, 2018, by and between TowneBank and Clyde E. McFarland, Jr. (incorporated herein by reference to Exhibit 10.1 to our Form 8-K, previously filed with the FDIC on February 9, 2018).
10.21	Consulting Agreement, dated February 5, 2018, by and between TowneBank and Clyde E. McFarland, Jr. (incorporated herein by reference to Exhibit 10.2 to our Form 8-K, previously filed with the FDIC on February 9, 2018).
10.22	Employment and Consulting Agreement, dated April 26, 2017, by and between TowneBank and Robert C. Hatley (incorporated herein by reference to Exhibit 10.21 to our Form 10-K, previously filed with the FDIC on March 1, 2018).
13	2019 Annual Report to Shareholders.
14	Code of Ethical Conduct.
21	Subsidiaries of TowneBank.

PART IV

Exhibits continued

31.1	CEO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	CFO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	Certification Pursuant to 18 U.S.C. Section 1350, as adopted by Section 906 of the Sarbanes-Oxley Act of 2002.

b) See (a)(3) above for all exhibits filed herewith and the Exhibit Index.

c) All schedules are omitted as the required information is not applicable or the information is presented in the Consolidated Financial Statements or related Notes.

Item 16. FORM 10-K SUMMARY

Not applicable.

SIGNATURES

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

TOWNEBANK

Registrant

February 28, 2020	/s/ J. Morgan Davis
Date	By: J. Morgan Davis President/Chief Executive Officer

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 registrant and in the capacities indicated on February 28, 2020:

SIGNATURES

/s/ Jacqueline B. Amato Jacqueline B. Amato	Director
/s/ G. Robert Aston, Jr. G. Robert Aston, Jr.	Executive Chairman of the Board, Director
/s/ E. Lee Baynor E. Lee Baynor	Director
/s/ Jeffrey F. Benson Jeffrey F. Benson	Vice Chairman of the Board, Director
/s/ Richard S. Bray Richard S. Bray	Lead Director
Thomas C. Broyles	Director

SIGNATURES

Bradford L. Cherry	Director
/s/ J. Morgan Davis J. Morgan Davis	President and Chief Executive Officer, Director (principal executive officer)
/s/ Douglas D. Ellis Douglas D. Ellis	Director
/s/ John W. Failes John W. Failes	Vice Chairman of the Board, Director
/s/ Andrew S. Fine Andrew S. Fine	Director
/s/ Kevin L. Fly Kevin L. Fly	Senior Executive Vice President and Chief Accounting Officer (principal accounting officer)
/s/ William I. Foster, III William I. Foster, III	President, Commercial and Real Estate Banking, Director
/s/ Robert C. Hatley Robert C. Hatley	Director
/s/ Howard Jung Howard J. Jung	Director

SIGNATURES

/s/ John R. Lawson, II John R. Lawson, II	Director
/s/ Harry T. Lester Harry T. Lester	Director
/s/ William B. Littreal William B. Littreal	Senior Executive Vice President and Chief Financial Officer (principal financial officer)
/s/ W. Ashton Lewis W. Ashton Lewis	Director
/s/ Stephanie J. Marioneaux Stephanie J. Marioneaux	Director
/s/ Juan M. Montero, II Juan M. Montero, II	Director
/s/ R. Scott Morgan R. Scott Morgan	Director
/s/ William T. Morrison William T. Morrison	Chairman and Chief Executive Officer of TowneBank Mortgage and Realty Group, Director
Thomas K. Norment, Jr.	Director
/s/ Robert M. Oman Robert M. Oman	Director

SIGNATURES

/s/ R.V. Owens, III R.V. Owens, III	Director
/s/ Elizabeth T. Patterson Elizabeth T. Patterson	Director
/s/ Elizabeth W. Robertson Elizabeth W. Robertson	Director
/s/ Dwight C. Schaubach Dwight C. Schaubach	Director
/s/ Brad E. Schwartz Brad E. Schwartz	Senior Executive Vice President and Chief Operating Officer, Director
/s/ Richard B. Thurmond Richard B. Thurmond	Director
/s/ Richard T. Wheeler, Jr. Richard T. Wheeler, Jr.	Director
/s/ Alan S. Witt Alan S. Witt	Director
/s/ F. Lewis Wood F. Lewis Wood	Director

Exhibit 4.2

DESCRIPTION OF TOWNEBANK'S SECURITIES

As of December 31, 2019, TowneBank's common stock was the only class of its securities registered under Section 12 of the Securities Exchange Act of 1934. The common stock is registered with the Federal Deposit Insurance Corporation. The following summary description of the material features of TowneBank's common stock is qualified in its entirety by reference to TowneBank's articles of incorporation and bylaws, each as amended. For more information, refer to TowneBank's articles of incorporation and bylaws and any applicable provisions of relevant law, including the Virginia Stock Corporation Act (the "Virginia SCA") and federal laws governing banks.

General

TowneBank is authorized to issue 150,000,000 shares of common stock, par value $1.667 per share. Each share of TowneBank's common stock has the same relative rights as, and is identical in all respects to, each other share of its common stock. TowneBank's common stock is traded on the Nasdaq Global Select Market under the symbol "TOWN." The transfer agent for TowneBank's common stock is Computershare, Inc., 250 Royall Street, Canton, Massachusetts 02021. TowneBank's common stock is not a deposit or a savings account and is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

Dividends

TowneBank's stockholders are entitled to receive dividends or distributions that its board of directors may declare out of funds legally available for those payments. The payment of distributions by TowneBank is subject to the restrictions of Virginia law applicable to the declaration of distributions by a Virginia banking corporation. Under Virginia law, TowneBank's board of directors may declare a dividend out of the net undivided profits of the bank, after providing for all expenses, losses, interest and taxes accrued or due. No dividend may be declared or paid by TowneBank that would impair its paid-in capital. To determine the net undivided profits, all debts due to TowneBank on which interest is past due and unpaid for a period of 12 months, unless well secured and in process of collection by law, are deducted from the undivided profits in addition to all expenses, losses, interest and taxes accrued. In addition, the payment of distributions to stockholders is subject to any prior rights of outstanding preferred stock. The ability of TowneBank to pay dividends in the future is and could be further influenced by bank regulatory requirements and capital guidelines.

Liquidation Rights

In the event of any liquidation, dissolution or winding up of TowneBank, the holders of shares of its common stock will be entitled to receive, after payment of all debts and liabilities of TowneBank and after satisfaction of all liquidation preferences applicable to any preferred stock, all remaining assets of TowneBank available for distribution in cash or in kind.

Voting Rights

The holders of TowneBank's common stock are entitled to one vote per share and, in general, a majority of votes cast with respect to a matter is sufficient to authorize action upon routine matters. Directors are elected by a plurality of the votes cast, and stockholders do not have the right to accumulate their votes in the election of directors.

Classes of Directors

TowneBank's board of directors is divided into three classes, apportioned as evenly as possible, with directors serving staggered three-year terms.

No Preemptive Rights; Redemption and Assessment

Holders of shares of TowneBank's common stock are not entitled to preemptive rights with respect to any shares that may be issued. TowneBank's common stock is not subject to redemption or any sinking fund and the outstanding shares are fully paid and nonassessable.

Preferred Stock

TowneBank's board of directors is empowered to authorize the issuance, in one or more series, of shares of preferred stock at such times, for such purposes and for such consideration as it may deem advisable without stockholder approval. TowneBank's board is also authorized to fix the designations, voting, conversion, preference and other relative rights, qualifications and limitations of any such series of preferred stock. TowneBank's board, without stockholder approval, may authorize the issuance of one or more series of preferred stock with voting and conversion rights which could adversely affect the voting power of the holders of TowneBank's common stock. The creation and issuance of any series of preferred stock, and the relative rights, designations and preferences of such series, if and when established, will depend upon, among other things, the future capital needs of TowneBank, then existing market conditions and other factors that, in the judgment of TowneBank's board, might warrant the issuance of preferred stock.

Anti-takeover Provisions

Certain provisions of the articles of incorporation and bylaws of TowneBank may discourage attempts to acquire control of TowneBank. These provisions also may render the removal of one or all directors more difficult or deter or delay corporate changes of control that TowneBank's board of directors did not approve. These provisions include the following:

Classified Board of Directors. TowneBank's articles of incorporation provide for classification of TowneBank's board of directors into three separate classes, which may have certain anti-takeover effects. For example, at least two annual meetings of stockholders may be required for the stockholders to replace a majority of the directors serving on TowneBank's board of directors.

Authorized Preferred Stock. TowneBank's board of directors may, subject to application of Virginia law and federal banking regulations, authorize the issuance of preferred stock at such times, for such purposes and for such consideration as the board may deem advisable without further stockholder approval. The issuance of preferred stock under certain circumstances may have the effect of discouraging an attempt by a third party to acquire control of TowneBank by, for example, authorizing the issuance of a series of preferred stock with rights and preferences designed to impede the proposed transaction.

Supermajority Voting Provisions. TowneBank's articles of incorporation state that certain significant corporate actions must be approved by a majority of all the votes entitled to be cast on the action by each voting group entitled to vote at a meeting at which a quorum of the voting group is present, provided that the action has been approved and recommended by at least two-thirds of the directors in office at the time of such approval and recommendation. If the action is not so approved and recommended by two-thirds of the directors in office, then the action must be approved by the affirmative vote of 80% or more of all of the votes entitled to be cast on such action by each voting group entitled to vote. These significant corporate actions include: adoption of plans of merger or share exchange; sales of all or substantially all of TowneBank's assets other than in the ordinary course of business; adoption of plans of dissolution; and amendments to or restatement of TowneBank's articles of incorporation.

Removal of Directors. TowneBank's articles of incorporation provide that any director may be removed by stockholders only for cause and only if the number of votes cast to remove the director constitutes a majority of the votes entitled to be cast at an election of directors of the voting group or voting groups by which the director was elected. Absent this provision, under Virginia law, a director may be removed with or without cause by a majority vote of the holders of the corporation's outstanding voting stock. The requirement that directors may only be removed for cause may provide anti-takeover protection through perpetuating the terms of incumbent directors by making it more difficult for stockholders to remove directors and replace them with their own nominees.

No Cumulative Voting. TowneBank's articles of incorporation do not provide for cumulative voting for any purpose. The absence of cumulative voting may afford anti-takeover protection by making it more difficult for stockholders of TowneBank to elect nominees opposed by the board of directors.

Special Meetings of Stockholders. The bylaws of TowneBank contain a provision pursuant to which special meetings of the stockholders of TowneBank may only be called by the chairman of the board, the chief executive officer, the president or by a majority of the board of directors. This provision is designed to afford anti-takeover protection by ensuring that only the board of directors and certain members of management may call a special meeting of stockholders to consider a proposed merger or other business combination.

Stockholder Nominations and Proposals. TowneBank's bylaws require a stockholder who intends to nominate a candidate for election to the board of directors, or to raise new business at a stockholder meeting, to deliver written notice to the Secretary of TowneBank not fewer than 60 days nor more than 90 days prior to the first anniversary of the preceding year's annual meeting; provided, however, if the date of the annual meeting is advanced by more than 30 days or delayed by more than 60 days from such anniversary date, notice by the stockholder must be delivered not earlier than the 90th day prior to such annual meeting and not later than the close of business on the later of the 60th day prior to such annual meeting or the 10th day following the day on which public announcement of the date of such meeting if first made.

The notice provision in TowneBank's bylaws requires TowneBank's stockholders who desire to raise new business to provide certain information to the corporation concerning the nature of the new business, the stockholder and the stockholder's interest in the business matter. Similarly, a TowneBank stockholder wishing to nominate any person for election as a director must provide TowneBank with certain information concerning the nominee and the proposing stockholder. These requirements may discourage TowneBank's stockholders from submitting director nominations and proposals.

Exhibit (13)

TOWNEBANK

2019 Annual Report

TowneBank
TABLE OF CONTENTS

As used in this report, the terms "Company," "we," "us," and "our" refer to TowneBank and our consolidated subsidiaries. The following list of acronyms and abbreviations are used in various sections of this Report, including the Notes to Consolidated Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations.

AFS	Available-for-Sale
ALCO	Asset/Liability Management Committee
ALLL	Allowance for Loan and Lease Losses
Angel	Angel Insurance and Financial Services, Inc.
AOCI	Accumulated Other Comprehensive Income (Loss)
ASC	Accounting Standard Codification
ASU	Accounting Standards Update
Basel III	Basel Committee on Banking Supervision's Capital Guidelines for U.S. Banks
BOLI	Bank-Owned Life Insurance
bp	Basis Points
BSA	Bank Secrecy Act
CECL	Current Expected Credit Loss
CETI	Common Equity Tier I
EPS	Earnings Per Share
FASB	Financial Accounting Standards Board
FDIC	Federal Deposit Insurance Corporation
FHLB	Federal Home Loan Bank of Atlanta
FHLMC	The Federal Home Loan Mortgage Corporation
FNMA	The Federal National Mortgage Association
FOMC	Federal Reserve Open Market Committee
FRB - Richmond	Federal Reserve Bank of Richmond
GAAP	Accounting Principles Generally Accepted in the United States of America
GNMA	Government National Mortgage Association
GSE	Government Sponsored Enterprise
HELOCs	Residential Home Equity Lines of Credit
HTM	Held-to-Maturity
LHFS	Loans Held for Sale
LIBOR	London InterBank Offered Rate
Monarch	Monarch Financial Holdings, Inc.
MBSs	Mortgage-backed Securities
N/M	Not meaningful
OCI	Other Comprehensive Income
OIS	Overnight Index Swap
OREO	Other Real Estate Owned
OTTI	Other Than Temporary Impairment
Paragon	Paragon Commercial Corporation
Paragon Bank	Paragon Commercial Bank
REPO	Retail Repurchase Agreement

RJFS	Raymond James Financial Services, Inc.
ROA	Annualized Return on Average Assets
ROE	Annualized Return on Average Equity
SCC	Virginia State Corporation Commission
SEC	Securities and Exchange Commission
SERP	Supplemental Executive Retirement Plan
SIL	Straus, Itzkowitz & LeCompte Insurance Agency, Inc.
TCJA or Tax Act	Tax Cuts and Jobs Act of 2017
TBA	To Be Announced
TDRs	Troubled Debt Restructurings
TIG	Towne Investment Group
TWM	Towne Wealth Management
U.S.	United States of America
VIE	Variable Interest Entity

TOWNEBANK
BUSINESS PROFILE AND CORPORATE MISSION STATEMENT

BUSINESS PROFILE

TowneBank was organized in 1998 under the laws of the Commonwealth of Virginia to engage in a general retail and commercial banking business and began operations on April 8, 1999. We place special emphasis on serving the financial needs of individuals, commercial enterprises, and professionals in Richmond, Virginia, the Greater Hampton Roads region in southeastern Virginia, northeastern North Carolina, Raleigh, Charlotte, Greensboro, and Greenville, North Carolina.

We offer a full range of banking and related financial services through our controlled divisions and subsidiaries. Unless indicated otherwise, the terms “Company,” “we,” “us,” and “our” refer to TowneBank and our consolidated subsidiaries.

Since our inception, we have expanded our financial services to include banking, real estate, mortgage, title, insurance, employee benefit services, and investments. We have three reportable segments: Banking, Realty, and Insurance.

Banking Segment. The Banking segment provides loan and deposit services to retail and commercial customers. We also provide commercial mortgage brokerage services and a variety of investment and asset management services.

Realty Segment. The Realty segment provides residential real estate services, originations of a variety of mortgage loans, resort property management, and residential and commercial title insurance.

Insurance Segment. The Insurance segment provides individual and business members with a wide array of insurance products, including life, property, casualty, travel, and health insurance.

CORPORATE MISSION STATEMENT

TowneBank will be a relationship and friendship-driven local bank focused on basic human values that will serve to create a warm sense of belonging and financial well-being among our family of members.

We will offer a competitive array of business and personal financial services, delivered only with the highest ethical standards. Our commitment to exquisite service for our members will lead to our ability to create a reasonable rate of return for our shareholders, a bright future for our dedicated bankers, and a leadership role for our bank in promoting the social, cultural, and economic well-being of the communities we serve.

TOWNEBANK
SELECTED FINANCIAL HIGHLIGHTS

Year Ended December 31,	2019	2018	Increase/(Decrease)	
(Dollars in thousands, except per share data)				
Results of Operations:				
Net interest income	$ 358,355	$ 341,073	$ 17,282	5.07 %
Noninterest income	205,588	191,593	13,995	7.30 %
Total revenue	563,943	532,666	31,277	5.87 %
Noninterest expenses	378,302	352,124	26,178	7.43 %
Provision for loan losses	9,371	8,541	830	9.72 %
Net income attributable to TowneBank	138,783	133,793	4,990	3.73 %
Net income per common share - basic	1.93	1.88	0.05	2.66 %
Net income per common share - diluted	1.92	1.88	0.04	2.13 %
Period End Data:				
Total assets	$ 11,947,663	$ 11,163,030	$ 784,633	7.03 %
Total assets - tangible (1)	11,446,448	10,670,620	775,828	7.27 %
Earning assets	10,687,658	10,020,525	667,133	6.66 %
Loans (net of unearned income and deferred costs)	8,419,288	8,018,233	401,055	5.00 %
Allowance for loan losses	58,234	52,094	6,140	11.79 %
Goodwill and other intangibles	501,215	492,410	8,805	1.79 %
Noninterest-bearing deposits	2,951,225	2,622,761	328,464	12.52 %
Interest-bearing deposits	6,319,692	5,747,661	572,031	9.95 %
Total deposits	9,270,917	8,370,422	900,495	10.76 %
Equity	1,653,694	1,538,420	115,274	7.49 %
Equity - tangible (1)	1,152,479	1,046,010	106,469	10.18 %
Book value per share	22.58	21.05	1.53	7.27 %
Book value per share - tangible (1)	15.69	14.26	1.43	10.03 %
Cash dividends declared per share	0.70	0.62	0.08	12.90 %
Daily Average Balances:				
Total assets	$ 11,638,426	$ 10,599,185	$ 1,039,241	9.80 %
Total assets - tangible (1)	11,135,318	10,129,663	1,005,655	9.93 %
Earning assets	10,428,539	9,504,755	923,784	9.72 %
Loans, excluding nonaccrual loans (net of unearned income)	8,122,210	7,567,571	554,639	7.33 %
Allowance for loan losses	54,476	48,737	5,739	11.78 %
Goodwill and other intangibles	503,108	469,522	33,586	7.15 %
Noninterest-bearing deposits	2,844,178	2,517,173	327,005	12.99 %
Interest-bearing deposits	6,110,692	5,314,060	796,632	14.99 %
Total deposits	8,954,870	7,831,233	1,123,637	14.35 %
Equity	1,597,281	1,454,796	142,485	9.79 %
Equity - tangible (1)	1,094,173	985,274	108,899	11.05 %
Key Ratios:				
Return on average assets	1.19%	1.26%	(0.07)%	(5.56)%
Return on average tangible assets (1)	1.33%	1.41%	(0.08)%	(5.67)%
Return on average equity	8.69%	9.20%	(0.51)%	(5.54)%
Return on average tangible equity (1)	13.58%	14.52%	(0.94)%	(6.47)%
Net interest margin (1)(2)	3.46%	3.61%	(0.15)%	(4.16)%
Efficiency ratio	66.98%	66.11%	0.87 %	1.32 %
Average earning assets/total average assets	89.60%	89.67%	(0.07)%	(0.08)%
Average loans/average deposits	90.70%	96.63%	(5.93)%	(6.14)%
Average noninterest deposits/total average deposits	31.76%	32.14%	(0.38)%	(1.18)%
Allowance for loan losses/period end loans	0.69%	0.65%	0.04 %	6.15 %
Period end equity/period end total assets	13.84%	13.78%	0.06 %	0.44 %

Notes:
(1) Non-GAAP financial measure. See the Non-GAAP Financial Measures section of Management's Discussion and Analysis for reconciliation.
(2) Presented on a tax-equivalent basis.

TOWNEBANK
SELECTED FINANCIAL HIGHLIGHTS

Year Ended December 31,	2017	2016	2015
(Dollars in thousands, except per share data)			
Results of Operations:			
Net interest income	$ 261,121	$ 218,876	$ 180,442
Noninterest income	188,121	155,222	117,283
Total revenue	449,242	374,098	297,725
Noninterest expenses	296,214	267,828	202,157
Provision for loan losses	5,426	5,357	3,027
Net income attributable to TowneBank	87,663	67,250	62,382
Net income per common share - basic	1.41	1.18	1.22
Net income per common share - diluted	1.41	1.18	1.22
Period End Data:			
Total assets	$ 8,522,176	$ 7,973,915	$ 6,296,574
Total assets - tangible (1)	8,213,358	7,671,149	6,115,579
Earning assets	7,706,747	7,346,961	5,827,888
Loans (net of unearned income and deferred costs)	5,946,965	5,807,221	4,519,393
Allowance for loan losses	45,131	42,001	38,359
Goodwill and other intangibles	308,819	302,766	180,995
Noninterest-bearing deposits	2,157,338	1,947,312	1,393,264
Interest-bearing deposits	4,290,882	4,087,885	3,520,763
Total deposits	6,448,220	6,035,197	4,914,027
Equity	1,142,505	1,086,558	820,194
Equity - tangible (1)	833,686	783,792	639,199
Book value per share	18.06	17.20	15.71
Book value per share - tangible (1)	13.13	12.36	12.21
Cash dividends declared per share	0.55	0.51	0.47
Daily Average Balances:			
Total assets	$ 8,334,999	$ 7,205,236	$ 6,039,418
Total assets - tangible (1)	8,027,381	6,958,267	5,858,762
Earning assets	7,517,473	6,603,377	5,380,881
Loans, excluding nonaccrual loans (net of unearned income)	5,901,797	5,129,990	4,239,887
Allowance for loan losses	43,760	39,547	37,194
Goodwill and other intangibles	307,618	246,968	180,656
Noninterest-bearing deposits	2,094,753	1,720,093	1,343,360
Interest-bearing deposits	4,248,571	3,852,100	3,324,533
Total deposits	6,343,324	5,572,192	4,667,893
Equity	1,123,588	963,775	804,744
Equity - tangible	815,969	716,807	624,088
Key Ratios:			
Return on average assets	1.05%	0.93%	1.03%
Return on average tangible assets (1)	1.15%	1.02%	1.10%
Return on average equity	7.80%	6.98%	7.75%
Return on average tangible equity (1)	11.35%	9.93%	10.34%
Net interest margin (1)(2)	3.51%	3.44%	3.39%
Efficiency ratio	65.94%	71.59%	68.11%
Average earning assets/total average assets	90.19%	89.41%	89.10%
Average loans/average deposits	93.04%	92.06%	90.83%
Average noninterest deposits/total average deposits	33.02%	30.87%	28.78%
Allowance for loan losses/period end loans	0.76%	0.72%	0.85%
Period end equity/period end total assets	13.41%	13.63%	13.03%

Notes:
(1) Non-GAAP financial measure. See the Non-GAAP Financial Measures section of Management's Discussion and Analysis for reconciliation.
(2) Presented on a tax-equivalent basis.

OVERVIEW

TowneBank is a commercial and retail banking business that places special emphasis on serving the financial needs of individuals, commercial enterprises, and professionals in our geographic footprint. We offer a full range of banking and related financial services through our controlled divisions and subsidiaries.

Our financial services include banking, real estate, mortgage, title, insurance, employee benefit services, and investments. We have three reportable segments: Banking, Realty, and Insurance. Our Banking segment provides loan and deposit services to retail and commercial customers and also provides commercial mortgage brokerage services and a variety of investment and asset management services. The Realty segment offers residential real estate services, originations of a variety of mortgage loans, resort property management, and residential and commercial title insurance. The Insurance segment provides individual and business members with a wide array of insurance products, including life, property, casualty, travel, and vehicle insurance, as well as employee and group benefits. Through Towne Insurance, we offer a full line of commercial and consumer insurance products and financial services. Through Towne Benefits, we offer health, life, dental, vision, and disability plans to employers, brokers, and individuals.

The following is a summary of the Company's 2019 financial performance:

- Net income increased to $138.78 million compared with $133.79 million in 2018. Diluted earnings were $1.92 per common share as compared to $1.88 per common share in 2018.

- Net interest income increased $17.28 million, or 5.07%, primarily due to a yield-driven increase in income from loans held for investment and investment securities.

- The provision for loan losses increased by $0.83 million, or 9.72%, from 2018. The loan loss reserve was 0.69% of total loans at December 31, 2019, up from 0.65% at year-end 2018. The increase in the provision for loan losses from the prior year was primarily a result of loan growth. Loan loss reserve as a percentage of total loans, excluding purchased loans was 0.81% and 0.82% at December 31, 2019, and 2018, respectively, which is consistent with continued stability in credit quality.

- Noninterest income increased by $14.00 million, or 7.30%, over 2018. Insurance commissions, real estate brokerage and property management income, residential mortgage brokerage income, and BOLI were all contributors to this growth. Insurance commissions income growth was driven by two agency acquisitions in 2019, a late 2018 agency acquisition, and organic growth. Residential mortgage brokerage income increased $1.71 million, or 2.62%, due to higher annual loan production. BOLI income increased due to the receipt of life insurance proceeds.

- Noninterest expense increased $26.18 million, or 7.43%, compared to 2018. This increase was driven by enhancements to Company infrastructure, resulting from changing industry standards and increased regulatory expectations related to exceeding $10 billion in assets, new market expansion, and increased operating expenses related to insurance agency acquisitions.

- The effective tax rate decreased to 19.02% in 2019 compared to 20.37% in 2018. The decrease in the rate from the prior year was the result of an increase in the benefit from tax advantaged income and certain investments. In 2018, additional net income tax expense was incurred due to non-deduction acquisition costs of $0.20 million and $0.70 million was recognized due to the finalization of the provisional component of the Tax Act.

The following is management's expectation of the Company's full-year 2020 performance, assuming a continuation of the current economic and rate environment:

- Net interest margin compression in the low single digits is expected.
- Noninterest expense is expected to have an average quarterly run rate of $94 - $97 million.
- ROA is expected to range between 1.10% - 1.20%.
- We will continue to work on driving our efficiency ratio down.
- Annual loan growth in the mid-single digits.
- Our capital and liquidity will continue to support growth.
- We will continue to maintain stable asset quality.
- Our new core banking system will go live in the second quarter
- We plan to pursue merger and acquisitions opportunities in our target market areas as they become available.

MERGER ACTIVITY

On January 1, 2019, the Company acquired Straus, Itzkowitz & LeCompte Insurance Agency, Inc., an independent insurance agency, which was merged into the operations of Towne Insurance Agency, LLC.

On September 1, 2019, the Company acquired Angel Insurance and Financial Services, Inc., an independent insurance agency, which was also merged into the operations of Towne Insurance Agency, LLC.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements and related disclosures in conformity with GAAP requires management to make judgments, assumptions, and estimates in certain circumstances that affect amounts reported in the Consolidated Financial Statements and the accompanying footnotes. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from management's current judgments. We consider our policies for the allowance for loan losses, other real estate owned, deferred income taxes, estimates of fair value of financial instruments, mergers and acquisitions, and goodwill and other intangibles to be critical accounting policies. Significant accounting policies and effects of new accounting pronouncements are discussed in detail in Note 1, "Summary of Significant Accounting Policies," in the "Notes to Consolidated Financial Statements."

The following is a summary of our critical accounting policies that are highly dependent on estimates, assumptions, and judgments.

Allowance for Loan Losses. The allowance for loan losses is established through charges to earnings in the form of a provision for loan losses. Increases and decreases in the allowance due to changes in the measurement of impaired loans, if applicable, are included in the provision for loan losses. We periodically evaluate the adequacy of the allowance for loan losses in order to maintain the allowance at a level that is sufficient to absorb probable credit losses. The amount of allowance is based on management's evaluation of the collectability of the loan portfolio, including the nature of the loan portfolio, credit concentrations, trends in historical loss experience, expected cash flows on purchased loans, specific impaired loans, and external influences such as changes in economic conditions.

In addition, various regulatory agencies, as an integral part of their examination process, periodically review our allowance for loan losses. Such agencies may require us to recognize additions to the allowance based on their judgments of information available to them at the time of their examination. Although management believes that we use the best information available to evaluate the adequacy of the allowance, unknown market or borrower circumstances could result in adjustments and net earnings being significantly affected if conditions differ substantially from the assumptions used by management in determining the adequacy of the allowance.

Other Real Estate Owned. OREO, which is included in other assets on the balance sheet, consists primarily of commercial and residential real estate that has been obtained in partial or full satisfaction of loan obligations and former bank premises held for sale. OREO is carried at the fair value of the property, less estimated selling costs, with any difference between the fair value of the property, less estimated selling costs, and the carrying value of the loan recorded through a charge to the allowance for loan losses upon transfer to OREO. Subsequent write-downs required for declines in value are recorded through a valuation allowance, or taken directly to the asset, and charged to other noninterest expense.

Deferred Income Taxes. Deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets, including tax loss and credit carry-forwards, and deferred tax liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Deferred income tax expense (benefit) represents the change during the period in the deferred tax assets and deferred tax liabilities.

We use the asset and liability method in accounting for income taxes. This method recognizes the amount of taxes payable or refundable for the current year and recognizes deferred tax liabilities and assets for the expected future tax consequences of events and transactions that have been recognized in our financial statements or tax returns. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Realization of the deferred income tax asset is dependent on generating sufficient taxable income in future years, and, as such, material changes could impact our financial condition and results of operations.

Estimates of Fair Value of Financial Instruments. The estimation of fair value is significant to certain assets, including loans held for sale, available-for-sale securities, on-balance-sheet commitments to originate loans held for sale, and other real estate held for sale. These assets and liabilities are recorded either at fair value or at the lower of cost or fair value, as applicable. The fair values of loans held for sale are based on commitments on hand from investors or, if commitments have not yet been obtained, prevailing market rates. The fair values of available-for-sale securities are based on published market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities. The fair values of commitments to originate loans held for sale are based on fees currently charged to enter into similar agreements and, for fixed-rate commitments, also consider the difference between current levels of interest rates and committed rates.

Fair values can be volatile and may be influenced by a number of factors, including market interest rates, prepayment speeds, discount rates, and market conditions. Since these factors can change significantly and rapidly, fair values are difficult to predict and subject to material changes that could impact our financial condition and results of operations.

Mergers and Acquisitions. Mergers and acquisitions are accounted for using the acquisition method, as required by ASC 805, *Business Combinations*. Under this method, the cost of the acquired entity will be allocated to the assets acquired and liabilities assumed based on their fair values at the date of acquisition. The excess of the cost over the fair value of the acquired net assets is recognized as goodwill.

Goodwill and Other Intangibles. We record all assets and liabilities acquired in purchase acquisitions, including goodwill, intangibles with indefinite lives, and other intangibles, at fair value as required by ASC 805, *Business Acquisitions*. The initial recording of goodwill and other intangibles requires subjective decisions concerning estimates of the fair value of the acquired assets and liabilities.

Goodwill is reviewed for potential impairment at the reporting unit level (one level below the identified business segments) on an annual basis, or more often if events or circumstances indicate there may be impairment. Testing is conducted in two steps: identifying the potential impairment and then, if necessary, identifying the amount of impairment. The first step compares the fair value of the reporting unit to its carrying amount. If the fair value is less than the carrying amount, a second test is conducted by comparing the implied fair value of reporting unit goodwill with the carrying amount of that goodwill. If the carrying amount exceeds the implied fair value, an impairment loss is recognized in an amount equal to that excess.

Other identifiable intangible assets are evaluated for impairment if events or changes in circumstances indicate a possible impairment. Such evaluation is based on undiscounted cash flow projections, which may extend far into the future and, by their nature, are difficult to determine over an extended timeframe. Fair value may be influenced by market prices, comparison to similar assets, market multiples, discounted cash flow analysis, and other determinants. Factors that may significantly affect the estimates include, among others, competitive forces, customer behaviors and attrition, changes in revenue growth trends, cost structures and technology, changes in discount rates, and specific industry or market sector conditions. Other key judgments in accounting for intangibles include useful life and classification between goodwill and intangibles with indefinite lives or other intangibles that require amortization.

ANALYSIS OF RESULTS OF OPERATIONS

Consolidated Performance Summary

Results of Operations: We reported net income for the years ended December 31, 2019, 2018, and 2017, of $138.78 million, $133.79 million, and $87.66 million, respectively. Diluted earnings per share were $1.92, $1.88, and $1.41 for the years ended December 31, 2019, 2018, and 2017, respectively. In 2019, EPS were affected by acquisition related expenses of $0.58 million on an after tax basis. In 2018, EPS were affected by the issuance of 9.46 million shares of common stock related to the acquisition of Paragon on January 26, 2018 and acquisition related expenses of $7.00 million on an after tax basis. Also, an additional expense of $0.70 million was recognized in 2018 due to the finalization of the provisional component of the Tax Act. EPS in 2017 were affected by the enactment of the Tax Act, which resulted in an additional net income tax expense of $10.11 million, primarily related to a revaluation of deferred tax assets at the lower statutory rate.

Profitability, as measured by our ROA, was 1.19%, 1.26%, and 1.05% for the years ended December 31, 2019, 2018, and 2017, respectively. Return on average tangible assets (non-GAAP) was 1.33%, 1.41%, and 1.15% for the same respective periods. ROE was 8.69%, 9.20%, and 7.80% for years ended December 31, 2019, 2018, and 2017, respectively, while return on average tangible equity (non-GAAP) was 13.58%, 14.52%, and 11.35% for the same respective years.

Our operating income, calculated as net interest income and noninterest income, excluding gains and losses on investment securities, was $564.79 million for the year ended December 31, 2019, compared to $532.66 million and $449.24 million for 2018 and 2017, respectively.

Net Interest Income: Net interest income, the major source of our earnings, is the income generated by interest-earning assets reduced by the total interest cost of the funds incurred to carry them. It is impacted by market interest rates and the mix and volume of earning assets and interest-bearing liabilities. The yields and rates in this discussion and in the following tables have been computed based upon interest income and expense adjusted to a fully taxable equivalent basis (non-GAAP) using a 21% federal marginal tax rate for 2019 and 2018, and a 35% federal marginal tax rate for 2017.

The Company utilizes various asset and liability management strategies to manage net interest income exposure to interest rate risk. Refer to the "Market Risk Management" and "Interest Sensitivity" sections of this financial review for further discussions regarding our asset and liability management policies.

Net interest income, on a tax-equivalent basis (non-GAAP), was $360.81 million for the year ended December 31, 2019, which was $17.50 million, or 5.10%, more than the $343.31 million reported in the previous year. In comparison to the prior year, net interest income rose primarily due to higher yields on earning assets. Accretion of purchase accounting marks added $9.83 million, or 10 bp, to margin in the current year and added $10.49 million, or 15 bp, to margin in 2018. This was partially offset by an increase in interest expense due to organic growth in interest-bearing liabilities.

Interest income, on a tax-equivalent basis (non-GAAP), was $470.28 million for the year ended December 31, 2019, which was $46.22 million, or 10.90%, greater than the $424.06 million for the year ended December 31, 2018. Average earning assets grew to $10.43 billion in 2019 from $9.50 billion in 2018, an increase of $0.92 billion, or 9.72%. The yield on earning assets was 4.51% in the year ended December 31, 2019, compared to 4.46% in the prior year. Average loan balances, excluding nonaccrual loans of $18.95 million, were $8.12 billion, or 7.16%, higher in 2019 than in 2018, while loan yields increased by 6 bp. The increase in interest income from the prior year was primarily driven by higher yields across all earning asset categories, coupled with organic growth in loans and investment securities.

Interest expense for the year ended December 31, 2019, increased by $28.72 million, or 35.57%, to $109.47 million, compared to $80.75 million for the year ended December 31, 2018. The balance of average interest-bearing liabilities increased to $6.97 billion in 2019 from $6.46 billion in 2018, an increase of $0.51 billion, or 7.82%. The increase in interest expense as compared to the prior year was primarily due to organic growth and an increase in costs related to interest-bearing deposits.

Net interest margin, on a tax-equivalent basis (non-GAAP), which is net interest income expressed as a percentage of average earning assets, was 3.46% in the year ended December 31, 2019, which was 15 bp lower than the 3.61% a year ago. The margin decline in comparison to prior year periods was driven by growth in interest-bearing deposits coupled with higher deposit costs which outpaced the increases in earning asset volume and yield.

The purpose of volume and rate analysis is to describe the impact on interest income resulting from changes in average balances and average interest rates from those in effect during the previous year. The following tables include average balances, interest income and expense, average yields and costs, and volume and rate analysis (dollars in thousands):

	Year Ended December 31,								
	2019			2018			2017		
	Average Balance	Interest Income/ Expense	Average Yield/ Rate (1)	Average Balance	Interest Income/ Expense	Average Yield/ Rate (1)	Average Balance	Interest Income/ Expense	Average Yield/ Rate (1)
Assets:									
Loans (net of unearned income and deferred costs), excluding nonaccrual loans (2)	$ 8,122,210	$ 405,511	4.99%	$ 7,567,570	$ 373,057	4.93%	$ 5,901,797	$ 276,747	4.69%
Taxable investment securities	1,202,107	34,141	2.84%	1,004,080	24,729	2.46%	600,080	11,597	1.93%
Tax-exempt investment securities	102,731	3,426	3.34%	79,720	2,920	3.66%	48,228	1,590	3.28%
Total Securities	1,304,838	37,567	2.88%	1,083,800	27,649	2.55%	648,308	13,187	2.03%
Interest-bearing deposits	665,903	13,825	2.08%	560,368	10,229	1.83%	696,507	7,480	1.07%
Mortgage loans held for sale	335,588	13,379	3.99%	293,017	13,124	4.48%	271,281	10,561	3.89%
Total earning assets	10,428,539	470,282	4.51%	9,504,755	424,059	4.46%	7,517,893	307,975	4.10%
Less: allowance for loan losses	(54,476)			(48,737)			(43,760)		
Total nonearning assets	1,264,363			1,143,167			860,866		
Total assets	$11,638,426			$10,599,185			$ 8,334,999		
Liabilities and Equity:									
Interest-bearing deposits									
Demand and money market	$ 3,351,135	$ 26,909	0.80%	$ 2,951,038	$ 16,458	0.56%	$ 2,260,378	$ 8,020	0.35%
Savings	280,894	3,296	1.17%	302,435	3,824	1.26%	319,940	3,305	1.03%
Certificates of deposit	2,478,663	56,050	2.26%	2,060,587	32,859	1.59%	1,668,252	17,467	1.05%
Total interest-bearing deposits	6,110,692	86,255	1.41%	5,314,060	53,141	1.00%	4,248,570	28,792	0.68%
Borrowings	609,142	11,368	1.84%	897,574	15,542	1.71%	617,720	9,942	1.61%
Subordinated debt, net	248,139	11,847	4.77%	251,097	12,067	4.81%	113,752	5,249	4.61%
Total interest-bearing liabilities	6,967,973	109,470	1.57%	6,462,731	80,750	1.25%	4,980,042	43,983	0.88%
Noninterest-bearing liabilities									
Demand deposits	2,844,178			2,517,173			2,094,753		
Other noninterest-bearing liabilities	228,994			164,486			136,616		
Total liabilities	10,041,145			9,144,390			7,211,411		
Shareholders' equity	1,597,281			1,454,795			1,123,588		
Total liabilities and equity	$11,638,426			$10,599,185			$ 8,334,999		
Net interest income (tax-equivalent basis)		$ 360,812			$ 343,309			$ 263,992	
Reconcilement of Non-GAAP Financial Measures:									
Tax-equivalent basis adjustment		(2,457)			(2,236)			(2,871)	
Net interest income (GAAP)		$ 358,355			$ 341,073			$ 261,121	
Interest rate spread (3)			2.94%			3.21%			3.22%
Interest expense as a percent of average earning assets			1.05%			0.85%			0.59%
Net interest margin (tax-equivalent basis) (non-GAAP) (4)			3.46%			3.61%			3.51%
Total cost of deposits			0.96%			0.68%			0.45%

(1) Yields and interest income are presented on a taxable-equivalent basis using the federal statutory tax rate of 21% in 2019 and 2018 and 35% in 2017.
(2) Excludes average nonaccrual loans of $18.95 million in 2019, $5.43 million in 2018, and $10.43 million in 2017.
(3) Interest rate spread is the average yield earned on earning assets less the average rate paid on interest-bearing liabilities.
(4) Net interest margin is net interest income expressed as a percentage of average earning assets. Fully tax equivalent.

(in thousands)	2019 vs 2018 Increase (Decrease) Due to Changes In			2018 vs 2017 Increase (Decrease) Due to Changes In		
	Volume	**Rate (1)**	**Total**	**Volume**	**Rate (1)**	**Total**
Assets:						
Loans (net of unearned income and deferred costs), excluding nonaccrual loans	$ 4,815	$ 27,639	$ 32,454	$ 81,500	$ 14,810	$ 96,310
Taxable investment securities	4,114	5,298	9,412	9,330	3,802	13,132
Tax-exempt investment securities	(279)	785	506	1,137	193	1,330
Interest-bearing deposits	1,516	2,080	3,596	(1,686)	4,435	2,749
Loans held for sale	(1,532)	1,787	255	890	1,673	2,563
Total earning assets	8,634	37,589	46,223	91,171	24,913	116,084
Liabilities and Equity:						
Interest-bearing deposits:						
Demand and money market accounts	7,988	2,463	10,451	2,939	5,499	8,438
Savings	(265)	(263)	(528)	(189)	708	519
Certificates of deposit	15,614	7,577	23,191	4,774	10,618	15,392
Total interest-bearing deposits	23,337	9,777	33,114	7,524	16,825	24,349
FHLB advances and repurchase agreements	1,133	(5,307)	(4,174)	4,796	804	5,600
Subordinated debt	(78)	(142)	(220)	6,591	227	6,818
Total interest-bearing liabilities	24,392	4,328	28,720	18,911	17,856	36,767
Net interest income (tax equivalent basis)	$ (15,758)	$ 33,261	$ 17,503	$ 72,260	$ 7,057	$ 79,317

(1) Variances caused by the change in rate times the change in balances are allocated to rate.

Provision for Loan Losses: The provision for loan losses is charged against earnings in order to establish and maintain the allowance for loan losses at a level that reflects management's evaluation of the risk inherent in the portfolio. Management considers continuing assessments of nonperforming and "watch list" loans, analytical reviews of loan loss experience in relation to outstanding loans, and management's judgment with respect to current and expected economic conditions and their impact on the existing loan portfolio. The provisions for loan losses recorded in 2019, 2018, and 2017 were $9.37 million, $8.54 million, and $5.43 million, respectively. Net charge-offs were $3.23 million, $1.58 million, and $2.30 million for 2019, 2018, and 2017, respectively. The increase in the provision for loan losses in the current year period from the prior year and the increase in 2018 from 2017 was primarily due to loan growth. The allowance for loan losses as a percentage of period-end loans was 0.69% and 0.65% at December 31, 2019 and 2018, respectively. The allowance for loan losses as a percentage of period-end loans, excluding purchased loans, was 0.81% and 0.82% at December 31, 2019 and 2018, respectively. For further discussion and analysis of the loan portfolio and the allowance for loan losses, see the "Analysis of Financial Condition" section found later in this report. Also, see Note 4, "Loans and Allowance for Loan Losses," in the Notes to Consolidated Financial Statements.

Noninterest Income: Total noninterest income for the year ended December 31, 2019, was $205.59 million, or $14.00 million, and 7.30% higher than 2018. Total noninterest income for the year ended December 31, 2018, was $191.59 million, representing a $3.47 million, or 1.85%, increase from 2017. Noninterest income, excluding securities gains or losses, for the year ended December 31, 2019, was 36.55% of total operating income, compared with 35.97% for 2018 and 41.88% for 2017.

The following table provides an analysis of noninterest income (dollars in thousands):

				2019 over 2018 Increase/(Decrease)		2018 over 2017 Increase/(Decrease)	
For the Year Ended December 31,	**2019**	**2018**	**2017**	**Amount**	**%**	**Amount**	**%**
Residential mortgage banking income, net	$ 66,812	$ 65,104	$ 75,851	$ 1,708	2.62 %	$ (10,747)	(14.17)%
Real estate brokerage and property management income, net	34,292	31,863	27,487	2,429	7.62 %	4,376	15.92 %
Insurance commissions and other title fees and income, net	64,478	56,164	51,933	8,314	14.80 %	4,231	8.15 %
Service charges on deposit accounts	10,544	11,808	10,594	(1,264)	(10.70)%	1,214	11.46 %
Credit card merchant fees, net	4,746	5,472	5,008	(726)	(13.27)%	464	9.27 %
BOLI	9,215	6,836	6,262	2,379	34.80 %	574	9.17 %
Other income							
Towne Investment income, net	6,807	6,354	4,870	453	7.13 %	1,484	30.47 %
Service fees on loans	3,020	2,209	1,629	811	36.71 %	580	35.60 %
Income from equity method investments	703	665	838	38	5.71 %	(173)	(20.64)%
Commercial mortgage brokerage fees, net	331	199	202	132	66.33 %	(3)	(1.49)%
Other	5,485	4,916	3,448	569	11.57 %	1,468	42.58 %
Total other income	16,346	14,343	10,987	2,003	13.97 %	3,356	30.55 %
Noninterest income before securities gain/(loss)	206,433	191,590	188,122	14,843	7.75 %	3,468	1.84 %
Gain/(loss) on securities available for sale	(845)	3	(1)	(848)	N/M	4	(400.00)%
Total noninterest income	$ 205,588	$ 191,593	$ 188,121	$ 13,995	7.30 %	$ 3,472	1.85 %

For the year ended December 31, 2019, residential mortgage banking income, net of commission expense, was $66.81 million, reflecting an increase of $1.71 million, or 2.62%, compared to 2018, which was $10.75 million, or 14.17%, below 2017. Production volume increased $133.34 million in 2019, as compared to 2018. Lower mortgage rates during the latter part of 2019 led to the increase in volume and an increase in refinance activity. Inventory levels remained low throughout 2019. Between 2018 and 2017, the loss of a group of mortgage producers resulted in an approximate $110.0 million in production decline. This was compounded by fluctuations in mortgage rates and lower housing inventory levels. The 2019 change in the value of rate lock commitments and forward contracts recorded had a positive impact on mortgage banking income of $2.49 million, as compared 2018. The change in the value of rate lock commitments and forward contracts in 2018 increased $1.15 million compared to 2017. For further information, refer to our discussion of the Realty segment in this Annual Report, which provides a comparative schedule of operations.

Real estate brokerage and property management income, net of commission expense, for the year ended December 31, 2019, was $34.29 million, an increase of $2.43 million, or 7.62%, from 2018, which was $4.38 million, or 15.92%, higher than 2017. The increases year-over-year for 2019 and 2018 were driven by higher property management fees due to increases in the number of property units managed. Real estate sales commissions, net, increased $0.41 million in 2019 compared to 2018, after increasing $1.47 million in 2018 compared to 2017. Sales volume increased $106.83 million in 2019 despite a 42 unit decline. Sales volume in 2018 increased $140.09 million. The number of units sold totaled 4,822 in 2019, 4,864 in 2018 and 4,388 in 2017.

For the year ended December 31, 2019, insurance commissions and other title income, net of commission expense, were $64.48 million, which was $8.31 million, or 14.80%, higher than comparative 2018. Property and casualty insurance commissions, net of commission expense, increased $8.61 million, driven by organic growth and 2019 acquisitions. Benefit and travel insurance commissions, net of commission expense, increased $0.71 million in 2019 compared to 2018. The agencies acquired late in 2018 and during 2019 contributed net commission and fee income of $7.29 million in 2019. The year ended December 31, 2019 included contingency and bonus revenue income of $6.31 million, compared to $4.89 million and $6.32 million for 2018 and 2017, respectively. When compared to 2017, insurance commissions for the year ended December 31, 2018, were $4.23 million, or 8.15%, higher, largely due to a full year of operations from three insurance agencies acquired in the second half of 2017.

Service charges on deposit accounts were $10.54 million for 2019, compared with $11.81 million and $10.59 million for 2018 and 2017, respectively. The decrease from the prior year was largely due to new regulations applicable to financial institutions that have assets of $10 billion or more, which took effect in third quarter 2019. These rules provide that the maximum permissible interchange fee for an electronic debit transaction is the sum of 21 cents per transaction and 5 bp multiplied by the value of the transaction. An upward adjustment of no more than 1 cent to an issuer's debit card interchange fee is allowed if the card issuer develops and implements policies and procedures reasonably designed to achieve certain fraud-prevention standards.The impact was a reduction in noninterest income of approximately $1.90 million in the second half of 2019. The increase between 2018 and 2017 was primarily attributable to accounts acquired in the Paragon merger and organic growth. Average deposits increased 14.35% and 23.46% in the years ended December 31, 2019 and 2018, respectively.

For the year ended December 31, 2019, credit card merchant fees totaled $4.75 million, which was $0.73 million, or 13.27%, lower than comparative 2018, which was $0.46 million, or 9.27%, higher than 2017. During 2019, we converted to a new processing platform that will allow us to provide additional services and capabilities, but had a short-term adverse effect on credit card merchant fees. The increase in 2018 from 2017 was primarily due to higher transaction volume.

Income from BOLI was $9.22 million in 2019, compared to $6.84 million in 2018 and $6.26 million in 2017. The year-over-year increase was driven by proceeds from life insurance policies and higher average BOLI balances.

Other noninterest income for the year ended December 31, 2019 was $16.35 million, compared with $14.34 million for the year ended December 31, 2018, and $10.99 million for the year ended December 31, 2017. Other noninterest income includes income generated by TIG and TWM, net of commission expense of $6.81 million, $6.35 million, and $4.87 million for the years ended December 31, 2019, 2018, and 2017, respectively. The increase in TIG and TWM income for 2019 and 2018 was driven by growth in assets under management by existing team members and the efforts of the teams built in 2017. Other contributing factors to the increase in noninterest income were an increase in loan service fees and gains on the sale of OREO.

Noninterest Expense: Total noninterest expense for 2019 was $378.30 million, which was $26.18 million, or 7.43%, higher than 2018. Primary components of 2019 noninterest expense were salaries and employee benefits of $218.92 million, occupancy expenses of $31.38 million, furniture and equipment expenses of $14.35 million, professional fees of $12.94 million, advertising and marketing expenses of $12.28 million, and amortization of intangibles of $12.37 million. The primary driver of the increase in total noninterest expense in 2019 from 2018 was production related growth and Company infrastructure enhancements due to changing industry standards and increased regulatory expectations related to our exceeding $10 billion in assets. The increase in 2018 compared to 2017 was driven by the January 26, 2018, acquisition of Paragon. Other sources of the increase were two insurance agency acquisitions in 2018 plus a full year of expenses for two companies acquired in 2017.

Total noninterest expense to total operating revenue was 66.98% for the year ended December 31, 2019, compared with 66.11% for 2018 and 65.94% for 2017. The following table provides an analysis of noninterest expense (dollars in thousands):

				2019 over 2018 Increase/(Decrease)		2018 over 2017 Increase/(Decrease)	
For the year ended December 31,	**2019**	**2018**	**2017**	**Amount**	**%**	**Amount**	**%**
Salaries and benefits	$218,920	$201,838	$169,449	$ 17,082	8.46 %	$ 32,389	19.11 %
Occupancy	31,381	27,644	26,855	3,737	13.52 %	789	2.94 %
Furniture and equipment	14,351	14,477	14,072	(126)	(0.87)%	405	2.88 %
Amortization - intangibles	12,370	11,710	7,656	660	5.64 %	4,054	52.95 %
Software expenses	11,717	10,621	8,517	1,096	10.32 %	2,104	24.70 %
Data processing	11,825	10,364	6,975	1,461	14.10 %	3,389	48.59 %
Professional fees	12,943	8,323	7,144	4,620	55.51 %	1,179	16.50 %
Advertising and marketing	12,279	11,194	9,867	1,085	9.69 %	1,327	13.45 %
Other expenses							
Acquisition-related expenses	657	8,428	2,268	(7,771)	(92.20)%	6,160	271.60 %
Bank franchise tax/SCC fees	7,251	5,647	5,303	1,604	28.40 %	344	6.49 %
Charitable contributions	9,339	5,104	5,550	4,235	82.97 %	(446)	(8.04)%
Directors' expense	2,136	1,991	1,734	145	7.28 %	257	14.82 %
FDIC and other insurance	3,119	5,047	4,249	(1,928)	(38.20)%	798	18.78 %
Foreclosed property expenses	985	820	782	165	20.12 %	38	4.86 %
Other	15,807	15,275	13,336	532	3.48 %	1,939	14.54 %
Stationery and office supplies	2,962	3,217	2,730	(255)	(7.93)%	487	17.84 %
Telephone and postage	6,426	6,788	6,907	(362)	(5.33)%	(119)	(1.72)%
Travel/Meals/Entertainment	3,834	3,636	2,820	198	5.45 %	816	28.94 %
Total other expenses	52,516	55,953	45,679	(3,437)	(6.14)%	10,274	22.49 %
Total noninterest expense	$378,302	$352,124	$296,214	$ 26,178	7.43 %	$ 55,910	18.87 %

Salaries and employee benefits, the largest portion of noninterest expense, were $218.92 million, representing 57.87% of total noninterest expense for the year ended December 31, 2019. This was a $17.08 million, or 8.46%, increase over comparative 2018. We added a Corporate Banking Group in the second quarter of 2019, established two new banking groups, located in Greensboro and Greenville, North Carolina, and opened full service banking offices in those cities in the fourth and first quarters of 2019, respectively. We also acquired two insurance agencies in the first and fourth quarter of 2019 plus one mid-fourth quarter 2018. Additional staffing requirements related to TowneBank exceeding $10.0 billion in assets also contributed to the increase with specific areas of expansion in information technology, risk and compliance, accounting, and internal audit. Salaries and benefits expense for the year ended December 31, 2018, was $201.84 million, up 19.11%, or $32.39 million, over 2017. The increase was primarily due to the addition of staff resulting from the Paragon acquisition, adding $19.39 million, while the insurance agency acquisitions added $1.26 million.

In our Banking segment, we had a total of 1,145 full-time equivalent employees ("FTE") at December 31, 2019, which was up from 1,068 and 877 at December 31, 2018 and 2017, respectively. In our non-Banking segments at December 31, 2019, we had a total of 1,301 FTEs, excluding real estate sales agents, a decrease from 1,342 at December 31, 2018, which had decreased from 1,436 at December 31, 2017. Real estate sales agents are independent contractors and, therefore, not included as the Company's employees. There were 407 real estate sales agents at December 31, 2019.

For the year ended December 31, 2019, occupancy expense totaled $31.38 million, representing an increase of $3.74 million, or 13.52%, over comparative 2018. Occupancy expense for 2018 was $0.79 million, or 2.94%, greater than the 2017 amount of $26.86 million. Occupancy expense related to North Carolina expansion and insurance agency acquisitions totaled $1.03 million in 2019. Excluding these expenses, the increase in occupancy expense was driven by higher maintenance and cleaning service expenses, as well as increases in rent expense and depreciation of leasehold improvements. Additionally, we performed a comprehensive review of all lease agreements in conjunction with our adoption of ASU 842. This review led to a correction of several lease schedules, resulting in a one-time increase to rent expense $1.08 million year-to-date. For further financial details, see Note 7 – Leases of the Notes to Consolidated Financial Statements in this report. Occupancy expense related to Paragon branches was $1.09 million in 2018, excluding occupancy related to Paragon branches and the acquired insurance agencies, occupancy expense declined $0.39 million.

Furniture and equipment expense was $14.35 million for 2019, or $0.13 million and 0.87% lower than 2018. Furniture and equipment expense was $14.48 million for 2018, or $0.41 million and 2.88% higher than comparative 2017. The decrease from 2018 to 2019 was due to lower year over year furniture and equipment costs from acquisitions. The increase from 2017 to 2018 was driven by acquisitions. Excluding acquisitions, furniture and equipment expense declined $0.35 million compared to 2017.

Other expenses for 2019 were $52.52 million, which was $3.44 million, or 6.14%, less than the 2018 amount of $55.95 million. The decrease from 2018 to 2019 was largely driven by the decrease in acquisition costs of $7.77 million, along with a decrease in FDIC and other insurance expense of $1.93 million related to small bank credits, offset by increases in charitable contributions of $4.24 million. The primary driver of the increase from 2017 to 2018 was the increase in acquisition costs, primarily related to the Paragon acquisition of $6.16 million, along with increases in software expense of $2.10 million, outside processing fees of $3.39 million, and amortization of intangible assets of $4.05 million.

Income Taxes: Income taxes for the year ended December 31, 2019, were $32.60 million. This was $1.63 million lower than the 2018 amount of $34.23 million, which was $20.59 million lower than the 2017 amount of $54.81 million. The effective tax rate decreased to 19.02% in 2019 compared to 20.37% in 2018. In 2018, additional net income tax expense was incurred due to non-deductible acquisition costs of $0.20 million and $0.70 million was recognized due to the finalization of the provisional component of the Tax Act.

SEGMENT PERFORMANCE SUMMARY

Our reportable segments are a traditional full-service community bank, a full-service realty business, and a full-service insurance agency. In this section, we discuss the performance and financial results of our segments. For further financial details, see Note 27, Segment Reporting, in the Notes to Consolidated Financial Statements.

Banking Segment: For the year ended December 31, 2019, the Banking segment represented 86.25%, or $119.71 million, of our total consolidated net income, compared to 89.69% and 83.97% for 2018 and 2017, respectively.

Pre-tax earnings for the year ended December 31, 2019, for the Banking segment were $145.41 million, decreasing $3.48 million, or 2.34%, from comparative 2018. A $22.19 million, or 6.10% increase in total revenues was outpaced by an increase in total expenses of $25.11 million, or 12.07%, leading to a decrease in earnings of $0.30 million, or 0.25%. The provision for loan loss increased $0.83 million or 9.72%, from 2018 due to portfolio growth while the provision for income tax decreased $3.17 million.

The increase in net interest income for the year ended December 31, 2019, of $22.39 million, or 6.79%, was primarily a result of additional interest income from an increase in earning assets due to organic growth and higher yields. Average earnings assets increased in all categories with most notable increases in average loan balances of $0.55 billion to $8.12 billion and taxable investment securities of $0.20 billion to $1.20 billion. These increases were partially offset by additional interest expense of $7.36 million, the majority of which is due to increased costs related to interest-bearing deposits.

Noninterest income decreased $0.20 million, or 0.57%, primarily due to a combination of a decrease in service charges on deposit accounts of $1.26 million driven by the Durbin amendment and investment security losses totaling $0.85 million. Included in other income is income from BOLI policies of $7.35 million and Towne Investment income of $6.81 million. Also included in other income is gains on sale of OREO of $0.77 million, compared to OREO gains of $0.48 million in 2018. Credit card merchant fees declined $0.73 million, year over year, related to the implementation of a new processing platform, as previously discussed.

Noninterest expense for the year ended December 31, 2019, increased $25.11 million, or 12.07%, over 2018 driven by expenses related to market expansion and an increase in infrastructure costs associated with additional regulatory and compliance demands due to Company assets exceeding $10 billion. Salaries and employee benefits expense increased $16.68 million, or 14.57%. Occupancy expense increased $3.01 million, or 17.28%, and furniture and equipment expense increased $0.33 million, or 3.31%. In 2019 professional fees increased $5.16 million, charitable contribution expense increased $4.24 million, and bank franchise/SCC expense increased $1.54 million over 2018.

Pre-tax earnings for the year ended December 31, 2018, for the Banking segment were $148.89 million, increasing $30.69 million, or 25.97%, from comparative 2017. The increase in earnings was driven by an $83.19 million, or 29.64%, increase in total revenues, offset by an increase in total expenses of $49.30 million, or 31.03%.

The increase in net interest income for the year ended December 31, 2018, of $78.58 million, or 31.31%, was primarily a result of additional interest income from an increase in earning assets related to the Paragon merger combined with organic growth and higher yields, as average loan balances increased by $1.67 billion to $7.57 billion and taxable investment securities increased by $0.40 billion to $1.00 billion. The increase was partially offset by additional interest expense of $7.36 million, the majority of which is due to increased costs related to interest-bearing deposits.

The increase in noninterest income of $4.61 million, or 15.56%, was primarily due to a combination of an increase from income generated by TIG and TWM, net of commission expense, of $1.48 million, an increase of service charges on deposit accounts of $1.21 million, income from BOLI policies of $0.58 million, and an increase in credit card merchant fees of $0.46 million. Gains and losses from the sale of OREO are carried in noninterest income. In 2018, we had gains on sale of OREO of $0.46 million, compared to losses of $0.53 million in 2017, for a benefit to noninterest income of $0.99 million.

Noninterest expense for the year ended December 31, 2018, increased $49.30 million, or 31.03%, over 2017 driven by expenses related to the acquisition of Paragon. Also impacting expenses were costs associated with additional regulatory and compliance demands due to Company assets exceeding $10.0 billion. Salaries and employee benefits expense increased $28.82 million, or 33.64%, $19.39 million of which was attributable to the acquisition of Paragon. Occupancy expense increased $1.05 million, or 6.39%, and furniture and equipment expense increased $0.51 million, or 5.38%. Merger and acquisition expenses increased $5.69 million and amortization of intangible assets increased $3.37 million in 2018 due to the Paragon merger. Other increases included outside processing expense of $2.83 million, professional fees of $1.44 million and software expense of $1.27 million.

The following chart presents revenue and expenses for the Banking segment (dollars in thousands):

	Year Ended December 31,			Increase/(Decrease)			
				2019 over 2018		2018 over 2017	
	2019	2018	2017	Amount	Percent	Amount	Percent
Revenue							
Net interest income	$ 351,969	$ 329,584	$ 251,003	$ 22,385	6.79 %	$ 78,581	31.31 %
Noninterest income							
Service charges on deposit accounts	10,544	11,808	10,594	(1,264)	(10.70)%	1,214	11.46 %
Credit card merchant fees	4,746	5,472	5,008	(726)	(13.27)%	464	9.27 %
Other income	19,620	16,977	14,046	2,643	15.57 %	2,931	20.87 %
Subtotal	34,910	34,257	29,648	653	1.91 %	4,609	15.55 %
Gain (loss) on investment securities	(845)	3	(1)	(848)	N/M	4	N/M
Total noninterest income	34,065	34,260	29,647	(195)	(0.57)%	4,613	15.56 %
Total revenue	386,034	363,844	280,650	22,190	6.10 %	83,194	29.64 %
Provision for loan losses	9,371	8,541	5,426	830	9.72 %	3,115	57.41 %
Expenses							
Salaries and employee benefits	131,149	114,472	85,654	16,677	14.57 %	28,818	33.64 %
Occupancy expense	20,419	17,410	16,365	3,009	17.28 %	1,045	6.39 %
Furniture and equipment	10,240	9,912	9,406	328	3.31 %	506	5.38 %
Amortization of intangible assets	5,160	5,658	2,288	(498)	(8.80)%	3,370	147.29 %
Other expenses	66,295	60,697	45,141	5,598	9.22 %	15,556	34.46 %
Total expenses	233,263	208,149	158,854	25,114	12.07 %	49,295	31.03 %
Income before income tax expense and corporate allocation	143,400	147,154	116,370	(3,754)	(2.55)%	30,784	26.45 %
Corporate allocation	2,011	1,736	1,828	275	15.84 %	(92)	(5.03)%
Income before income tax provision	145,411	148,890	118,198	(3,479)	(2.34)%	30,692	25.97 %
Provision for income tax expense	25,706	28,880	44,584	(3,174)	(10.99)%	(15,704)	(35.22)%
Net income	119,705	120,010	73,614	(305)	(0.25)%	46,396	63.03 %
Noncontrolling interest	2	(8)	1	10	N/M	(9)	N/M
Net income attributable to TowneBank	$ 119,707	$ 120,002	$ 73,615	$ (295)	(0.25)%	$ 46,387	63.01 %

Realty Segment: For the year ended December 31, 2019, the Realty segment represented 7.05%, or $9.78 million, of our total consolidated net income, compared to 4.80%, or $6.42 million, for 2018, and 8.39%, or $7.35 million, for 2017.

Earnings before income tax provision and noncontrolling interest for the year ended December 31, 2019, for the Realty segment were $17.20 million, increasing 46.87% from 2018. Total revenue decreased to $113.09 million in 2019 from $114.02 million in 2018.

Net residential mortgage banking income increased by $1.75 million to $68.44 million from 2018 primarily as a result of a $133.34 million increase in production volume. Residential mortgage banking income included an increase in the value of rate lock commitments and forward contracts of $2.49 million in 2019, as compared to an increase of $1.15 million in 2018. The increase in property management fees from 2018 was primarily due to increased revenue from additional rental properties. The decrease in net interest and other income primarily resulted from higher average funding costs on mortgage loans held for sale.

Expenses for the Realty segment decreased 6.41%, or $6.49 million, when compared to 2018. Salaries and benefits expense decreased $5.83 million, or 9.98%, professional fees decreased $0.62 million, or 38.56%, and furniture and equipment expense decreased $0.60 million, or 16.18%, when compared to 2018. These 2019 cost reductions were part of management focus on improved efficiencies that began late in 2018.

Earnings before income tax provision and noncontrolling interest for the year ended December 31, 2018, for the Realty segment were $11.71 million, decreasing 30.71% from 2017. Total revenue decreased to $114.02 million in 2018 from $118.04 million in 2017. Net residential mortgage banking income decreased by $9.55 million to $66.70 million from 2017, primarily as a result of a $334.4 million reduction in production volume. Residential mortgage banking income included an increase in the value of rate lock commitments and forward contracts of $1.15 million in 2018, as compared to an increase of $0.33 million in 2017. The increase in property management fees from 2017 was primarily due to increased revenue from additional rental properties. The increase in net interest and other income primarily resulted from a higher balance of average mortgage loans held for sale coupled with higher rates.

Expenses for the Realty segment increased 1.29%, or $1.29 million, when compared to 2017. Outside processing increased $0.64 million, or 36.81%, and software expense increased $0.47 million, or 19.35%, when compared to 2017.

The following chart presents revenue and expenses for the Realty segment (dollars in thousands):

	Year Ended December 31,			Increase/(Decrease)			
				2019 over 2018		2018 over 2017	
	2019	2018	2017	Amount	Percent	Amount	Percent
Revenue							
Residential mortgage banking income, net	$ 68,443	$ 66,696	$ 76,245	$ 1,747	2.62 %	$ (9,549)	(12.52)%
Real estate brokerage income, net	9,865	9,458	7,991	407	4.30 %	1,467	18.36 %
Title insurance and settlement fees	2,111	1,877	1,877	234	12.47 %	—	— %
Property management fees, net	24,427	22,405	19,496	2,022	9.02 %	2,909	14.92 %
Income from unconsolidated subsidiary	516	370	704	146	39.46 %	(334)	(47.44)%
Net interest and other income	7,724	13,210	11,725	(5,486)	(41.53)%	1,485	12.67 %
Total revenue	113,086	114,016	118,038	(930)	(0.82)%	(4,022)	(3.41)%
Expenses							
Salaries and employee benefits	52,619	58,450	58,586	(5,831)	(9.98)%	(136)	(0.23)%
Occupancy expense	8,285	7,871	8,171	414	5.26 %	(300)	(3.67)%
Furniture and equipment	3,099	3,697	3,865	(598)	(16.18)%	(168)	(4.35)%
Amortization of intangible assets	2,741	2,782	2,566	(41)	(1.47)%	216	8.42 %
Other expenses	27,982	28,416	26,742	(434)	(1.53)%	1,674	6.26 %
Total expenses	94,726	101,216	99,930	(6,490)	(6.41)%	1,286	1.29 %
Income before income tax, corporate allocation, and noncontrolling interest	18,360	12,800	18,108	5,560	43.44 %	(5,308)	(29.31)%
Corporate allocation	(1,163)	(1,091)	(1,210)	(72)	6.60 %	119	(9.83)%
Income before income tax provision and noncontrolling interest	17,197	11,709	16,898	5,488	46.87 %	(5,189)	(30.71)%
Provision for income tax	3,707	2,892	5,791	815	28.18 %	(2,899)	(50.06)%
Net income	13,490	8,817	11,107	4,673	53.00 %	(2,290)	(20.62)%
Noncontrolling interest	(3,711)	(2,398)	(3,756)	(1,313)	54.75 %	1,358	(36.16)%
Net income attributable to TowneBank	$ 9,779	$ 6,419	$ 7,351	$ 3,360	52.34 %	$ (932)	(12.68)%

The following chart shows key data for the Realty segment (dollars in thousands):

	Year Ended December 31,			Increase/(Decrease)			
				2019 over 2018		2018 over 2017	
	2019	2018	2017	Amount	Percent	Amount	Percent
Key data							
Number of units sold	4,822	4,864	4,388	(42)	(0.86)%	476	10.85 %
Volume of units sold	$1,589,753	$1,482,919	$1,342,828	$ 106,834	7.20 %	$ 140,091	10.43 %
Number of real estate agents	407	411	414	(4)	(0.97)%	(3)	(0.72)%
Loans originated, mortgage	$2,273,483	$2,114,558	$2,580,913	$ 158,925	7.52 %	$ (466,355)	(18.07)%
Loans originated, joint ventures	884,997	911,475	779,558	(26,478)	(2.90)%	131,917	16.92 %
Total loans originated	$3,158,480	$3,026,033	$3,360,471	$ 132,447	4.38 %	$ (334,438)	(9.95)%
Number of loans, mortgage	7,729	7,656	9,887	73	0.95 %	(2,231)	(22.56)%
Number of loans, joint ventures	3,714	4,006	3,561	(292)	(7.29)%	445	12.50 %
Total number of loans	11,443	11,662	13,448	(219)	(1.88)%	(1,786)	(13.28)%
Average loan amount, mortgage	$ 294	$ 276	$ 261	$ 18	6.52 %	$ 15	5.75 %
Average loan amount, joint ventures	238	228	219	10	4.39 %	9	4.11 %
Average loan amount	$ 276	$ 259	$ 250	$ 17	6.56 %	$ 9	3.60 %
Number of originators, mortgage	155	213	232	(58)	(27.23)%	(19)	(8.19)%
Number of originators, joint ventures	62	80	78	(18)	(22.50)%	2	2.56 %
Number of originators	217	293	310	(76)	(25.94)%	(17)	(5.48)%

Mortgage. The loan volume for combined mortgage operations increased during the year ended December 31, 2019, as compared to 2018. Total loans originated in 2019 were $3.16 billion, a 4.38%, or $0.13 billion, increase from $3.03 billion in 2018, which was a $0.33 billion, or 9.95%, decrease compared to the 2017 volume of $3.36 billion. Refinance activity comprised 23.76% of loan volume for the year ended December 31, 2019, while purchases accounted for the remaining 76.24% in loan volume for the year. For the years ended December 31, 2018 and 2017, refinance volume was 11.53% and 15.85%, respectively, while purchase volume was 88.56% and 90.47%, respectively. The number of units originated declined by 219 in 2019 compared to 2018, but the average mortgage size increased by $16.54 thousand. Refinance activity increased during the year as 10-year U.S. Treasury rates dipped. Funding costs associated with our warehouse line have increased, creating margin compression.

Insurance Segment: The Insurance segment is comprised of property and casualty, group benefits, and travel divisions. The Insurance segment represented 6.70%, or $9.30 million, of our total consolidated net income in 2019 compared to 5.51%, or $7.37 million, in 2018.

Earnings before taxes and noncontrolling interest for the Insurance segment were $13.66 million in 2019, as compared to $11.40 million in 2018. The primary factors affecting earnings were increases in our property and casualty and benefits income related to new agency acquisitions and organic growth in 2019. There was an increase in total commissions and fees of $9.03 million, or 14.85%, over 2018, and an increase in contingency and bonus revenue of $1.42 million. Contingent revenue primarily consists of amounts received from various property and casualty insurance carriers. The carriers use several non-client-specific factors to determine the amount of the contingency payments. Such factors include the aggregate loss performance of insurance policies previously placed and the volume of business, among other things.

Earnings before taxes and noncontrolling interest for the Insurance segment were $11.40 million in 2018, as compared to $12.51 million in 2017. The primary factor affecting earnings was a one time accrual made prior to the accounting changes in 2018. With the adoption of ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606),* in 2018, we modified the timing for recognizing contingent commissions revenue.

The following chart presents revenue and expenses for the Insurance segment (dollars in thousands):

	Year Ended December 31,			Increase/(Decrease) 2019 over 2018		Increase/(Decrease) 2018 over 2017	
	2019	2018	2017	Amount	Percent	Amount	Percent
Commission and fee income							
Property and casualty	$ 50,380	$ 40,948	$ 35,694	$ 9,432	23.03 %	$ 5,254	14.72 %
Employee benefits	14,726	14,088	12,551	638	4.53 %	1,537	12.25 %
Travel insurance	4,085	5,123	4,668	(1,038)	(20.26)%	455	9.75 %
Specialized benefit services	672	673	657	(1)	(0.15)%	16	2.44 %
Total commissions and fees	69,863	60,832	53,570	9,031	14.85 %	7,262	13.56 %
Contingency and bonus revenue	6,307	4,888	6,322	1,419	29.03 %	(1,434)	(22.68)%
Other income	2,032	295	308	1,737	588.81 %	(13)	(4.22)%
Total revenue	78,202	66,015	60,200	12,187	18.46 %	5,815	9.66 %
Employee commission expense	13,379	11,209	9,646	2,170	19.36 %	1,563	16.20 %
Revenue, net of commission expense	$ 64,823	$ 54,806	$ 50,554	$ 10,017	18.28 %	$ 4,252	8.41 %
Salaries and employee benefits	35,152	28,916	25,209	6,236	21.57 %	3,707	14.71 %
Occupancy expense	2,677	2,363	2,319	314	13.29 %	44	1.90 %
Furniture and equipment	1,012	868	801	144	16.59 %	67	8.36 %
Amortization of intangible assets	4,469	3,269	2,803	1,200	36.71 %	466	16.63 %
Other expenses	7,003	7,343	6,298	(340)	(4.63)%	1,045	16.59 %
Total expenses	50,313	42,759	37,430	7,554	17.67 %	5,329	14.24 %
Income before income tax, corporate	14,510	12,047	13,124	2,463	20.44 %	(1,077)	(8.21)%
Corporate allocation	(848)	(645)	(618)	(203)	31.47 %	(27)	4.37 %
Income before income tax provision and	13,662	11,402	12,506	2,260	19.82 %	(1,104)	(8.83)%
Provision for income tax expense	3,183	2,455	4,438	728	29.65 %	(1,983)	(44.68)%
Net income	10,479	8,947	8,068	1,532	17.12 %	879	10.89 %
Noncontrolling interest	(1,182)	(1,575)	(1,371)	393	(24.95)%	(204)	14.88 %
Net income attributable to TowneBank	$ 9,297	$ 7,372	$ 6,697	$ 1,925	26.11 %	$ 675	10.08 %

Total revenue for the year ended December 31, 2019, increased $12.19 million, or 18.46%. The increase from the prior period was driven by an increase in property and casualty fee income of $9.43 million and was positively impacted by late 2018 and full year 2019 insurance agency acquisitions. The acquired insurance agencies contributed additional revenue, net of commission expense, of $7.28 million. Also contributing to the increase was improvement in commercial lines commissions due to organic growth and an increase in employee benefits commissions of $0.64 million. The Company goal is to grow insurance commissions to $100 million over the next three to five years.

Salaries and employee benefits expense increased $6.24 million, or 21.57%, when comparing 2019 to 2018, and increased $3.71 million, or 14.71%, when comparing 2018 to 2017. The increases were mainly driven by insurance agency acquisitions, which resulted in additional salaries and employee benefit expenses of $4.12 million and $1.26 million for 2019 and 2018, respectively.

Occupancy expense increased $0.31 million, or 13.29%, when comparing 2019 to 2018, and increased $0.04 million, or 1.90%, when comparing 2018 to 2017, largely as a result of the insurance agency acquisitions.

Amortization of intangible assets increased by $1.20 million, or 36.71%, during the year ended December 31, 2019, compared to 2018, and increased $0.47 million, or 16.63%, when comparing 2018 to 2017, which was also a result of the acquisitions.

ANALYSIS OF FINANCIAL CONDITION

Overview: Our total assets increased $0.78 billion, or 7.03%, to $11.95 billion at December 31, 2019, from $11.16 billion at December 31, 2018. Our loan portfolio grew by 5.00%, or $0.40 billion, to $8.42 billion at December 31, 2019, from $8.02 billion at December 31, 2018.

Our total average assets were $11.64 billion for 2019, reflecting an increase of $1.04 billion, or 9.80%, compared to the 2018 average of $10.60 billion. Total average assets for 2018 increased $2.26 billion, or 27.16%, compared to the 2017 average of $8.33 billion. Average earning assets were $10.43 billion in 2019, reflecting an increase of $0.92 billion, or 9.72%, compared to 2018.

Our average total deposits were $8.95 billion in 2019, reflecting growth of $1.12 billion, or 14.35%, compared to 2018. Growth continued in average noninterest-bearing deposits, which increased $327.01 million, or 12.99%.

Securities: Our securities consist of AFS securities and HTM securities. Our AFS securities portfolio, which is held primarily for earnings, liquidity, and asset/liability management purposes, is reported at fair value based on market prices for similar instruments. Our HTM securities portfolio, which is held primarily for yield and pledging purposes, is valued at amortized cost. Our investment portfolio totaled $1.52 billion as of December 31, 2019, with a balance of $1.44 billion in AFS, $43.69 million in HTM, $6.46 million in other equity securities, and $30.09 million in FHLB stock. Average yield on AFS securities was 2.67% at December 31, 2019, compared with 2.56% at December 31, 2018, and 1.61% at December 31, 2017. Average yield on HTM securities was 3.22% at December 31, 2019, compared to 3.23% at December 31, 2018, and 3.26% at December 31, 2017.

Our AFS securities portfolio consists of U.S. agency securities, municipal securities, MBSs, and trust preferred corporate obligations. Our HTM portfolio consists of MBSs, municipal securities, and trust preferred corporate obligations. Our investment activities are governed internally by a written and Board-approved investment policy, which is administered by our ALCO, which generally meets quarterly to review the economic environment, to assess current activities for appropriateness, and to establish investment strategies.

Investment strategies are established by the ALCO in consideration of the interest rate cycle, balance sheet mix, actual and anticipated loan demand, funding options, and our overall interest rate sensitivity. In general, the investment portfolio is managed in a manner appropriate with the attainment of the following goals: (i) to provide a sufficient margin of liquid assets to cover unanticipated deposit and loan fluctuations, seasonal funds flow variations, and overall funds management objectives; (ii) to provide eligible securities to secure public funds, trust deposits, and repurchase agreements as prescribed by law; and (iii) to earn the maximum return on funds invested that is commensurate with meeting the requirements of (i) and (ii).

The following table provides information regarding the composition of our securities portfolio, showing selected maturities and yields (dollars in thousands). For more information, refer to Note 3, Investment Securities, in the Notes to Consolidated Financial Statements.

	Year Ended December 31,								
	2019			2018			2017		
	Amortized Cost	Estimated Fair Value	Weighted Average Yield	Amortized Cost	Estimated Fair Value	Weighted Average Yield	Amortized Cost	Estimated Fair Value	Weighted Average Yield
Securities Available for Sale:									
U.S. agency securities	$ 128,451	$ 129,038	2.22%	$ 362,272	$ 358,542	1.88%	$ 277,062	$ 274,468	1.40%
U.S. Treasury notes	1,000	1,000	2.56%	1,247	1,246	2.11%	301,472	301,497	1.03%
Municipal securities	217,911	223,106	2.94%	87,044	87,308	3.21%	17,495	17,487	2.59%
Trust preferred corporate securities	51,724	53,367	4.72%	30,498	30,992	4.94%	22,799	23,364	4.97%
Mortgage-backed securities	1,022,487	1,034,797	2.57%	626,188	617,251	2.76%	253,737	249,322	2.16%
Total securities available for sale	1,421,573	1,441,308	2.67%	1,107,249	1,095,339	2.56%	872,565	866,138	1.61%
Securities Held to Maturity:									
Trust preferred corporate securities	2,369	2,599	3.42%	500	676	8.75%	500	731	8.75%
Municipal securities	29,167	30,388	3.70%	34,488	35,541	3.69%	40,825	42,572	3.80%
Mortgage-backed securities	12,152	12,184	2.05%	15,610	15,051	2.04%	19,979	19,582	2.01%
Total securities held to maturity	43,688	45,171	3.22%	50,598	51,268	3.23%	61,304	62,885	3.26%
Total Portfolio	$ 1,465,261	$ 1,486,479	2.69%	$ 1,157,847	$ 1,146,607	2.59%	$ 933,869	$ 929,023	1.72%

The following table indicates the maturities of securities at December 31, 2019 (dollars in thousands):

	Available for Sale			Held to Maturity		
	Amortized Cost	Fair Market Value	Weighted Average Yield	Amortized Cost	Fair Market Value	Weighted Average Yield
U.S. Treasury & U.S. agency securities						
Due in one year or less	$ 56,003	$ 56,000	1.75%	$ —	$ —	—
After one year through five years	24,619	25,115	2.35%	—	—	—
After five years through ten years	30,311	30,252	2.65%	—	—	—
After ten years	18,518	18,671	2.80%	—	—	—
Municipal securities						
Due in one year or less	3,489	3,494	1.91%	—	—	—
After one year through five years	12,332	12,496	2.62%	11,693	11,813	3.15%
After five years through ten years	108,810	111,795	2.97%	10,500	10,934	3.96%
After ten years	93,280	95,321	3.00%	6,974	7,641	4.22%
Mortgage-backed securities						
Due in one year or less	899	898	1.95%	—	—	—
After one year through five years	20,903	21,440	2.83%	5,640	5,632	1.47%
After five years through ten years	470,425	472,705	2.38%	5,907	5,890	2.11%
After ten years	530,260	539,754	2.73%	605	662	6.79%
Trust preferred corporate securities						
Due in one year or less	—	—	—	—	—	—
After one year through five years	—	—	—	—	—	—
After five years through ten years	51,724	53,367	4.72%	—	—	—
After ten years	—	—	—	2,369	2,599	3.42%
Total Portfolio	$ 1,421,573	$ 1,441,308	2.67%	$ 43,688	$ 45,171	3.22%

Loans Held for Sale: At December 31, 2019, we held $419.23 million in mortgage loans originated and intended for sale in the secondary market, compared with $220.99 million at December 31, 2018. Average loans held for sale were 3.22% and 3.08% of average earning assets for the years ended December 31, 2019 and 2018, respectively.

Our mortgage banking activities include two types of commitments: rate lock commitments and forward loan commitments. Rate lock commitments are loans in our pipeline that have an interest rate locked with the customer. The commitments are generally for periods of 60 days and are at market rates. In order to mitigate the effect of the interest rate risk inherent in providing rate lock commitments, we enter into either a forward loan sales contract under best efforts delivery, or a trade of TBA MBS ("notional securities") for mandatory delivery. When the interest rate is locked with the borrower, the rate lock commitment and MBS position are undesignated derivatives and marked to fair value through earnings. The fair value of the rate lock derivative is based on quoted prices for similar loans in the secondary market adjusted by a factor which considers the likelihood that the loan in a lock position will ultimately close. Both the rate lock commitment and the corresponding TBA MBS are considered derivatives, but are not accounted for using hedge accounting. As such, changes in the estimated fair value of the derivatives during the commitment period are recorded in current earnings and included in net residential mortgage banking income in the Consolidated Statements of Income.

Loan Portfolio: Our loan portfolio, net of unearned income and deferred costs, totaled $8.42 billion on December 31, 2019. As a percentage of total average earning assets, average loans were 77.88% in 2019, compared with 79.62% in 2018 and 78.50% in 2017. Lending activities represent our primary source of income. Management expects annualized loan growth to be in the mid-single digits for 2020. The following tables provide the balance and composition of the loan portfolio by major classification for the periods indicated (dollars in thousands):

Year Ended December 31,	2019	2018	2017	2016	2015
Real estate loans					
1-4 family residential	$ 1,653,084	$ 1,626,896	$ 1,217,349	$ 1,215,823	$ 973,331
Commercial	3,512,376	3,241,340	2,283,541	2,251,312	1,784,393
Construction and land development	1,120,533	1,067,239	930,426	826,027	598,875
Multi-family	243,041	260,987	198,720	222,791	167,371
Total real estate loans	6,529,034	6,196,462	4,630,036	4,515,953	3,523,970
Commercial and industrial loans	1,574,275	1,510,364	1,087,157	1,089,539	857,036
Consumer loans and other	315,979	311,407	229,772	201,729	138,387
Loans, net of unearned income and deferred costs	$ 8,419,288	$ 8,018,233	$ 5,946,965	$ 5,807,221	$ 4,519,393

Year Ended December 31,	2019	2018	2017	2016	2015
Real estate loans					
1-4 family residential	19.63%	20.29%	20.47%	20.94%	21.54%
Commercial	41.72%	40.43%	38.40%	38.77%	39.48%
Construction and land development	13.31%	13.31%	15.65%	14.22%	13.25%
Multi-family	2.89%	3.25%	3.34%	3.84%	3.70%
Total real estate loans	77.55%	77.28%	77.86%	77.77%	77.97%
Commercial and industrial loans	18.70%	18.84%	18.28%	18.76%	18.97%
Consumer loans and other	3.75%	3.88%	3.86%	3.47%	3.06%
Loans, net of unearned income and deferred costs	100.00%	100.00%	100.00%	100.00%	100.00%

The table below provides the maturity and sensitivity of the loan portfolio at December 31, 2019 (in thousands):

					Due After One Year	
	Due in One Year or Less	Due After One Year Through Five Years	Due After Five Years	Totals	Fixed Rates	Adjustable Rates
Real estate loans						
1-4 family residential	$ 105,374	$ 254,556	$ 1,293,154	$ 1,653,084	$ 718,448	$ 829,262
Commercial	228,492	1,029,700	2,254,184	3,512,376	2,948,554	335,330
Construction and land development	609,799	370,373	140,361	1,120,533	195,838	314,896
Multifamily	10,555	79,831	152,655	243,041	201,797	30,689
Total real estate loans	954,220	1,734,460	3,840,354	6,529,034	4,064,637	1,510,177
Commercial and industrial loans	605,505	417,861	531,160	1,554,526	771,500	177,521
Consumer loans and other	38,219	205,340	92,169	335,728	283,075	14,434
Loans, net of unearned income and deferred costs	$ 1,597,944	$ 2,357,661	$ 4,463,683	$ 8,419,288	$ 5,119,212	$ 1,702,132

The following table is a summary of our floating rate loan portfolio and contractual interest rate indices at December 31, 2019 (in thousands):

Contractual Interest Rate Index	Floating Rate (at floor rate)	Floating Rate (not at floor or ceiling rate)	Floating Rate (at ceiling rate)	Total Floating Rate	Percentage of Floating Rate Loans
Wall Street Journal Prime	$ 173,998	$ 1,303,315	$ 3,245	$ 1,480,558	53.2%
LIBOR	173,858	698,718	—	872,576	31.4%
Other contractual interest rate indices	3,031	425,055	—	428,086	15.4%
	$ 350,887	$ 2,427,088	$ 3,245	$ 2,781,220	100.0%

At December 31, 2019, the majority of our floating rate loans are tied to LIBOR interest rates or Wall Street Journal Prime interest rates. LIBOR is the global benchmark rate supporting a diverse range of financial activities in the U.S. and abroad. The Financial Conduct Authority, which is the governing body responsible for collecting and communicating LIBOR rates, has announced they will cease their activities in 2021. Transition to another benchmark is expected to have a financial impact on the banking industry, as a whole. The full impact of the transition cannot be determined at this time.

Allowance for Loan Losses: The allowance for loan losses is established through a provision for loan losses charged against earnings. The level of the allowance for loan losses is based on management's evaluation of the risk inherent in the loan portfolio at the balance sheet date and changes in the nature and volume of loan activity. This evaluation includes a review of loans for which collection may not be reasonably assured. It considers internal risk grades, the estimated fair value of the underlying collateral, current economic conditions, historical loan loss experience, and other current factors that warrant consideration in determining an adequate allowance.

The allowance for loan losses consists of three elements: (i) specific valuation allowances determined in accordance with ASC 310, *Receivables*, based on probable losses on specific loans; (ii) historical valuation allowances determined in accordance with ASC 450, *Contingencies*, based on historical loan loss experience for similar loans with similar characteristics and trends, adjusted, as necessary, to reflect the impact of current conditions; and (iii) general valuation allowances determined in accordance with ASC 450 based on general economic conditions and other qualitative risk factors both internal and external to the Company.

Our policy is to establish internal risk grades to all loans as a component of the approval process. Based on the size of the loan, senior credit officers, regional credit administrators, and the chief credit officer review the classification to ensure accuracy and consistency of classifications, which are then validated by the internal loan review process. Loan classifications are internally reviewed to determine if any changes in the circumstances of the loan require a different risk grade. To determine the most appropriate risk grade classification for each loan, the credit officers examine the borrower's liquidity level, asset quality, the amount of the borrower's other indebtedness, cash flow, earnings, sources of financing, and existing lending relationships. The allowances established for probable losses on specific loans are based on a regular analysis and evaluation of classified loans.

Historical valuation allowances are calculated based on the historical loss experience of specific types of loans. We calculate historical loss ratios for pools of similar loans with similar characteristics based on the proportion of actual charge-offs experienced to the total population of loans in the pool. Historical loss ratios are updated quarterly based on actual charge-off experience. An historical valuation allowance is established for each pool of similar loans based upon the product of the historical loss ratio and the total dollar amount of the loans in the pool. Our pools of similar loans include groups of construction and land development loans, commercial real estate loans, commercial and industrial business loans, 1-4 family residential real estate loans, multifamily real estate loans, and consumer and other loans.

General valuation allowances are based on general economic conditions and other qualitative risk factors both internal and external to TowneBank. In general, such valuation allowances are determined by evaluating, among other things: (i) the experience, ability, and effectiveness of the Company's lending management and staff; (ii) the effectiveness of the Company's loan policies, procedures, and internal controls; (iii) changes in asset quality; (iv) changes in loan portfolio volume; (v) the composition and concentrations of credit; (vi) the effectiveness of the internal loan review function; (vii) the impact of national economic trends on portfolio risks; and (viii) the impact of local economic trends on portfolio risk. Management evaluates the degree of risk that each one of these components has on the quality of the loan portfolio on a quarterly basis to determine an appropriate general valuation allowance.

Loans 30 to 89 days past due totaled $10.64 million, or 0.13% of total loans, including purchased impaired loans of $0.46 million, at December 31, 2019, down from $14.33 million, or 0.18% of total loans, at December 31, 2018. Total past due and nonaccruing loans were $28.69 million, or 0.34% of total loans, including purchased impaired past-due loans of $0.76 million, at December 31, 2019, compared to $20.20 million, or 0.25% of total loans, at December 31, 2018.

The allowance for loan losses at December 31, 2019, 2018, and 2017, was $58.23 million, $52.09 million, and $45.13 million, respectively. The allowance was equal to 0.69% of total loans outstanding at December 31, 2019, compared with 0.65% at December 31, 2018, and 0.76% at December 31, 2017. Excluding purchased loans, the allowance was equal to 0.81% of total loans outstanding at December 31, 2019, compared with 0.82% at December 31, 2018, and 0.86% at December 31, 2017. We believe the slight decline in the ratio, excluding purchased loans, is appropriate given the risk profile of our loan portfolio and diversification efforts in the loan portfolio. Reflective of strong credit quality, classified loans, defined as loans in the substandard and doubtful categories, remained low at 0.55% of total loans at December 31, 2019, down from 0.57% at December 31, 2018. Also reflecting the credit quality of our loan portfolio and supporting the adequacy of coverage levels of the allowance for loan losses, the allowance was equal to 3.34x of nonperforming loans at December 31, 2019, compared with 10.97x at December 31, 2018. We believe our allowance for loan losses is adequate to cover loan losses inherent in the loan portfolio at December 31, 2019.

The following table provides a summary of the activity in the allowance for loan losses for the periods indicated (dollars in thousands):

Year Ended December 31,	2019	2018	2017	2016	2015
Balance beginning of period	$ 52,094	$ 45,131	$ 42,001	$ 38,359	$ 35,917
Loans charged off:					
Real estate - residential 1-4 family	(1,098)	(1,102)	(2,291)	(1,448)	(1,443)
Real estate - multi-family	—	—	—	—	—
Real estate -commercial	(1,298)	(168)	(139)	(399)	(279)
Real estate - construction and development	(43)	(72)	—	(107)	(208)
Commercial and industrial	(984)	(716)	(345)	(481)	(122)
Consumer and other loans	(1,068)	(748)	(644)	(459)	(109)
Total	(4,491)	(2,806)	(3,419)	(2,894)	(2,161)
Loans recovered:					
Real estate - residential 1-4 family	635	531	286	716	636
Real estate - multi-family	—	—	2	2	1
Real estate -commercial	38	32	339	59	244
Real estate - construction and development	144	74	34	110	80
Commercial and industrial	148	263	82	121	493
Consumer and other loans	295	328	380	171	122
Total	1,260	1,228	1,123	1,179	1,576
Net loans charged off	(3,231)	(1,578)	(2,296)	(1,715)	(585)
Provision for loan losses	9,371	8,541	5,426	5,357	3,027
Balance end of period	$ 58,234	$ 52,094	$ 45,131	$ 42,001	$ 38,359
Nonperforming assets:					
Nonperforming loans	$ 17,437	$ 4,749	$ 4,807	$ 13,099	$ 8,670
Former bank premises	1,521	2,253	3,469	3,494	—
Foreclosed property	13,839	17,163	19,818	21,011	34,420
Total nonperforming assets	$ 32,797	$ 24,165	$ 28,094	$ 37,604	$ 43,090
Loans past due 90 days accruing interest	$ 309	$ 394	$ 103	$ 76	$ 424
Asset Quality Ratios					
Allowance for loan losses to nonperforming loans	3.34x	10.97x	9.39x	3.21x	4.42x
Allowance to nonperforming assets	1.78x	2.16x	1.61x	1.12x	.89x
Allowance for loan losses to period end loans	0.69%	0.65%	0.76%	0.72%	0.85%
Allowance for loan losses to period end loans excluding purchased loans	0.81%	0.82%	0.86%	0.87%	0.94%
Nonperforming loans to period end loans	0.21%	0.06%	0.08%	0.23%	0.19%
Nonperforming assets to period end assets	0.27%	0.22%	0.33%	0.47%	0.68%
Net charge-offs to average loans	0.04%	0.03%	0.04%	0.03%	0.01%

Nonperforming assets consist of nonaccrual loans, former bank premises, foreclosed real estate, and other repossessed collateral. Our policy is to place commercial loans on nonaccrual status when full collection of principal and interest becomes doubtful, or when any portion of principal or interest becomes 90 days past due, whichever occurs first, unless the debt is both well-secured and in the process of collection. When loans are placed on nonaccrual status, interest receivable is reversed against interest income recognized in the current period, and any prior year unpaid interest is charged off against the allowance for loan losses. Interest payments received thereafter are applied as a reduction of the remaining principal balance so long as doubt exists as to the ultimate collection of the principal. Loans are removed from nonaccrual status when they become current as to both principal and interest and when the collection of principal or interest is no longer doubtful. Similarly, residential mortgage loans and other consumer loans are also placed on nonaccrual status when full collection of principal and interest becomes doubtful, or when any portion of principal or interest becomes 120 days past due, whichever occurs first, unless the debt is both well-secured and in the process of collection.

At December 31, 2019, we had $32.80 million in nonperforming assets, which amounted to 0.27% of total assets. Nonperforming assets consist of $17.44 million in nonperforming loans, $1.52 million in former bank premises related to the Monarch merger, as well as $13.84 million in foreclosed property. Nonperforming loans increased by $12.69 million from December 31, 2018, driven principally by the migration of one credit relationship to nonaccrual status. At December 31, 2019, foreclosed property totaled $13.84 million, a decrease from $17.16 million at December 31, 2018. Foreclosed property consists of six residential properties, 12 construction and development properties, and one commercial properties. The five largest foreclosed property developments represented approximately 96.01% of total foreclosed property at December 31, 2019, with the largest development representing approximately 44.94%.

At December 31, 2019, loans 60 to 89 days delinquent, excluding nonperforming loans, totaled $1.05 million. Additionally, there are other performing loans, totaling $19.08 million, that are current but have certain documentation deficiencies or other potential weaknesses that management believes warrant additional monitoring. All loans in these categories are subject to constant management attention, and their status is reviewed on a regular basis.

In order to maximize collection of loan balances, we evaluate troubled loan accounts on a case-by-case basis to determine if a loan modification would be appropriate. We may pursue loan modifications when there is a reasonable chance that an appropriate modification would allow our clients to continue servicing the debt. Because some TDRs may not ultimately result in the complete collection of principal and interest (as modified by the terms of the restructuring), additional incremental losses could result. These potential incremental losses have been factored into our overall allowance for loan losses estimate.

At December 31, 2019, nonaccruing TDRs, which are included in nonperforming loans, totaled $2.27 million, and accruing TDRs totaled $15.02 million. Nonaccruing loans that are modified can be placed back on accrual status when both principal and interest are current, there is a sustained repayment performance of six months or greater, and it is probable that we will be able to collect all amounts due (both principal and interest) according to the terms of the loan agreement. All restructured loans are considered impaired in the calendar year of restructuring. In subsequent years, a restructured loan may cease being classified as impaired if the loan was modified at a market rate and has performed according to the modified terms for at least six months.

The following table provides information on the composition of nonperforming loans by loan type (in thousands):

	December 31, 2019	December 31, 2018
Real estate - residential 1-4 family	$ 5,973	$ 1,954
Real estate - commercial	7,513	538
Real estate - construction and development	43	—
Commercial and industrial loans	3,284	1,820
Consumer and other loans	624	437
Total nonperforming loans	$ 17,437	$ 4,749

Allocation of the Allowance for Loan Losses: At December 31, 2019, all of the allowance for loan losses was allocated to specific loan categories. Management monitors whether or not the allowance for loan loss allocation model, as a whole, calculates an appropriate level of allowance for loan losses that moves in direct correlation to the general macroeconomic and loan portfolio conditions the Company experiences over time. This allocation of the allowance for loan losses is calculated on an approximate basis and is not intended as an indication of the specific amounts, by loan classification, to be charged to the allowance. The entire amount of the allowance is available to absorb losses occurring in any category of loans. The following table provides a breakdown of the allowance for loan losses among the various loan types for the periods indicated (in thousands):

Year Ended December 31,	**2019**	**2018**	**2017**	**2016**	**2015**
Real estate loans:					
1-4 family residential	$ 10,623	$ 10,245	$ 9,345	$ 9,050	$ 8,990
Commercial	23,241	19,488	16,864	16,248	14,687
Construction	6,926	6,171	5,753	4,280	4,984
Multi-family	1,047	1,011	1,075	1,370	945
Total real estate loans	41,837	36,915	33,037	30,948	29,606
Commercial and industrial loans	9,836	8,669	6,596	6,410	5,774
Consumer and other loans	6,561	6,510	5,498	4,643	2,979
Total	$ 58,234	$ 52,094	$ 45,131	$ 42,001	$ 38,359

In the opinion of management, the allowance was adequate at December 31, 2019, based on known conditions. However, the allowance may be increased or decreased in the future based on loan balances outstanding, changes in internally generated credit quality ratings of the loan portfolio, changes in the value of collateral, and changes in general economic conditions and other risk factors.

Allowance for Loan Losses Policy and Methodology: Our allowance for loan loss methodology is based on guidance provided by various regulatory agencies and includes allowance allocations calculated in accordance with ASC 310, *Receivables*, and allowance allocations calculated in accordance with ASC 450, *Contingencies*. Accordingly, the methodology is based on historical loss experience by type of credit and internal risk grade, specific homogeneous risk pools, and specific loss allocations, with adjustments for current events and conditions. The Company's process for determining the appropriate level of the allowance for possible loan losses is designed to account for credit deterioration as it occurs. Our objective is to maintain a loan portfolio that is diverse in terms of loan type, industry concentration, and borrower concentration in order to reduce overall credit risk by minimizing the adverse impact of any single event or combination of related events.

Commercial lending may involve a higher degree of risk as compared to other types of lending because repayment usually depends on the cash flows generated by a borrower's business, and the debt service capacity of a business can deteriorate because of downturns in national and local economic conditions. Additionally, construction and development lending involves an elevated degree of risk because loans are generally made to builders for specific construction projects, and successful repayment of these types of loans is generally dependent upon the sale of the constructed property. To control risk, initial and continuing financial analysis of a borrower's financial information is required. While management uses the best information available to establish the allowance for loan losses, future adjustments to the allowance methodology may be necessary if economic conditions differ substantially from the assumptions used in making the valuations, or if required by regulators based upon information at the time of their examinations. Such adjustments to original estimates, as necessary, are made in the period in which these factors and other relevant considerations indicate that loss levels may vary from previous estimates.

Deposits: Customer deposits are attractive sources of liquidity because of their stability, low average cost, and the ability to generate fee income through the cross-sale of other services to depositors. Deposits are attracted principally from customers within our market area through the offering of a broad selection of deposit instruments, including demand deposits, savings accounts, money rate savings, certificates of deposit, and individual retirement accounts. Deposit account terms vary with respect to the minimum balance required, the time period the funds must remain on deposit, and service charge schedules.

Interest rates paid on specific deposit types are set by considering the (i) interest rates offered by competitors, (ii) anticipated amount and timing of funding needs, (iii) availability of and cost of alternative sources of funding, and (iv) anticipated future economic conditions and interest rates.

Deposit accounts held as of December 31, 2019, totaled $9.27 billion. This represented an increase of $0.90 billion, or 10.76%, over 2018, which was $1.92 billion, or 29.81%, over 2017. Deposit accounts represent our primary source of funds and are provided by individuals, professionals, and small- to medium-sized businesses in our market area. The deposits consist of demand deposits, interest-bearing checking accounts, money market deposit accounts, and time deposits. Some of our interest-bearing deposits were obtained through brokered transactions and our participation in CDARS. We had brokered time deposits of $331.52 million and CDARS deposits of $119.75 million at December 31, 2019, and $319.70 million and $115.19 million, respectively, at December 31, 2018.

The following table provides the average balance and cost rate of interest-bearing deposits for the periods indicated (dollars in thousands). The aggregate amount of time deposits of $250,000 or more was $905.37 million and $742.85 million at December 31, 2019 and 2018, respectively. See Note 10, Deposits, in the Notes to Consolidated Financial Statements for additional information on deposits.

	Average Balance			Average Cost Rate		
For the Year Ended December 31,	**2019**	**2018**	**2017**	**2019**	**2018**	**2017**
Noninterest-bearing demand deposits	$ 2,844,178	$ 2,517,173	$ 2,094,753	—	—	—
Demand and money markets	3,351,135	2,951,038	2,260,378	0.80%	0.56%	0.35%
Savings	280,894	302,435	319,940	1.17%	1.26%	1.03%
Certificates of deposit:						
Less than $250,000	1,609,151	1,380,611	1,143,687	2.07%	1.60%	1.03%
$250,000 or more	869,512	679,976	524,566	2.62%	1.58%	1.09%
Total interest-bearing deposits	6,110,692	5,314,060	4,248,571	1.41%	1.00%	0.68%
Total deposits	$ 8,954,870	$ 7,831,233	$ 6,343,324	0.96%	0.68%	0.45%

Average noninterest-bearing demand deposits were 31.76% of average total deposits during the year ended December 31, 2019, and 32.14% and 33.02% during 2018 and 2017, respectively. The average cost of interest-bearing deposits was 1.41% for the year ended December 31, 2019, compared with 1.00% for 2018, and 0.68% for 2017.

Advances from the Federal Home Loan Bank: Our ability to borrow funds through nondeposit sources provides additional flexibility in meeting the liquidity needs of customers while enhancing our cost of funds structure. Average funds borrowed from the FHLB were $559.66 million and $849.99 million for the years ended December 31, 2019 and 2018, respectively. The balance at December 31, 2019, of $471.69 million, decreased $327.63 million from the balance at December 31, 2018, of $799.32 million. Refer to Note 11, Borrowings, in the Notes to Consolidated Financial Statements for additional disclosures related to borrowing arrangements.

Subordinated Debt: On July 17, 2017, the Company issued $250.0 million of fixed-to-floating rate subordinated notes due July 30, 2027, in a public offering. The Company received $247.07 million in net proceeds after deducting discounts and issuance costs. The subordinated notes accrue interest at a fixed rate of 4.50% for the first five years until July 30, 2022. From and including this date and for the remaining five years of the subordinated notes' term, interest will accrue at a floating rate of three-month LIBOR plus 2.55%. The Company may redeem the subordinated notes, in whole or in part, on or after July 30, 2022. At December 31, 2019, the carrying value of the notes totaled $248.46 million and average subordinated debt during 2019 was $248.14 million, while the average cost of the debentures was 4.77%. At December 31, 2018, the carrying value of the notes totaled $247.86 million and average subordinated debt during 2018 was $251.10 million, while the average cost of the debentures was 4.81%.

Liquidity: Liquidity represents our ability to provide funds to meet customer demand for loan and deposit withdrawals without impairing profitability. Our liquid assets consist of cash, interest-bearing deposits in financial institutions, federal funds sold, and investments and loans maturing within one year. Asset liquidity is also provided by managing both loan and security maturities.

We maintained an average of $665.90 million outstanding in overnight interest-bearing deposits during 2019, compared with $560.37 million for 2018. We intend to maintain sufficient liquidity at all times to meet our funding commitments and growth plans. During 2019, we primarily funded our growth in total assets with deposit growth.

Capital Resources: Federal banking laws set forth certain regulatory capital requirements that apply to us. Within the framework established by the law, we qualify for the classification "well-capitalized," which is the highest regulatory classification.

Additional information concerning our capital resources is contained in Note 18, Regulatory Capital Requirements, in the Notes to Consolidated Financial Statements.

Contractual Obligations, Contingent Liabilities, and Commitments: The following table summarizes our significant contractual obligations, contingent liabilities, and certain other commitments outstanding as of December 31, 2019 (in thousands):

	Payments Due by Period				
Contractual Obligations	**Total**	**Less Than 1 Year**	**1 - 3 years**	**3 - 5 years**	**More Than 5 Years**
Operating lease obligations	$ 69,063	$ 10,626	$ 15,463	$ 9,985	$ 32,989
Other long-term liabilities reflected on the registrant's balance sheet under GAAP					
FHLB advances	471,687	365,000	100,000	—	6,687
Other commitments					
Standby letters of credit	140,630	140,630	—	—	—
Commitments to extend credit	3,094,615	2,443,244	651,371	—	—
Total contractual obligations	$ 3,775,995	$ 2,959,500	$ 766,834	$ 9,985	$ 39,676

Impact of Inflation and Changing Prices: The financial statements and related data presented herein have been prepared in accordance with GAAP. These principles dictate that financial position and operating results be measured in terms of historical dollars, without considering changes in the relative purchasing power of money over time due to inflation. A financial institution's assets and liabilities are primarily monetary in nature. As a result, general levels of inflation typically have a less significant effect on financial performance than do changes in interest rates; however, noninterest expenses tend to rise in periods of general inflation.

Return on Equity and Assets: The annualized ratio of operating income to average total assets and average shareholders' equity and average equity to average assets for the periods indicated are as follows:

Year Ended December 31,	**2019**	**2018**	**2017**
Return on average assets	1.19%	1.26%	1.05%
Return on average equity	8.69%	9.20%	7.80%
Return on average tangible equity	13.58%	14.52%	11.35%
Average equity to average assets	13.72%	13.73%	13.48%

Interest Sensitivity: Prudent balance sheet management requires processes that monitor and protect us against unanticipated or significant changes in the level of market interest rates. Net interest income stability should be maintained in changing rate environments by ensuring that interest rate risk is kept to an acceptable level. The ability to reprice our interest-sensitive assets and liabilities over various time intervals is of critical importance.

We use a variety of traditional and on-balance-sheet tools to manage our interest rate risk. Gap analysis, which monitors the "gap" between interest-sensitive assets and liabilities, is one such tool. In addition, we use simulation modeling to forecast future balance sheet and income statement behavior. By studying the effects on net interest income of rising, stable, and falling interest rate scenarios, we can position ourselves to take advantage of anticipated interest rate movement, and protect ourselves from unanticipated rate movements, by understanding the dynamic nature of our balance sheet components.

An asset-sensitive balance sheet structure implies that assets, such as loans and securities, will reprice faster than liabilities; consequently, net interest income should be positively affected in an increasing interest rate environment. Conversely, a liability-sensitive balance sheet structure implies that liabilities, such as deposits, will reprice faster than assets; consequently, net interest income should be positively affected in a decreasing interest rate environment. At December 31, 2019, we had $0.75 billion more assets than liabilities subject to repricing within one year and, therefore, were in an asset-sensitive position.

Market Risk Management: The effective management of market risk is essential to achieving our strategic objectives. As a financial institution, our most significant market risk exposure is interest rate risk. The primary objective of the management of interest rate risk is to minimize the effect that changes in interest rates have on net interest income. This is accomplished through active management of asset and liability portfolios, with a focus on the strategic pricing of asset and liability accounts and management of appropriate maturity mixes of assets and liabilities. The goal of these activities is the development of appropriate maturity and repricing opportunities in our portfolios of assets and liabilities that will produce consistent net interest income during periods of changing interest rates. Our ALCO monitors loan, investment, and liability portfolios to ensure comprehensive management of interest rate risk. These portfolios are analyzed for proper fixed-rate and variable-rate mixes under various interest rate scenarios.

The asset and liability management process is designed to achieve relatively stable net interest margins and assure liquidity by coordinating the volumes, maturities, and/or repricing opportunities of earning assets, deposits, and borrowed funds. It is the responsibility of the ALCO to determine and achieve the most appropriate volume and mix of earning assets and interest-bearing liabilities, as well as ensure an adequate level of liquidity and capital within the context of corporate performance goals. The ALCO also sets policy guidelines and establishes long-term strategies with respect to interest rate risk exposure and liquidity. The ALCO meets regularly to review our interest rate risk and liquidity positions in relation to present and prospective market and business conditions. In addition, funding and balance sheet management strategies are adopted with the intent to ensure that the potential impact on earnings and liquidity due to fluctuations in interest rates are within acceptable standards. We currently do not use off-balance-sheet financial instruments to manage interest rate sensitivity and net interest income.

Earnings Simulation Analysis: Management uses simulation analysis to measure the sensitivity of net interest income to changes in interest rates. The model calculates an earnings estimate based on current and projected balances and rates. This method is subject to the accuracy of the assumptions that underlie the process, but it provides an additional analysis of the sensitivity of earnings to changes in interest rates to static gap analysis. Assumptions used in the model rates are derived from historical trends, peer analysis, and management's outlook, and include loans and deposit growth rates and projected yields and rates. All maturities, calls, and prepayments in the securities portfolio are assumed to be reinvested in like instruments. Mortgage loans and mortgage-backed securities prepayment assumptions are based on industry estimates of prepayment speeds for portfolios with similar coupon ranges and seasoning. Different interest rate scenarios and yield curves are used to measure the sensitivity of earnings to changing interest rates. Interest rates on different asset and liability accounts move differently when the prime rate changes and is reflected in the different rate scenarios.

The following table represents interest rate sensitivity on our net interest income using different rate scenarios:

Change in Prime Rate	% Change in Net Interest Income
+ 300 basis points	11.23 %
+ 200 basis points	8.19 %
+ 100 basis points	4.77 %
- 100 basis points	(7.51)%

Market Value Simulation: Market value simulation is used to calculate the estimated fair value of assets and liabilities over different interest rate environments. Market values are calculated based on discounted cash flow analysis. The net market value is the market value of all assets minus the market value of all liabilities. The change in net market value over different rate environments is an indication of the longer term repricing risk in the balance sheet. The same assumptions are used in the market value simulation as in the earnings simulation. The following table reflects the change in net market value over different rate environments:

Change in Prime Rate	Change in Net Market Value (in thousands)
+ 300 basis points	$ 5,780
+ 200 basis points	$ 24,590
+ 100 basis points	$ 41,838
- 100 basis points	$ (163,689)

Credit Risk Elements: We place commercial loans in nonaccrual status when management believes, after considering economic and business conditions and collections efforts, that the borrower's financial condition is such that full collection of principal and interest is doubtful or when the loan is past due for 90 days or more, unless the debt is both well-secured and in the process of collection. Residential mortgage loans and other consumer loans are placed on nonaccrual status when full collection of principal and interest becomes doubtful or when the loan is past due for 120 days or more, unless the debt is both well-secured and in the process of collection.

FORWARD-LOOKING STATEMENTS

This report contains certain forward-looking statements with respect to our plans, objectives, future performance, and business, which are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Words such as "expects," "anticipates," "believes," "estimates," and other similar expressions or future or conditional verbs such as "will," "should," "would," and "could" are intended to identify such forward-looking statements. These forward-looking statements are not guarantees of future performance and involve certain risks and uncertainties and are based on the beliefs and assumptions of our management.

Factors that may cause actual results to differ materially from those contemplated by such forward-looking statements include, among others, the following:

- competitive pressures in the banking industry may increase significantly;
- changes in the interest rate environment may reduce margins and/or the volumes and values of loans made or held, as well as the value of other financial assets held;
- changes in the creditworthiness of customers and the possible impairment of the collectability of loans;
- general economic conditions, either nationally or regionally, may be less favorable than expected, resulting in, among other things, a deterioration in credit quality and/or a reduced demand for credit or other services;
- changes in the legislative or regulatory environment, including changes in accounting standards and tax laws, may adversely affect our businesses;
- costs or difficulties related to the integration of the business and the businesses we have acquired may be greater than expected;
- expected cost savings associated with pending or recently completed acquisitions may not be fully realized or realized within the expected time frame;

- our competitors may have greater financial resources and develop products that enable them to compete more successfully;
- changes in business conditions;
- changes in the securities market; and
- changes in our local economy with regard to our market area and its heavy concentration of U.S. military bases and related personnel.

We undertake no obligation to update or clarify these forward-looking statements, whether as a result of new information, future events or otherwise.

NON-GAAP FINANCIAL MEASURES

This report contains financial information determined by methods other than in accordance with GAAP. The Company's management uses these non-GAAP financial measures in its analysis of the Company's performance. Management believes presentations of these non-GAAP financial measures provide useful supplemental information that is essential to a proper understanding of the operating results of the Company's core businesses. These non-GAAP disclosures should not be viewed as a substitute for operating results determined in accordance with GAAP, nor are they necessarily comparable to non-GAAP performance measures that may be presented by other companies.

The Company presents return on average assets, return on average tangible assets, return on average equity, and return on average tangible equity. The Company excludes the balance of average goodwill and other intangible assets from our calculation of return on average tangible assets and return on average tangible equity. This adjustment allows management to review the Company's core operating results and core capital position.

(dollars in thousands, except per share data)

Year Ended December 31,	**2019**	**2018**
Return on average assets (GAAP basis)	1.19%	1.26%
Impact of excluding average goodwill and other intangibles and amortization	0.14%	0.15%
Return on average tangible assets (non-GAAP)	1.33%	1.41%
Return on average equity (GAAP basis)	8.69%	9.20%
Impact of excluding average goodwill and other intangibles and amortization	4.89%	5.32%
Return on average tangible equity (non-GAAP)	13.58%	14.52%
Average assets (GAAP basis)	$ 11,638,426	$ 10,599,185
Less: average goodwill and other intangibles	503,108	469,522
Average tangible assets (non-GAAP)	$ 11,135,318	$ 10,129,663
Average equity (GAAP basis)	$ 1,597,281	$ 1,454,796
Less: average goodwill and other intangibles	503,108	469,522
Average tangible equity (non-GAAP)	$ 1,094,173	$ 985,274

The Company presents book value (period ended shareholders' equity divided by the period ended common shares outstanding) and tangible book value. In calculating tangible book value, the Company excludes goodwill and other intangible assets, allowing management to review its core capital position.

(dollars in thousands, except per share data)	Per share			
Year Ended December 31,		**2019**		**2018**
Book value (GAAP basis)	$	22.58	$	21.05
Impact of excluding average goodwill and other intangibles and amortization		(6.89)		(6.79)
Tangible book value (non-GAAP)	$	15.69	$	14.26
Period End:				
Common equity (GAAP basis)	$	1,653,694	$	1,538,420
Goodwill and other intangibles		501,215		492,410
Tangible common equity (non-GAAP)	$	1,152,479	$	1,046,010

When computing the efficiency ratio (noninterest expense divided by the sum of net interest income and noninterest income, excluding securities gains or losses), the Company excludes gains and losses on securities because of the uncertainty of the amount of gain or loss recognized.

DHG
DIXON HUGHES GOODMAN LLP

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of TowneBank

Opinions on the Consolidated Financial Statements and Internal Control Over Financial Reporting

We have audited the accompanying consolidated balance sheets of TowneBank and subsidiaries (the "Company") as of December 31, 2019 and 2018, and the related consolidated statements of income, comprehensive income, equity, and cash flows for each of the three years in the period ended December 31, 2019 and the related notes (collectively referred to as the "consolidated financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO").

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2019 and 2018, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2019, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by COSO.

Basis for Opinion

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control. Our responsibility is to express an opinion on the Company's consolidated financial statements, and an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and

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evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current period audit of the financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the financial statements, taken as a whole, as we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

Goodwill Impairment Assessment

As described in Note 8 to the consolidated financial statements, the Company's consolidated goodwill balance was $446.8 million at December 31, 2019, which is allocated to the Company's reporting units. Goodwill is tested for impairment at least annually at the reporting unit level. The determination of the fair value of the reporting units requires management to make significant estimates and assumptions, such as the rate of growth of revenues and expenses, in determining the discounted projected future cash flows, which are derived from internal forecasts, economic expectations and the discount rate. As disclosed by management, changes in these assumptions could have a significant impact on either the fair value of the reporting units, the amount of any goodwill impairment charge, or both.

We identified the Company's goodwill impairment assessment as a critical audit matter. Management makes estimates and assumptions for each reporting unit regarding revenue and expense growth over the forecast period as well as the discount rate, which include a higher degree of subjectivity. As a result, auditing the reasonableness of management's significant estimates and assumptions, particularly as it relates to the rate of growth of revenue and expenses, involves a higher degree of judgment and subjectivity. In addition, the extent of audit effort included the use of the firm's internal valuation specialists to assist in performing these procedures and evaluating whether management's judgments were appropriate.

The primary procedures we performed to address this critical audit matter included:

- We tested the design and operating effectiveness of controls relating to management's goodwill impairment tests, including controls over management's review of the significant inputs and assumptions, such as the rate of growth of revenues and expenses, in determining the discounted projected future cash flows, associated with the fair value determination of the reporting units.
- We evaluated the historical performance of each of the reporting units as compared to forecasted performance and assessing any significant forecasted changes. We also considered evidence gathered in other areas of the audit and the potential impact that could have on the assumptions used in the calculations.
- We involved the firm's internal valuation specialists in our evaluation of management's significant assumptions, as described above, used in developing the fair value estimate for each reporting unit.

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Allowance for Loan Losses
As described in Note 4 to the consolidated financial statements, the Company's consolidated allowance for loan losses was $58.2 million at December 31, 2019. As described by management, the allowance for loan losses includes consideration of specific valuation allowances on impaired loans, historical loss experience, and current general economic conditions and other internal and external qualitative risk factors. Estimating an appropriate allowance requires management to make numerous assumptions about losses that have been incurred but not yet realized in the loan portfolio as of the balance sheet date. The most significant judgments in the allowance as of December 31, 2019 include the determination of the impact of general economic conditions and external and internal qualitative risk factors and the identification and valuation of impaired loans.

We identified the allowance for loan losses as a critical audit matter. The principal considerations for our determination of the allowance for loan losses as a critical audit matter include management's judgment applied in determining the impact of qualitative and other risk factors and the valuation risk involved in appropriately identifying and valuing impaired loans. In turn, auditing management's judgments regarding loan loss estimates and assumptions, specifically the identification and valuation of impaired loans and internal and external qualitative risk factors applied in the allowance calculation involved a high degree of subjectivity and an increased extent of audit effort.

The primary procedures we performed to address this critical audit matter included:

- We tested the design and operating effectiveness of controls relating to management's determination of the allowance for loan losses, including:
    - Controls over management's credit administration function, such as the identification and valuation of impaired loans, approvals of risk grade changes and charge-off requests, and automated system controls placing past-due loans onto non-accrual status.
    - Controls over management's review and approval of the allowance reserve, including management's evaluation of the internal and external qualitative factors.
- We tested the calculation of losses on identified impaired loans, including comparing inputs to loan agreements, external appraisals other source documents, and loan reports to determine whether there were any unidentified impaired loans.
- We evaluated management's application of general economic and other qualitative risk factor adjustments to the allowance and compared the underlying support to third party or internal sources, as applicable.
- We assessed overall trends in credit quality at the Company by analyzing key performance indicators as well as changes in the industry and how the Company's allowance model and qualitative and other risk factors compared to those trends. We also considered the weight of confirming and disconfirming evidence from internal and external sources, loan portfolio performance and third-party data, and whether such assumptions were applied consistently period over period.

Definition and Limitations of Internal Control Over Financial Reporting
A company's 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 generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made

only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Dixon Hughes Goodman LLP

We have served as the Company’s auditor since 1999.

Norfolk, Virginia
February 28, 2020

INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of TowneBank is responsible for the preparation and fair presentation of the financial statements and other financial information contained in this report. The accompanying consolidated financial statements were prepared in conformity with accounting principles generally accepted in the United States of America and include, as necessary, best estimates and judgments by management. Management also prepared other information in the Annual Report and is responsible for its accuracy and consistency with the consolidated financial statements. Our management is responsible for establishing and maintaining adequate internal control over financial reporting and for our compliance with laws and regulations relating to safety and soundness designated by the Federal Deposit Insurance Corporation ("FDIC"). Our internal control system was designed to provide reasonable assurance to our management and Board of Directors regarding the preparation and fair presentation of published financial statements.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

We maintain systems of controls that we believe are reasonably designed to provide our management with timely and accurate information about our operations. The system of internal controls includes, but is not limited to, maintaining internal audit and compliance functions; establishing formal written policies, procedures, and codes of conduct; training personnel; and segregating key duties and functions, where appropriate.

The Audit Committee of the Board of Directors participates in the adequacy of the system of internal controls and financial reporting. The Audit Committee consists of independent directors who meet regularly with management, the internal auditor, and the independent auditors to review the scope of their work and findings.

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2019, including controls over regulatory financial statements in accordance with the Federal Financial Institutions Examination Council instructions for Consolidated Reports of Condition and Income. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control – Integrated Framework (2013). Based on our assessment we believe that, as of December 31, 2019, our internal control over financial reporting is effective based on those criteria.

Financial Statements

Our management is responsible for the preparation, integrity, and fair presentation of our published consolidated financial statements as of December 31, 2019, and for the year then ended. The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America and, as such, include amounts, some of which are based on management's judgments and estimates.

Compliance with Designated Laws and Regulations

Our management is also responsible for compliance with federal and state laws and regulations concerning dividend restrictions and federal laws and regulations concerning loans to insiders designated by the FDIC as safety and soundness laws and regulations. Management assessed our compliance with the designated laws and regulations. Based on this assessment, our management believes that we complied, in all significant respects, with the designated laws and regulations relating to safety and soundness for the year ended December 31, 2019.

Management's assessment of the effectiveness of internal control over financial reporting, including controls over the preparation of regulatory financial statements in accordance with the Federal Financial Institutions Examination Council instructions for Consolidated Reports of Condition and Income, as of December 31, 2019, has been audited by Dixon Hughes Goodman LLP, the independent registered public accounting firm, as stated in their report dated February 28, 2020. A copy of this report, which is combined with the report expressing an opinion on the consolidated financial statements, precedes.

February 28, 2020

/s/ J. Morgan Davis

J. Morgan Davis
President and Chief Executive Officer

/s/ William B. Littreal

William B. Littreal
Senior Executive Vice President and Chief Financial Officer

TOWNEBANK
CONSOLIDATED BALANCE SHEETS
(dollars in thousands, except share data)
December 31, 2019 and 2018

ASSETS

	2019	2018
Cash and due from banks	$ 97,593	$ 94,604
Interest-bearing deposits at FRB- Richmond	322,505	570,425
Interest-bearing deposits in financial institutions	22,518	21,667
Total Cash and Cash Equivalents	442,616	686,696
Securities available for sale, at fair value	1,441,308	1,095,339
Securities held to maturity, at amortized cost	43,688	50,598
Other equity securities	6,462	4,797
FHLB stock	30,094	43,229
Total Securities	1,521,552	1,193,963
Mortgage loans held for sale	419,233	220,986
Loans, net of unearned income and deferred costs:	8,419,288	8,018,233
Less: allowance for loan losses	(58,234)	(52,094)
Net Loans	8,361,054	7,966,139
Premises and equipment, net	231,806	211,796
Goodwill	446,816	433,658
Other intangible assets, net	54,399	58,752
BOLI	243,062	237,371
Other assets	227,125	153,669
TOTAL ASSETS	$ 11,947,663	$ 11,163,030
LIABILITIES AND EQUITY		
Deposits:		
Noninterest-bearing demand	$ 2,951,225	$ 2,622,761
Interest-bearing:		
Demand and money market accounts	3,586,364	3,223,215
Savings	276,205	286,684
Certificates of deposit	2,457,123	2,237,762
Total Deposits	9,270,917	8,370,422
Advances from the FHLB	471,687	799,315
Subordinated debt, net	248,458	247,861
Repurchase agreements and other borrowings	52,391	47,156
Total Borrowings	772,536	1,094,332
Other liabilities	250,516	159,856
TOTAL LIABILITIES	10,293,969	9,624,610
Preferred stock		
Authorized and unissued shares - 2,000,000	—	—
Common stock, $1.667 par value		
Authorized shares - 150,000,000		
Issued and outstanding shares - 72,649,682 in 2019		
and 72,465,923 in 2018	121,107	120,801
Capital surplus	1,041,160	1,034,676
Retained earnings	467,186	379,239
Common stock issued to deferred compensation trust, at cost		
818,578 shares in 2019 and 769,200 shares in 2018	(15,555)	(13,955)
Deferred compensation trust	15,555	13,955
Accumulated other comprehensive income (loss)	11,302	(9,190)
TOTAL SHAREHOLDERS' EQUITY	1,640,755	1,525,526
Noncontrolling interest	12,939	12,894
TOTAL EQUITY	1,653,694	1,538,420
TOTAL LIABILITIES AND EQUITY	$ 11,947,663	$ 11,163,030

See accompanying Notes to Consolidated Financial Statements.

TOWNEBANK
CONSOLIDATED STATEMENTS OF INCOME
(dollars in thousands, except per share data)
For the Years Ended December 31, 2019, 2018, and 2017

	2019	2018	2017
INTEREST INCOME:			
Loans, including fees	$ 403,675	$ 371,343	$ 273,999
Investment securities	36,946	27,127	13,064
Interest-bearing deposits in financial institutions and federal funds sold	13,825	10,229	7,480
Mortgage loans held for sale	13,379	13,124	10,561
Total interest income	467,825	421,823	305,104
INTEREST EXPENSE:			
Deposits	86,255	53,141	28,792
Advances from the FHLB	11,018	15,340	9,837
Subordinated debt, net	11,847	12,067	5,249
Repurchase agreements and other borrowings	350	202	105
Total interest expense	109,470	80,750	43,983
Net interest income	358,355	341,073	261,121
PROVISION FOR LOAN LOSSES	9,371	8,541	5,426
Net interest income after provision for loan losses	348,984	332,532	255,695
NONINTEREST INCOME:			
Residential mortgage banking income, net	66,812	65,104	75,851
Insurance commissions and other title fees and income, net	64,478	56,164	51,933
Real estate brokerage and property management income, net	34,292	31,863	27,487
Service charges on deposit accounts	10,544	11,808	10,594
Credit card merchant fees, net	4,746	5,472	5,008
BOLI	9,215	6,836	6,262
Other income	16,346	14,343	10,987
Net gain (loss) on investment securities	(845)	3	(1)
Total noninterest income	205,588	191,593	188,121
NONINTEREST EXPENSE:			
Salaries and employee benefits	218,920	201,838	169,449
Occupancy	31,381	27,644	26,855
Furniture and equipment	14,351	14,477	14,072
Amortization - intangibles	12,370	11,710	7,656
Software expense	11,717	10,621	8,517
Data processing	11,825	10,364	6,975
Professional fees	12,943	8,323	7,144
Advertising and marketing	12,279	11,194	9,867
Other expenses	52,516	55,953	45,679
Total noninterest expense	378,302	352,124	296,214
Income before income tax expense and noncontrolling interest	176,270	172,001	147,602
Provision for income tax expense	32,596	34,227	54,813
Net income	$ 143,674	$ 137,774	$ 92,789
Net income attributable to noncontrolling interest	(4,891)	(3,981)	(5,126)
Net income attributable to TowneBank	$ 138,783	$ 133,793	$ 87,663
Per common share information			
Basic earnings	$ 1.93	$ 1.88	$ 1.41
Diluted earnings	$ 1.92	$ 1.88	$ 1.41
Cash dividends declared	$ 0.70	$ 0.62	$ 0.55

See accompanying Notes to Consolidated Financial Statements.

TOWNEBANK
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands)
For the Years Ended December 31, 2019, 2018, and 2017

	2019	2018	2017
Net income	$ 143,674	$ 137,774	$ 92,789
Other comprehensive income (loss)			
Unrealized gains (losses) on securities			
Unrealized holding gains (losses) arising during the period	30,797	(5,511)	(1,644)
Deferred tax (expense) benefit	(6,707)	1,224	575
Realized losses (gains) reclassified into earnings	845	(3)	1
Deferred tax (expense) benefit	(177)	1	—
Net unrealized gains (losses)	24,758	(4,289)	(1,068)
Pension and postretirement benefit plans			
Prior service costs	(2,704)	(224)	(1,027)
Deferred tax benefit	601	49	359
Actuarial (loss) gain	(2,754)	2,327	(400)
Deferred tax benefit (expense)	612	(506)	142
Amortization of prior service costs	613	305	288
Deferred tax expense	(133)	(66)	(100)
Amortization of net actuarial (gain) loss	(645)	85	156
Deferred tax benefit (expense)	144	(19)	(56)
Change in retirement plans, net of tax	(4,266)	1,951	(638)
Other comprehensive income (loss), net of tax	20,492	(2,338)	(1,706)
Comprehensive income	$ 164,166	$ 135,436	$ 91,083
Comprehensive income attributable to noncontrolling interest	(4,891)	(3,981)	(5,126)
Comprehensive income attributable to TowneBank	$ 159,275	$ 131,455	$ 85,957

See accompanying Notes to Consolidated Financial Statements.

TOWNEBANK
CONSOLIDATED STATEMENTS OF EQUITY
(dollars in thousands, except share data)
For the Years Ended December 31, 2019, 2018, and 2017

	Common Shares	Common Stock	Capital Surplus	Retained Earnings	Deferred Compensation Trust	Common Stock Issued to Deferred Compensation Trust	Accumulated Other Comprehensive (Loss)	Non-controlling Interests	Total
Balance, December 31, 2016	**62,492,168**	**$ 104,174**	**$ 745,411**	**$ 229,503**	**$ 11,168**	**$ (11,168)**	**$ (3,986)**	**$ 11,456**	**$ 1,086,558**
Net income	—	—	—	87,663	—	—	—	5,126	92,789
Other comprehensive loss, net of taxes	—	—	—	—	—	—	(1,706)	—	(1,706)
Cash dividends declared on common stock ($0.55 per share)	—	—	—	(34,437)	—	—	—	—	(34,437)
Directors' deferred compensation	—	—	—	—	1,356	(1,356)	—	—	—
Investment of noncontrolling interest in consolidated joint ventures	—	—	—	—	—	—	—	1,029	1,029
Distribution of interests in joint ventures, net	—	—	—	—	—	—	—	(6,346)	(6,346)
Conversion of convertible debt into common stock	1,528	2	20	—	—	—	—	—	22
Issuance of common stock - stock compensation plans	65,459	110	2,314	—	—	—	—	—	2,424
Issuance of common stock - net contingent consideration earned on acquisitions	69,846	117	2,055	—	—	—	—	—	2,172
Balance, December 31, 2017	**62,629,001**	**$ 104,403**	**$ 749,800**	**$ 282,729**	**$ 12,524**	**$ (12,524)**	**$ (5,692)**	**$ 11,265**	**$ 1,142,505**
Impact of adoption of new accounting standards (1)	—	—	—	7,579	—	—	(1,160)	—	6,419
Net income	—	—	—	133,793	—	—	—	3,981	137,774
Other comprehensive loss, net of taxes	—	—	—	—	—	—	(2,338)	—	(2,338)
Cash dividends declared on common stock ($0.62 per share)	—	—	—	(44,862)	—	—	—	—	(44,862)
Directors' deferred compensation	—	—	—	—	1,431	(1,431)	—	—	—
Investment of noncontrolling interest in consolidated joint ventures	—	—	—	—	—	—	—	2,945	2,945
Distribution of interests in joint ventures, net	—	—	—	—	—	—	—	(5,297)	(5,297)
Conversion of convertible debt into common stock	553	1	8	—	—	—	—	—	9
Issuance of common stock - acquisitions	9,457,197	15,764	279,293	—	—	—	—	—	295,057
Issuance of common stock - stock compensation plans	293,349	490	3,112	—	—	—	—	—	3,602
Issuance of common stock - net contingent consideration earned on acquisitions	85,823	143	2,463	—	—	—	—	—	2,606
Balance, December 31, 2018	**72,465,923**	**$ 120,801**	**$ 1,034,676**	**$ 379,239**	**$ 13,955**	**$ (13,955)**	**$ (9,190)**	**$ 12,894**	**$ 1,538,420**
Net income	—	—	—	138,783	—	—	—	4,891	143,674
Other comprehensive income, net of taxes	—	—	—	—	—	—	20,492	—	20,492
Cash dividends declared on common stock ($0.88 per share)	—	—	—	(50,836)	—	—	—	—	(50,836)
Directors' deferred compensation	—	—	—	—	1,600	(1,600)	—	—	—
Investment of noncontrolling interest in consolidated joint ventures	—	—	—	—	—	—	—	100	100
Distribution of interests in joint ventures, net	—	—	—	—	—	—	—	(4,946)	(4,946)
Issuance of common stock - stock compensation plans	130,943	219	5,107	—	—	—	—	—	5,326
Issuance of common stock - net contingent consideration earned on acquisitions	52,816	87	1,377	—	—	—	—	—	1,464
Balance, December 31, 2019	**72,649,682**	**$ 121,107**	**$ 1,041,160**	**$ 467,186**	**$ 15,555**	**$ (15,555)**	**$ 11,302**	**$ 12,939**	**$ 1,653,694**

(1) Represents the impact of adopting ASU No. 2018-02 and ASU No. 2014-09. See Note 1 to the Consolidated Financial Statements for more information.

See accompanying Notes to Consolidated Financial Statements.

TOWNEBANK
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
For the Years Ended December 31, 2019, 2018, and 2017

OPERATING ACTIVITIES:	2019	2018	2017
Net income	$ 143,674	$ 137,774	$ 92,789
Adjustments to reconcile net income to net cash from operating activities:			
Net amortization of securities	2,774	2,874	2,359
Investment securities losses (gains)	845	(3)	1
Depreciation, amortization, and other intangible amortization	29,371	28,724	24,500
Amortization of debt issuance costs	597	665	124
Provision for loan losses	9,371	8,541	5,426
Bank-owned life insurance income	(9,215)	(6,836)	(6,262)
Deferred income tax expense (benefit)	4,783	(1,300)	570
Share-based compensation expense	5,345	2,905	2,706
(Gain) loss on sale and write-down of foreclosed assets	(247)	(956)	1,087
Originations of mortgage loans held for sale	(3,175,797)	(2,984,899)	(3,329,859)
Proceeds from sales of mortgage loans held for sale	3,082,906	3,179,752	3,443,801
Gain on sales of mortgage loans held for sale	(105,356)	(102,583)	(113,152)
Changes in:			
Interest receivable	(46)	(10,579)	(2,213)
Other assets	(40,124)	11,456	27,337
Interest payable	1,065	3,224	5,720
Other liabilities	34,019	38,591	(13,856)
Net cash from (used for) operating activities	(16,035)	307,350	141,078
INVESTING ACTIVITIES:			
Purchase of available-for-sale securities	(778,538)	(960,334)	(1,139,278)
Purchase of held-to-maturity securities	(1,896)	—	—
Purchase of other securities	(1,669)	(964)	(28)
Sale of available-for-sale securities	186,043	48,549	306
Net change in FHLB stock	13,135	6,721	6,816
Proceeds from maturities, calls, and prepayments of available-for-sale securities	274,641	851,369	1,080,013
Proceeds from maturities, calls, and prepayments of held-to-maturity securities	8,718	10,555	4,988
Proceeds from maturities, calls, and prepayments of other securities	—	1,176	27
Net increase in loans	(407,416)	(643,266)	(146,610)
Purchases of premises and equipment	(36,717)	(20,847)	(13,445)
Proceeds from sales of premises and equipment	649	634	674
Proceeds from sales of foreclosed assets	8,041	7,994	7,595
Proceeds from bank-owned life insurance	1,385	582	—
Investment from noncontrolling interest in consolidated joint ventures	100	123	1,029
Acquisition of business, net of cash acquired	(19,747)	61,100	(11,469)
Net cash used for investing activities	(753,271)	(636,608)	(209,382)
FINANCING ACTIVITIES:			
Net increase in deposit accounts	900,495	673,566	413,022
Net change in borrowings	(322,393)	(113,387)	(168,256)
Proceeds from (repayments of) subordinated debt	—	(18,558)	247,072
Proceeds (payments) from share-based compensation activity	(19)	697	(282)
Proceeds from issuance of common stock	1,464	2,606	2,172
Distribution of interest in joint ventures	(4,946)	(5,297)	(6,346)
Cash dividends paid	(49,375)	(44,862)	(34,437)
Net cash from financing activities	525,226	494,765	452,945
Change in cash and cash equivalents	(244,080)	165,507	384,641
Cash and cash equivalents at beginning of year	686,696	521,189	136,548
Cash and cash equivalents at end of year	$ 442,616	$ 686,696	$ 521,189
Supplemental cash flow information:			
Cash paid for interest	$ 108,405	$ 58,578	$ 38,262
Cash paid for income taxes	$ 28,065	$ 24,612	$ 35,972
Noncash financing and investing activities:			
Transfer from loans to foreclosed property	$ 3,130	$ 2,917	$ 4,570
Sales of foreclosed assets financed by the Company	$ 227	$ 1,340	$ 1,012
Transfers to foreclosed property from premises and equipment	$ —	$ —	$ 843
Net unrealized loss on available-for-sale securities	$ 24,758	$ (4,289)	$ (1,068)
Dividends declared but not paid	$ 13,005	$ 11,699	$ 8,769
Common stock issued in connection with business acquisitions	$ —	$ 295,057	$ —
Right of use asset recognized upon adoption of ASC 842	$ 43,260	$ —	$ —

See accompanying Notes to Consolidated Financial Statements.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business: TowneBank was organized and incorporated under the laws of the Commonwealth of Virginia on September 1, 1998, and commenced operations on April 8, 1999. The Company, through its banking and non-banking subsidiaries, provides a diverse range of financial services and products throughout Richmond, Virginia, the Greater Hampton Roads region in southeastern Virginia, northeastern North Carolina, and the Raleigh, Charlotte, Greensboro, and Greenville, North Carolina metropolitan areas.

Basis of presentation: The Consolidated Financial Statements include the accounts of the Company and all other entities in which the Company has a controlling financial interest. The accompanying Consolidated Financial Statements are prepared in conformity with GAAP and prevailing practices of the banking industry. All significant intercompany balances and transactions have been eliminated in consolidation. The following is a summary of the significant accounting and reporting policies used in preparing the Consolidated Financial Statements.

Reclassifications and corrections: To maintain consistency and comparability, certain amounts from prior periods have been reclassified to conform to current period presentation with no effect on net income or shareholders' equity as previously reported.

Use of estimates: The preparation of consolidated 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 periods. Actual results could differ from those estimates and assumptions. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, valuation of OREO, deferred income taxes, fair value estimates, and valuation of goodwill, intangible assets, and other purchase accounting related adjustments.

Cash and cash equivalents: For purposes of reporting cash flows, the Company considers cash and due from banks, interest-bearing deposits in financial institutions, and federal funds sold as cash and cash equivalents. Generally, federal funds and securities purchased under agreements to resell are purchased and sold for one-day periods. The Company is required to maintain average reserve balances in cash with the FRB - Richmond; required reserves were $39.90 million and $28.72 million at December 31, 2019 and 2018, respectively.

Investment securities: Investment securities are classified in three categories and accounted for as follows:

a) Debt securities that the Company has the positive intent and ability to hold to maturity are classified as HTM securities and reported at amortized cost.

b) Debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and reported at fair value, with unrealized gains and losses included in earnings.

c) Debt securities not classified as either HTM or trading securities are classified as AFS securities and reported at fair value, with unrealized holding gains and losses excluded from earnings and reported as other comprehensive income, a separate component of shareholders' equity, until realized.

Gains and losses on sales of securities are determined on a trade date basis using specific identification of the adjusted cost of each security and included in noninterest income. Amortization of premiums and accretion of discounts are computed by the effective yield method and included in interest income. Other-than-temporary declines in the fair value of individual HTM and AFS securities below their cost, if any, are included in earnings as realized losses.

The Company evaluates debt securities for indicators of OTTI on a quarterly basis. Management assesses whether OTTI has occurred when the fair value of a debt security is less than the amortized cost basis at the balance sheet date. Management reviews the amount of unrealized loss, the length of time the security has been in an unrealized loss position, the credit rating history, market trends of similar security classes, time remaining to maturity, and the source of both interest and principal payments to identify securities which could potentially be impaired. OTTI is considered to have occurred if (i) management intends to sell the security; (ii) it is more likely than not management will be required to sell the security before recovery of its amortized cost basis; or (iii) the present value of expected cash flows is not sufficient to recover all contractually required principal and interest payments. For securities that management does not intend to sell, or it is not more likely than not to be required to sell, the OTTI is separated into credit and noncredit components. A discounted cash flow analysis, which includes evaluating the timing of expected cash flows, is completed for all debt securities subject to credit impairment. The measurement of the credit loss component is equal to the difference between the debt security's cost basis and the present value of its expected future cash flows discounted at the security's effective yield. The credit-related OTTI, represented by the expected loss in principal, is recognized by reducing the amortized cost basis of the security with offset to noninterest income. The remaining difference between the security's fair value and the present value of future expected cash flows is due to factors that are not credit-related and, therefore, is recognized in OCI. Management believes that it will fully collect the carrying value of securities on which noncredit-related impairment has been recognized in OCI. Noncredit-related OTTI results from other factors, including increased liquidity spreads and extension of the security. For securities that management does expect to sell, or if it is more likely than not the Company will be required to sell the security before recovery of its amortized cost basis, any OTTI is recognized in earnings.

Loans: Loans that management has the intent and ability to hold for the foreseeable future, or until maturity or pay-off, generally are stated at the amount of outstanding principal less unamortized fees and costs on originated loans, unearned income, and participation interests sold to other lending institutions. Interest on loans is accrued and credited to income based upon the principal amount outstanding. Fees collected and costs incurred in connection with loans originated are deferred and recognized as interest income over the term of the loan as an adjustment of yield.

Allowance for loan losses: The allowance for loan losses is established through a provision for loan losses charged against earnings. The level of the allowance for loan losses is based on management's evaluation of the risk inherent in the loan portfolio at the balance sheet date, and changes in the nature and volume of loan activity. This evaluation includes a review of loans for which collection may not be reasonably assured. It considers internal risk grades, the estimated fair value of the underlying collateral, current and anticipated economic conditions, historical loan loss experience, and other current factors that warrant consideration in determining an adequate allowance.

The allowance for loan losses consists of three elements: (i) specific valuation allowances determined in accordance with ASC 310, *Receivables*, based on probable losses on specific loans; (ii) historical valuation allowances determined in accordance with ASC 450, *Contingencies*, based on historical loan loss experience for similar loans with similar characteristics and trends, adjusted, as necessary, to reflect the impact of current conditions; and (iii) general valuation allowances determined in accordance with ASC 450 based on general economic conditions and other qualitative risk factors both internal and external to the Company.

It is our policy to assign internal risk grades to all loans as a component of the approval process. Based on the size of the loan, senior credit officers, regional credit administrators, and the chief credit officer review the classification to ensure accuracy and consistency of classifications, which are then validated by the internal loan review process. Loan classifications are internally reviewed to determine if any changes in the circumstances of the loan require a different risk grade. To determine the most appropriate risk grade classification for each loan, the credit officers examine the borrower's liquidity level, asset quality, the amount of the borrower's other indebtedness, cash flow, earnings, sources of financing, and existing lending relationships. The allowances established for probable losses on specific loans are based on a regular analysis and evaluation of classified loans.

Historical valuation allowances are calculated based on the historical loss experience of specific types of loans. We calculate historical loss ratios for pools of similar loans with similar characteristics based on the proportion of actual charge-offs experienced to the total population of loans in the pool. The historical loss ratios are updated quarterly based on actual charge-off experience. An historical valuation allowance is established for each pool of similar loans based upon the product of the historical loss ratio and the total dollar amount of the loans in the pool. Our pools of similar loans include groups of construction and land development loans, commercial real estate loans, commercial and industrial business loans, 1-4 family residential real estate loans, multifamily real estate loans, and consumer and other loans.

General valuation allowances are based on general economic conditions and other qualitative risk factors both internal and external to the Company. In general, such valuation allowances are determined by evaluating, among other things: (i) the experience, ability, and effectiveness of the Company's lending management and staff; (ii) the effectiveness of the Company's loan policies, procedures, and internal controls; (iii) changes in asset quality; (iv) changes in loan portfolio volume; (v) the composition and concentrations of credit; (vi) the effectiveness of the internal loan review function; (vii) the impact of national economic trends on portfolio risks; and (viii) the impact of local economic trends on portfolio risk. Management evaluates the degree of risk that each one of these components has on the quality of the loan portfolio on a quarterly basis to determine an appropriate general valuation allowance. Management considers the current level of allowance for loan losses adequate to absorb losses inherent in the loan portfolio. Management's determination of the adequacy of the allowance for loan losses, which is based on the factors and risk identification procedures previously discussed, requires the use of judgments and estimations that may change in the future. Changes in the factors used by management to determine the adequacy of the allowance or the availability of new information could cause the allowance for loan losses to be adjusted in future periods.

Loans acquired: Loans acquired through the completion of a transfer, including loans acquired in a business combination, that have evidence of deterioration of credit quality since origination and for which it is probable, at acquisition, that the Company will be unable to collect all contractually required payments receivable, are initially recorded at fair value (as determined by the present value of expected future cash flows) with no valuation allowance. Loans are evaluated individually to determine if there is evidence of deterioration of credit quality since origination. Loans where there is evidence of deterioration of credit quality since origination may be aggregated and accounted for as a pool of loans, if the loans being aggregated have common risk characteristics. The difference between the undiscounted cash flows expected at acquisition and the investment in the loan, or the "accretable yield," is recognized as interest income on a level-yield method over the life of the loan. The difference between the contractually required payments at acquisition and the cash flows expected to be collected at acquisition is referred to as the nonaccretable difference. A subsequent decrease in the estimate of cash flows expected to be received on purchased credit-impaired loans generally results in the recognition of an allowance for loan losses. Increases in cash flows result in reversal of any nonaccretable difference (or allowance for loan losses to the extent any has been recorded) with a positive impact on interest income subsequently recognized. The measurement of cash flows involves assumptions and judgments for interest rates, prepayments, default rates, loss severity, and collateral values. All of these factors are inherently subjective and significant changes in the cash flow estimates over the life of the loan can result.

For purchased loans that are not deemed impaired at acquisition, discounts representing the principal losses expected over the life of the loan are a component of the initial fair value. Loans may be aggregated and accounted for as a pool of loans if the loans being aggregated have common risk characteristics. Subsequent to the purchase date, the methods utilized to estimate the required allowance for credit losses for these loans is similar to originated loans; however, the Company records a provision for loan losses only when the required allowance exceeds any remaining discounts. The difference between the initial fair value at acquisition and the undiscounted expected cash flows is recorded in interest income over the life of the loans using a method that approximates the effective interest method.

Current expected credit losses: In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments - Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments.* This ASU supersedes the existing impairment guidance within *ASC Topic 310 - Receivables*, related to Financing Receivables. ASC 326 replaces the incurred loss impairment methodology with an expected credit loss methodology, commonly referred to as CECL. The incurred loss methodology required the recognition of credit losses when it was probable a loss had been incurred. In contrast, the CECL methodology requires expected credit losses to be estimated over the life of the financial instruments and to be recorded at origination, or acquisition of the asset.

For our Company, ASU No. 2016-13 is effective for interim and annual periods beginning after December 15, 2019. The Company adopted ASU No. 2016-13 on January 1, 2020.

To prepare for this adoption, management built a company-wide, cross-discipline, working group to oversee CECL implementation. The working group has been focusing on a number of areas including; policy development, system and controls identification and documentation, development, and documentation of key accounting and governance processes, and new model build-out. Management also engaged a nationally recognized accounting firm to assist management in implementation and selected a third-party software solution to assist in CECL application. A credit model that facilitates the utilization of multiple economic scenarios with probability weightings, reasonable and supportable forecasting with reversion to long term historical loss after two years, and in depth portfolio analysis, was substantially completed in the second quarter of 2019. Model implementation is complete and we are in the process of reviewing the most recent model runs to finalize internal controls around the process and and test assumptions, including qualitative adjustments and economic forecasts.

For financial assets measured at amortized cost, the Company adopted the standard utilizing the modified-retrospective method, which required a cumulative-effect adjustment to retained earnings. Acquired loans that were previously classified as purchased credit-impaired loans and accounted for under ASC 310-30 were transitioned over as purchased credit deteriorated under ASU 2016-13. Consistent with the requirements of the ASU 2016-13, management did not reassess whether legacy purchased credit-impaired assets met the criteria of purchased credit deteriorated assets as of the date of adoption.

The adoption of ASC 326 addresses a broader range of topics than that covered by historic guidance. AFS debt securities and HTM debt securities will be evaluated for allowances for credit losses in the Consolidated Balance Sheets. Corresponding provisions for credit losses have been added to the existing provisions and the line item provision for loan losses is replaced with a broader provision for credit losses. New disclosures requirements have also been introduced and will be incorporated in future financial statements.

We currently estimate our loss reserves may increase up to 10% upon the finalization of our adoption of the new ASU, which includes an increase related to off-balance sheet exposures. The actual impact will depend on a number of internal and external factors including: outstanding balances, characteristics of our loan and securities portfolios, macroeconomic conditions, forecast information, and management's judgment. Additionally, adoption of the new ASU could result in higher volatility in our quarterly credit loss provision than the current reserve process and could adversely impact the Company's ongoing earnings.

Mortgage loans held for sale: Loans originated and intended for sale in the secondary market using "best efforts" delivery are carried at the lower of cost or estimated fair value. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income. Loans originated and intended for sale in the secondary market using "mandatory" delivery are carried at estimated fair value.

Premises and equipment: Premises and equipment are stated at cost, less accumulated depreciation. Leasehold improvements are amortized over the lives of the respective leases or the estimated useful life of the leasehold improvement, whichever is less.

For financial reporting purposes, depreciation is computed by the straight-line method over the estimated useful lives of the assets. For income tax purposes, the modified accelerated cost recovery system is used. Costs of maintenance and repairs are charged to expense as incurred. Costs of replacing structural parts of major units are considered individually and are expensed or capitalized as the facts dictate.

Fixed assets may be retired and disposed of by sale, trade, abandonment, or through a casualty loss such as a fire or storm. At retirement, the cost of the asset and its related accumulated depreciation are removed from the accounts. The type of disposal will determine the specific treatment of the asset.

Leases: Effective January 1, 2019, the Company adopted the provisions of Accounting Standards Update No. 2016-02 - *Leases (Topic 842)*, for all open leases with a term greater than one year as of the adoption date, using the alternative transition approach. Prior comparable periods are presented in accordance with previous guidance under ASC 840. The Company elected the ASU's package of three practical expedients, which allowed the Company to forego a reassessment of (1) whether any expired or existing contracts are, or contain, leases, (2) the lease classification for any expired or existing leases, and (3) the initial direct costs for any existing leases. The Company has implemented a lease management system to assist in accounting for all leases.

Operating lease liabilities reflect the Company's obligation to make future lease payments. Lease terms typically comprise contractual terms but may include extension options reasonably certain of being exercised at lease inception. Payments are discounted using the rate the Company would pay to borrow amounts equal to the lease payments over the lease term (the Company's incremental borrowing rate). The Company does not separate lease and non-lease components for contracts in which it is the lessee. Operating lease expense is recognized on a straight-line basis over the lease term, while variable lease payments are recognized as incurred. Common area maintenance and other executory costs are the main components of variable lease payments. Operating and variable lease expenses are recorded in net occupancy expense on the Consolidated Statements of Income.

Goodwill and other intangibles: Goodwill is not subject to amortization, but is subject to an annual assessment for impairment by applying a fair-value-based test as required by FASB ASC 350, *Goodwill and Other Intangible Assets*. Additionally, under ASC 350, acquired intangible assets are separately recognized if the benefit of the assets can be sold, transferred, licensed, rented, or exchanged, and amortized over their useful life.

Goodwill is tested for impairment at the reporting unit level on an annual basis as of August 31, or more often if events or circumstances indicate there may be impairment. Testing is conducted in two steps: identifying the potential impairment and then, if necessary, identifying the amount of impairment. The first step (step 1) compares the fair value of the reporting unit to its carrying amount. If the fair value is less than the carrying amount, a second test is conducted by comparing the implied fair value of goodwill with the carrying amount of that goodwill. If the carrying amount exceeds the implied fair value, an impairment loss is recognized in an amount equal to that excess. For our annual impairment testing conducted during 2019, we identified six reporting units with goodwill: Berkshire Hathaway HomeServices Towne Realty; property and casualty insurance division; benefits insurance division; mortgage division; resort property management division; and Banking. For purposes of performing step 1 of the goodwill impairment test, the Company uses the income and market approach to value its reporting units. The income approach consists of discounting projected long-term future cash flows, which are derived from internal forecasts and economic expectations for the respective reporting units. The significant inputs include expected future cash flows, the long-term target tangible equity to tangible assets ratio, and the discount rate. Discount rates are unique to each reporting unit and are based upon the cost of capital specific to the industry in which the reporting unit operates. Management evaluated the sensitivity of the significant assumptions in its impairment analysis, including consideration of the effect of changes in estimated future cash flows or the discount rate for each reporting unit. Based on our analysis, we determined there is no goodwill impairment, since the fair value for all reporting units was in excess of the respective reporting unit's carrying value as of August 31, 2019.

The second step (step 2) of impairment testing is necessary only if the reporting unit does not pass step 1. Step 2 compares the implied fair value of the reporting unit goodwill with the carrying amount of the goodwill for the reporting unit. The implied fair value of goodwill is determined in the same manner as goodwill that is recognized in a business combination. Significant judgment and estimates are involved in estimating the fair value of the assets and liabilities of the reporting unit. Since none of the reporting units failed step 1, step 2 was not applicable during 2019 testing. The Company monitored events and circumstances during the fourth quarter of 2019, and it determined that there were no triggering events requiring an updated impairment test as of December 31, 2019.

Significant judgment is applied when goodwill is assessed for impairment. This judgment includes developing cash flow projections, selecting appropriate discount rates, identifying relevant market comparables, and incorporating general economic and market conditions. Selection and weighting of the various fair value techniques may result in a higher or lower fair value. Judgment is applied in determining the weightings most representative of fair value.

Intangible assets are amortized or tested for impairment based on whether they have finite or indefinite lives. Intangibles that have finite lives are amortized on a straight-line basis over their useful life and tested for impairment whenever events or circumstances indicate the carrying amount of the assets may not be recoverable. Intangibles with indefinite lives are tested annually for impairment. Note 8 provides additional information related to goodwill and other intangible assets.

Other real estate owned: OREO, which is included in other assets on the balance sheet, consists primarily of commercial and residential real estate that has been obtained in partial or full satisfaction of loan obligations. OREO is carried at the lower of carrying value or fair value of the property, less estimated selling costs, with any difference between the fair value of the property, less estimated selling costs, and the carrying value of the loan recorded through a charge to the allowance for loan losses. Subsequent write-downs required for declines in value are recorded through a valuation allowance, or taken directly to the asset, charged to other noninterest expense.

Transfers of financial assets: Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (i) the asset has been isolated from the Company, (ii) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred asset, and (iii) the Company does not maintain effective control over the transferred asset.

Credit-related financial instruments: In the ordinary course of business, the Company 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. They are considered in calculating the provision for loan losses and any reserve is recognized in other liabilities.

Interest rate lock commitments and TBA MBSs: The Company enters into rate lock commitments with its mortgage customers whereby the interest rate on the mortgage loan is determined prior to funding. The commitments are generally for periods of 60 days and are at market rates. The Company is also a party to sales of TBA MBSs. The rate lock commitment and MBS position are undesignated derivatives and marked to fair value through earnings. Both the rate lock commitment and the corresponding MBSs are considered derivatives, but are not accounted for using hedge accounting. As such, changes in the estimated fair value of the derivatives are recorded in current earnings and included in net residential mortgage banking income in the Consolidated Statements of Income.

We sell mortgage loans under both "mandatory" and "best efforts" delivery programs. Under "best efforts", in order to mitigate risk from interest rate fluctuations, the Company enters into forward loan sale commitments on a loan-by-loan basis while the loan is in the pipeline. Under the "mandatory" delivery system, loans with interest rate locks are paired with the sale of TBA MBSs bearing similar attributes. We commit to deliver loans to an investor at an agreed-upon price after the close of such loans.

Revenue recognition: Revenue earned on interest-earning assets is recognized based on the effective yield of the financial instrument. Revenue recognized from contracts with customers, which is accounted for under ASC 606, is primarily included in the Company’s noninterest income. Interest income and certain other types of noninterest income are accounted for under other applicable accounting standards.

Service charges on deposit accounts are recognized as charged. Credit-related fees, including letter of credit fees, are recognized in noninterest income when earned. See Note 16 for additional information about revenue from contracts with customers.

Income recognition on impaired and nonaccrual loans: Commercial loans, including impaired loans, are generally classified as nonaccrual if they are past due as to maturity or payment of principal or interest for a period of more than 90 days, unless such loans are well-secured and in the process of collection. Residential mortgage loans and other consumer loans are classified as nonaccrual if they are past due as to maturity or payment of principal or interest for a period of more than 120 days, unless the debt is both well-secured and in the process of collection. If a loan or a portion of a loan is classified as doubtful or is partially charged off, the loan is generally classified as nonaccrual. Loans that are on a current payment status or past due less than 90 days may also be classified as nonaccrual, if repayment in full of principal and/or interest is unlikely.

While a loan is classified as nonaccrual and the probability of collecting the recorded loan balance is doubtful, collections of interest and principal are generally applied as a reduction to principal outstanding. When the probability of collecting the recorded loan balance is expected, interest income may be recognized on a cash basis. In the case where a nonaccrual loan had been partially charged off, recognition of interest on a cash basis is limited to that which would have been recognized on the recorded loan balance at the contractual interest rate. Cash interest receipts in excess of that amount are recorded as recoveries to the allowance for loan losses until prior charge-offs have been fully recovered.

Loans may be returned to accrual status when all principal and interest amounts contractually due (including arrearages) are reasonably assured of repayment within an acceptable period of time, and there is a sustained period of repayment performance by the borrower in accordance with the contractual terms of interest and principal.

Advertising costs: Advertising costs are expensed as incurred.

Segment information: Operating segments as defined by ASC 280, *Segment Reporting*, are components of an enterprise for which separate financial information is available that is evaluated regularly by the chief operating decision-maker in deciding how to allocate resources and in assessing performance. The accounting policies of operating segments are the same as those described elsewhere in this footnote. Revenue for all segments is derived from external sources. See Note 27 for further discussion of the Company's operating segments.

Mergers and acquisitions: Mergers and acquisitions are accounted for using the acquisition method, as required by ASC 805, *Business Combinations*. Under this method, the cost of the acquired entity will be allocated to the assets acquired and liabilities assumed based on their fair values at the date of acquisition. The excess of the cost over the fair value of the acquired net assets is recognized as goodwill and any merger related costs are expensed as incurred. See Note 2 for further discussion on the Company's mergers and acquisitions.

Income taxes: Income taxes are accounted for under the asset and liability method. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities that result in future taxable or deductible amounts. The effect on deferred taxes of a change in tax rates is recognized in the year of enactment and is measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized in the near term. Note 22 provides additional information on the Company's income taxes.

Comprehensive income: Accounting principles generally require that recognized revenue, expenses, gains, and losses be included in net income or loss. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with the operating net income or loss, are components of comprehensive income or loss. Other comprehensive income or loss includes unrealized gains and losses on available-for-sale securities and actuarial gains and losses on our SERP and other postretirement benefit plans.

Share-based compensation: The Company has a share-based employee compensation plan, which is described in more detail in Note 14. The Company accounts for the plan using the fair value method, which requires that compensation cost relating to stock-based payment transactions be recognized in the financial statements over the vesting period. The compensation cost is measured based on the fair value of the instruments issued.

Earnings per share: Basic earnings per share are computed by dividing earnings available to common shareholders by the weighted-average number of common shares outstanding for the year, less the average number of nonvested restricted stock awards. Diluted earnings per share reflect the potential dilution from the issuance of additional shares of common stock caused by the exercise of stock options and restricted stock awards. See Note 28 for further discussion on the Company's earnings per share.

Recent accounting pronouncements:

Accounting standards adopted in current year		
Standard	**Summary of guidance**	**Effects on financial statements**
Topic 350 - Intangibles - Goodwill and Other **Subtopic 350 - 40 - Internal Use Software: Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract** **ASU 2018 - 15** **Issued August 2018**	Aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include internal-use software licenses).	The Company adopted the standard effective April 1, 2019. We applied the Standard on a prospective basis to all implementation costs incurred after the date of adoption. The adoption of the accounting standard did not have a material impact on the Company's Consolidated Financial Statements.
Topic 718 - Compensation - Stock Compensation: Improvements to Non-employee Share-Based Payment Accounting **ASU 2018 - 07** **Issued June 2018**	Expands the scope of the Topic (which currently only includes share-based payments issued to employees) to include share-based payments issued to non-employees for goods and services. Substantially aligns the accounting for share-based payments to employees and non-employees. Supersedes Subtopic 505-50 - Equity - Equity-Based Payments to Non-Employees.	The Company adopted the standard effective January 1, 2019. The adoption of the accounting standard did not have a material impact on the Company's Consolidated Financial Statements.
Topic 815 - Derivatives and Hedging **ASU 2018 - 16** **Issued October 2018**	Permits the use of the Overnight Index Swap rate based on the Secured Overnight Financing Rate as a U.S. benchmark interest rate for hedge accounting purposes in addition to the U.S. Treasury rate, the LIBOR swap rate, the OIS rate based on the Fed Funds Effective Rate, and the Securities Industry and Financial Markets Association Municipal Swap Rate.	The Company adopted the standard effective January 1, 2019. The Company previously adopted the related ASU 2017-12, and the adoption of this guidance did not have a material impact on its Consolidated Financial Statements.

Accounting standards adopted in current year		
Standard	**Summary of guidance**	**Effects on financial statements**
Topic 842 - Leases **ASU 2016 - 02** **Issued February 2016** **Leases: Codification Improvements** **ASU 2018 - 10** **ASU 2018 - 11** **Issued July 2018** **ASU 2018 - 20** **Issued December 2018**	ASU 2016 - 02 was issued in order to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet for those leases classified as operating leases under previous GAAP. Requires the lessee to recognize a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term on the balance sheet. ASU 2018 - 10 Narrows aspects of the guidance issued in ASU 2016 - 02. Provides clarification to the guidance and corrects the unintended application of the existing guidance. ASU 2018 - 11 Provides entities with an additional (and optional) transition method to adopt the new leases standard. Under this new transition method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balances of retained earnings in the period of adoption. In applying this transition method, an entity's reporting for the comparative periods presented in the financial statements in which it adopts the new leases standard will continue to be in accordance with Topic 840 - Leases. ASU 2018 - 20 Clarifies the accounting by lessors for variable payments that relate to both a lease component and a non-lease component. It is related to sales taxes and other similar taxes collected from lessees.	The Company adopted this standard January 1, 2019, applying the alternative transition method whereby comparative periods were not restated, and any cumulative effect adjustment to the opening balance of retained earnings would be recognized as of January 1, 2019. There was no cumulative effect adjustment recognized. The Company elected the ASU's package of three practical expedients, which allowed the Company to forego a reassessment of (1) whether any expired or existing contracts are, or contain, leases, (2) the lease classification for any expired or existing leases, and (3) the initial direct costs for any existing leases. The Company has implemented a lease management system to assist in accounting for all leases. The January 1, 2019 impact of adopting this standard was to record right-of-use assets totaling $43.3 million and additional lease liabilities totaling $45.8 million, based on the present value of expected remaining lease payments.

Accounting standards not yet adopted		
Standard	**Summary of guidance**	**Effects on financial statements**
Topic 350 - Intangibles - Goodwill and Other: Simplifying the Test for Goodwill Impairment **ASU 2017 - 04** **Issued January 2017**	Simplifies goodwill impairment testing by eliminating the second step of the analysis under which the implied fair value of goodwill is determined as if the reporting unit were being acquired in a business combination. Requires the entity to instead compare the fair value of a reporting unit with its carrying amount and recognize an impairment charge for any amount by which the carrying amount exceeds the reporting unit's fair value, to the extent that the loss recognized does not exceed the amount of goodwill allocated to that reporting unit.	Effective for fiscal years ending after December 15, 2019. The guidance is to be applied on a prospective basis. Early adoption is permitted. The Company does not expect the adoption of this guidance to have a material impact on its Consolidated Financial Statements.
Topic 715 - Compensation - Retirement Benefits **Subtopic 715 - 20 - Defined Benefit Plans - General: Disclosure Framework - Changes in the Disclosure Requirements for Defined Benefit Plans** **ASU 2018 - 14** **Issued August 2018**	Removes, adds, and clarifies certain required financial statement disclosures that apply to all employers that sponsor defined benefit pension or other postretirement plans.	Effective for fiscal years ending after December 15, 2020. Early adoption is permitted. The Company is currently evaluating the impact the pronouncement will have on its Consolidated Financial Statements, but does not expect the adoption of this guidance to have a material impact.
Topic 740 - Income Taxes: Simplifying the Accounting for Income Taxes **ASU 2019 - 12** **Issued December 2019**	Simplifies the accounting for income taxes by removing certain exceptions to the general principles in Topic 740. Improves the consistent application and simplification of GAAP for other areas of Topic 740 by clarifying and amending existing guidance.	Effective for interim and annual periods beginning after December 15, 2020. The Company is currently evaluating the impact the pronouncement will have on its Consolidated Financial Statements, but does not expect the adoption of this guidance to have a material impact.

NOTE 2: MERGERS AND ACQUISITIONS

Angel Insurance and Financial Services, Inc.: Effective September 1, 2019, the Company acquired Angel, an independent insurance agency, which was merged into the operations of Towne Insurance Agency, LLC, a wholly owned subsidiary of TowneBank. The acquisition was accounted for as a business combination under the acquisition method of accounting in accordance with ASC 805, *Business Combinations,* and, as such, the assets acquired and liabilities assumed in the transaction were recorded at their respective fair values as of the acquisition date. Such fair values were preliminary estimates and are subject to adjustment for up to one year after the merger date, or when additional information relative to the closing date fair values becomes available and such information is considered final, whichever is earlier. Primary areas of the preliminary allocation of the fair value of consideration transferred that are not yet finalized relate to the fair values of certain intangible assets acquired and the residual goodwill. The results of operations of the acquired business were included in the Company's Consolidated Statements of Income commencing September 1, 2019.

Straus, Itzkowitz & LeCompte Insurance Agency, Inc.: Effective January 1, 2019, the Company acquired SIL, an independent insurance agency, which was merged into the operations of Towne Insurance Agency, LLC, a wholly owned subsidiary of TowneBank. The acquisition was accounted for as a business combination under the acquisition method of accounting in accordance with ASC 805, *Business Combinations,* and, as such, the assets acquired and liabilities assumed in the transaction were recorded at their respective fair values as of the acquisition date. Such fair values were preliminary estimates and were subject to adjustment for up to one year after the merger date, or when additional information relative to the closing date fair values becomes available and such information is considered final, whichever is earlier. Primary areas of the allocation of the fair value of consideration transferred related to the fair values of certain intangible assets acquired and the residual goodwill. The results of operations of the acquired business were included in the Company's Consolidated Statements of Income commencing January 1, 2019.

Middle Peninsula Insurance Agency, Inc.: Effective November 6, 2018, the Company acquired Middle Peninsula Insurance Agency, Inc., an independent insurance agency, which was merged into the operations of Towne Insurance Agency, LLC, a wholly owned subsidiary of TowneBank. The acquisition was accounted for as a business combination under the acquisition method of accounting in accordance with ASC 805, *Business Combinations,* and, as such, the assets acquired and liabilities assumed in the transaction were recorded at their respective fair values as of the acquisition date. Such fair values were preliminary estimates and were subject to adjustment for up to one year after the merger date, or when additional information relative to the closing date fair values became available and such information was considered final. Primary areas of the allocation of the fair value of consideration transferred related to the fair values of certain intangible assets acquired and the residual goodwill. The results of operations of the acquired business are included in the Company's Consolidated Statements of Income commencing November 6, 2018.

Michael R. Bare, LLC: Effective May 15, 2018, the Company acquired Michael R. Bare, LLC, an independent insurance agency, which was merged into the operations of Towne Insurance Agency, LLC, a wholly owned subsidiary of TowneBank. The acquisition was accounted for as a business combination under the acquisition method of accounting in accordance with ASC 805, *Business Combinations*, and, as such, the assets acquired and liabilities assumed in the transaction were recorded at their respective fair values as of the acquisition date. Such fair values were preliminary estimates and were subject to adjustment for up to one year after the merger date, or when additional information relative to the closing date fair values becomes available and such information is considered final. Primary areas of the allocation of the fair value of consideration transferred related to the fair values of certain intangible assets acquired and the residual goodwill. The results of operations of the acquired business are included in the Company's Consolidated Statements of Income commencing May 15, 2018.

Paragon Commercial Corporation: Effective January 26, 2018, TowneBank completed its acquisition of Paragon in an all-stock transaction. As part of the merger, Paragon merged with and into TB Acquisition, LLC, a wholly owned subsidiary of TowneBank, and Paragon Bank, a wholly owned subsidiary of Paragon, merged with and into TowneBank.

In the merger with Paragon, each outstanding share of Paragon common stock was converted into the right to receive 1.725 shares of TowneBank common stock. TowneBank issued an aggregate of 9.43 million shares of its common stock to former Paragon stockholders. Based on the closing price of TowneBank's common stock on January 26, 2018, of $31.20 per share, the aggregate consideration paid to former Paragon common stockholders and holders of equity awards to acquire Paragon common stock was approximately $294.07 million.

Paragon Bank was headquartered in Raleigh, North Carolina and had three branches serving the metropolitan areas of Charlotte and Raleigh, North Carolina. TowneBank engaged in this transaction with the expectation that it would expand its community banking franchise into new geographic markets that it believes are demographically attractive and rapidly growing. The integration of Paragon Bank's deposit system and the conversion of Paragon Bank's branches to TowneBank's operating platform were completed over the weekend of January 27-28, 2018.

The Paragon merger has been accounted for under the acquisition method of accounting. Under this guidance, an entity is required to recognize the assets acquired, liabilities assumed, and consideration given at their fair value on the acquisition date. The assets and liabilities, both tangible and intangible, were recorded at their estimated fair values as of the January 26, 2018, merger date. Such fair values were preliminary estimates and were subject to adjustment for up to one year after the merger date, or when additional information relative to the closing date fair values became available and such information was considered final. The fair value of consideration exchanged exceeded the recognized amounts of the identifiable net assets and resulted in goodwill of $149.73 million. Goodwill resulted from a combination of expected synergies, expansion in the metropolitan areas of Charlotte and Raleigh, North Carolina, with the addition of three branch locations, and growth opportunities. None of the goodwill recognized is expected to be deductible for income tax purposes

The following table presents the estimated fair values of the assets acquired and liabilities assumed for Paragon as of January 26, 2018 (dollars in thousands):

Fair value of assets acquired:		
Cash and cash equivalents	$	79,372
Securities available for sale		184,184
Loans held for investment		1,432,497
Bank premises and equipment		13,647
OREO		1,330
Core deposit intangible		21,520
Other assets		69,315
Total assets	$	1,801,865
Fair value of liabilities assumed:		
Deposits	$	1,248,636
Total borrowings		378,558
Other liabilities		30,326
Total liabilities	$	1,657,520
Net identifiable assets acquired		144,345
Goodwill		149,725
Net assets acquired	$	294,070
Purchase price:		
Company common shares issued		9,425,213
Purchase price per share of Company’s common stock	$	31.20
Common stock issued	$	294,067
Cash exchanged for fractional shares		3
Fair value of total consideration transferred	$	294,070

The loans acquired in the Paragon merger were divided into loans with evidence of credit quality deterioration, which are accounted for under ASC 310-30 (purchased impaired), and loans that do not meet this criteria, which are accounted for under ASC 310-20 (purchased performing). As of January 26, 2018, the estimated fair value of the Paragon purchased performing loans acquired was $1.42 billion, the related gross contractual amount was $1.67 billion, and the estimated contractual cash flows not expected to be collected were $12.51 million.

The following table presents the acquired impaired loans receivable at the acquisition date, as adjusted (dollars in thousands):

Contractual principal and interest at acquisition	$	26,697
Nonaccretable difference		(10,672)
Expected cash flows at acquisition		16,025
Accretable yield		(1,857)
Estimated fair value of loans acquired with a deterioration of credit quality	$	14,168

NOTE 3: INVESTMENT SECURITIES

Available-for-sale securities

The following chart indicates the amortized cost and fair values of AFS securities for the periods indicated (in thousands):

December 31, 2019

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. agency securities	$ 128,451	$ 788	$ (201)	$ 129,038
U.S. Treasury notes	1,000	—	—	1,000
Municipal securities	217,911	6,032	(837)	223,106
Trust preferred and other corporate securities	51,724	1,668	(25)	53,367
Mortgage-backed securities issued by GSE	1,022,487	15,462	(3,152)	1,034,797
Total available-for-sale securities	$ 1,421,573	$ 23,950	$ (4,215)	$ 1,441,308

December 31, 2018

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. agency securities	$ 362,272	$ 143	$ (3,873)	$ 358,542
U.S. Treasury notes	1,247	—	(1)	1,246
Municipal securities	87,044	679	(415)	87,308
Trust preferred and other corporate securities	30,498	601	(107)	30,992
Mortgage-backed securities issued by GSE	626,188	2,000	(10,937)	617,251
Total available-for-sale securities	$ 1,107,249	$ 3,423	$ (15,333)	$ 1,095,339

For the year ended December 31, 2019, the Company had proceeds from sales of securities AFS in the amount of $186.04 million, resulting in gross realized losses of $1.28 million and gross realized gains of $0.43 million. Despite the losses on these securities, they were not considered OTTI at the time of sale, as the losses were driven by interest rate fluctuations, rather than credit quality issues. We sold the securities in order to position our portfolio for better yield, going forward. For the year ended December 31, 2018, the Company had proceeds from sales of securities AFS in the amount of $48.55 million, resulting in gross realized gains of $3,000. For the year ended December 31, 2017, there were proceeds from sales of securities AFS in the amount of $0.31 million, resulting in gross realized losses of $1,000.

Held-to-maturity securities

The amortized cost and fair values of HTM investment securities for the periods indicated (in thousands):

December 31, 2019

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Trust preferred and other corporate securities	$ 2,369	$ 230	$ —	$ 2,599
Municipal securities	29,167	1,221	—	30,388
Mortgage-backed securities issued by GSE	12,152	69	(37)	12,184
Total held-to-maturity securities	$ 43,688	$ 1,520	$ (37)	$ 45,171

December 31, 2018	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Trust preferred and other corporate securities	$ 500	$ 176	$ —	$ 676
Municipal securities	34,488	1,053	—	35,541
Mortgage-backed securities issued by GSE	15,610	42	(601)	15,051
Total held-to-maturity securities	$ 50,598	$ 1,271	$ (601)	$ 51,268

Maturities of investment securities

Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. The amortized cost and estimated fair value of investment securities are shown by contractual maturity (including MBSs) in the following tables (in thousands):

December 31, 2019	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 60,390	$ 60,390	$ —	$ —
Due after one year through five years	57,854	59,051	17,334	17,445
Due after five years through ten years	661,270	668,119	16,407	16,824
Due after ten years	642,059	653,748	9,947	10,902
	1,421,573	1,441,308	43,688	45,171
Other equity securities	6,462	6,462	—	—
	$ 1,428,035	$ 1,447,770	$ 43,688	$ 45,171

December 31, 2018	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 114,888	$ 113,956	$ —	$ —
Due after one year through five years	273,327	270,256	10,612	10,568
Due after five years through ten years	200,418	198,564	31,814	31,895
Due after ten years	518,616	512,563	8,172	8,805
	1,107,249	1,095,339	50,598	51,268
Other equity securities	4,797	4,797	—	—
	$ 1,112,046	$ 1,100,136	$ 50,598	$ 51,268

Pledged securities

At December 31, 2019 and 2018, the Company had investment securities with market values of $306.25 million and $232.61 million, respectively, pledged to secure federal, state, and municipal deposits. Additionally, the Company had no investment securities pledged to secure borrowings from the FRB - Richmond at December 31, 2019 or 2018. The Company also had $64.62 million in investment securities pledged against repurchase agreements with commercial customers at December 31, 2019, compared to $66.24 million at December 31, 2018.

Unrealized losses

The following tables show the Company's gross unrealized losses and fair values aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position for the periods indicated (in thousands, except number of securities):

December 31, 2019	Less than 12 months			12 months or more		Total	
Description of Securities	**Number**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
U.S. Treasury obligations and direct obligations of U.S. government agencies	4	$ 29,035	$ (192)	$ 39,992	$ (9)	$ 69,027	$ (201)
Municipal securities	14	62,153	(836)	502	(1)	62,655	(837)
Mortgage-backed securities issued by GSE	58	377,146	(2,401)	61,751	(788)	438,897	(3,189)
Trust preferred and other corporate obligations	1	3,052	(25)	—	—	3,052	(25)
Total temporarily impaired securities	77	$ 471,386	$ (3,454)	$ 102,245	$ (798)	$ 573,631	$ (4,252)

December 31, 2018	Less than 12 months			12 months or more		Total	
Description of Securities	**Number**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
U.S. Treasury obligations and direct obligations of U.S. government agencies	18	$ 120,117	$ (1,100)	$ 227,833	$ (2,774)	$ 347,950	$ (3,874)
Municipal securities	40	22,758	(250)	11,672	(165)	34,430	(415)
Mortgage-backed securities issued by GSE	77	172,481	(1,987)	243,672	(9,551)	416,153	(11,538)
Trust preferred and other corporate obligations	3	6,001	(46)	20,548	(61)	26,549	(107)
Total temporarily impaired securities	138	$ 321,357	$ (3,383)	$ 503,725	$ (12,551)	$ 825,082	$ (15,934)

At December 31, 2019, the Company's unrealized losses on securities were caused by interest rate fluctuations. The severity and duration of these unrealized losses will fluctuate with interest rates in the economy. Based on the credit quality of the issuers, and because the Company does not intend to sell these securities, and it is not more likely than not that the Company will be required to sell the securities before their anticipated recovery, the Company does not consider these investments OTTI.

Federal Home Loan Bank stock

The Company is required to maintain an investment in the capital stock of the FHLB. The FHLB stock is stated at cost, as this is a restricted security without a readily determinable fair value. The Company had $30.09 million and $43.23 million of FHLB stock at December 31, 2019 and 2018, respectively. Based on the Company's review of the credit quality of the institution, the institution's ability to repurchase shares, and the Company's carrying value in the shares, the Company does not consider this investment impaired.

NOTE 4: LOANS AND ALLOWANCE FOR LOAN LOSSES

The Company grants commercial, real estate, and consumer loans to customers throughout our lending area. Although the Company has a diversified loan portfolio, a substantial portion of the Company's debtors' abilities to honor their contracts is dependent upon the economic environment of the lending area.

A summary of loan balances by major classification (in thousands):

December 31,	2019	2018
Real estate loans:		
1-4 family residential	$ 1,653,084	$ 1,626,896
Commercial	3,512,376	3,241,340
Construction and land development	1,120,533	1,067,239
Multifamily	243,041	260,987
Total real estate loans	6,529,034	6,196,462
Commercial and industrial business	1,574,275	1,510,364
Consumer loans and other	315,979	311,407
Loans, net of unearned income and deferred costs	$ 8,419,288	$ 8,018,233

Unearned loan income was $8.98 million in excess of deferred loan costs at December 31, 2019, $7.06 million at December 31, 2018, and $4.83 million at December 31, 2017. There were $17.44 million, $4.75 million, and $4.81 million in nonaccrual loans at December 31, 2019, 2018, and 2017, respectively. The Company would have earned $0.58 million in 2019, $0.23 million in 2018, and $0.14 million in 2017 if interest on the loans had been accruing. Of total loans, $1.48 billion were pledged as collateral to secure overnight borrowings with the FHLB, and $122.39 million was pledged to secure borrowings from the discount window at the FRB - Richmond at December 31, 2019.

Allowance for Loan Losses

The total allowance reflects management's estimate of loan losses inherent in the loan portfolio at the balance sheet date. While portions of the allowance are attributed to specific portfolio segments, the entire allowance is available to absorb credit losses inherent in the total loan portfolio. The Company considers the allowance for loan losses of $58.23 million adequate to cover loan losses inherent in the loan portfolio at December 31, 2019. The following table presents, by portfolio segment, the changes in the allowance for loan losses for the years ended December 31, 2019, 2018, and 2017 (in thousands):

December 31, 2019	Real Estate Construction and Land Development	Real Estate Commercial	Real Estate Multi-Family	Real Estate 1-4 Family Residential	Commercial and Industrial Business	Consumer and Other Loans	Total
Allowance for loan losses:							
Balance, beginning of year	$ 6,171	$ 19,488	$ 1,011	$ 10,245	$ 8,669	$ 6,510	$ 52,094
Provision charged to expense	654	5,013	36	841	2,003	824	9,371
Losses charged off	(43)	(1,298)	—	(1,098)	(984)	(1,068)	(4,491)
Recoveries	144	38	—	635	148	295	1,260
Balance, end of year	$ 6,926	$ 23,241	$ 1,047	$ 10,623	$ 9,836	$ 6,561	$ 58,234
December 31, 2018							
Allowance for loan losses:							
Balance, beginning of year	$ 5,753	$ 16,864	$ 1,075	$ 9,345	$ 6,596	$ 5,498	$ 45,131
Provision charged to expense	416	2,760	(64)	1,471	2,526	1,432	8,541
Losses charged off	(72)	(168)	—	(1,102)	(716)	(748)	(2,806)
Recoveries	74	32	—	531	263	328	1,228
Balance, end of year	$ 6,171	$ 19,488	$ 1,011	$ 10,245	$ 8,669	$ 6,510	$ 52,094
December 31, 2017							
Allowance for loan losses:							
Balance, beginning of year	$ 4,280	$ 16,248	$ 1,370	$ 9,050	$ 6,410	$ 4,643	$ 42,001
Provision charged to expense	1,439	416	(297)	2,300	449	1,119	5,426
Losses charged off	—	(139)	—	(2,291)	(345)	(644)	(3,419)
Recoveries	34	339	2	286	82	380	1,123
Balance, end of year	$ 5,753	$ 16,864	$ 1,075	$ 9,345	$ 6,596	$ 5,498	$ 45,131

The following table presents, by portfolio segment, the allocation of the allowance for loan losses at December 31, 2019 and 2018 (in thousands):

December 31, 2019	Real Estate Construction and Land Development	Real Estate Commercial	Real Estate Multi-Family	Real Estate 1-4 Family Residential	Commercial and Industrial Business	Consumer and Other Loans	Total
Period-end balance allocated to:							
Loans individually evaluated for impairment	$ 16	$ 472	$ 39	$ 427	$ 267	$ 41	$ 1,262
Loans collectively evaluated for impairment	6,910	22,769	1,008	10,068	9,484	6,520	56,759
Loans acquired with deteriorated credit quality	—	—	—	128	85	—	213
Balance, end of year	$ 6,926	$ 23,241	$ 1,047	$ 10,623	$ 9,836	$ 6,561	$ 58,234
December 31, 2018							
Period-end balance allocated to:							
Loans individually evaluated for impairment	$ 13	$ 557	$ 42	$ 629	$ 82	$ 29	$ 1,352
Loans collectively evaluated for impairment	6,158	18,931	969	9,547	8,587	6,481	50,673
Loans acquired with deteriorated credit quality	—	—	—	69	—	—	69
Balance, end of year	$ 6,171	$ 19,488	$ 1,011	$ 10,245	$ 8,669	$ 6,510	$ 52,094

The following table presents, by portfolio segment, the Company's investment in loans (in thousands):

December 31, 2019	Real Estate Construction and Land Development	Real Estate Commercial	Real Estate Multi-Family	Real Estate 1-4 Family Residential	Commercial and Industrial Business	Consumer and Other Loans	Total
Ending balance: individually evaluated for impairment	$ 1,415	$ 21,123	$ 3,941	$ 15,105	$ 5,383	$ 1,296	$ 48,263
Ending balance: collectively evaluated for impairment	1,118,463	3,464,328	233,254	1,619,314	1,568,892	314,683	8,318,934
Ending balance: loans acquired with deteriorated credit quality	655	26,925	5,846	18,665	—	—	52,091
Ending Balance	$ 1,120,533	$ 3,512,376	$ 243,041	$ 1,653,084	$ 1,574,275	$ 315,979	$ 8,419,288
December 31, 2018							
Ending balance: individually evaluated for impairment	$ 1,589	$ 18,924	$ 1,158	$ 12,467	$ 12,923	$ 938	$ 47,999
Ending balance: collectively evaluated for impairment	1,052,383	3,202,982	247,571	1,592,449	1,497,441	310,469	7,903,295
Ending balance: loans acquired with deteriorated credit quality	13,267	19,434	12,258	21,980	—	—	66,939
Ending Balance	$ 1,067,239	$ 3,241,340	$ 260,987	$ 1,626,896	$ 1,510,364	$ 311,407	$ 8,018,233

Loans acquired in a transfer, including business combinations, where there is evidence of credit deterioration since origination and it is probable at the date of acquisition that we will not collect all contractually required principal and interest payments, are accounted for as purchased impaired loans. Purchased impaired loans are initially recorded at fair value, which includes estimated future credit losses expected to be incurred over the life of the loan. Accordingly, the historical allowance for credit losses related to these loans is not carried over.

Accounting for purchased impaired loans involves estimating fair value, at acquisition, using the principal and interest cash flows expected to be collected discounted at the prevailing market rate of interest. The excess of cash flows expected to be collected over the estimated fair value at acquisition date is referred to as the accretable yield and is recognized in interest income using an effective yield method over the remaining life of the loans. The difference between contractually required payments and the cash flows expected to be collected at acquisition, considering the impact of prepayments, is referred to as the nonaccretable difference. Any decreases in cash flows expected to be collected (other than due to decreases in interest rate indices and changes in prepayment assumptions) will be charged to the provision for loan losses, resulting in an increase to the allowance for loan losses.

The following table presents changes in the accretable yield for purchased impaired loans for the years ended December 31, 2019 and 2018 (in thousands):

	December 31,	
	2019	2018
Balance at beginning of period	$ 35,461	$ 38,542
Additions	—	1,857
Accretion	(7,312)	(10,686)
Reclassifications from nonaccretable balance, net	3,564	6,469
Other changes, net	(4,772)	(721)
Balance at end of period	$ 26,941	$ 35,461

At December 31, 2019, none of the purchased impaired loans were classified as nonperforming assets. Therefore, interest income, through accretion of the difference between the carrying amount of the loans and expected cash flows, is being recognized on all purchased loans. Any decreases in cash flows expected to be collected (other than due to decreases in interest rate indices and changes in prepayment assumptions), will be charged to the provision for loan losses, resulting in an increase to the allowance for loan losses.

Portfolio Quality Indicators

The Company's portfolio grading analysis estimates the capability of the borrower to repay the contractual obligations of the loan agreements as scheduled or at all. The Company's internal credit risk grading system is based on numerous factors, including management's experiences with similarly graded loans. Credit risk grades on impaired credits are refreshed each quarter as they become available, at which time management analyzes the resulting scores, as well as other external statistics and factors, to track loan performance.

The Company's internally assigned grades are as follows:

- Pass – Several pass credit grades comprise loans in this category, which are assigned based on varying levels of risk, ranging from credits that are secured by cash or marketable securities, to management attention credits which have all the characteristics of an acceptable credit risk but warrant more than the normal level of monitoring.

- Special Mention – Loans in this category are considered to have potential weaknesses that deserve management's attention. The borrower's ability to repay from the primary (intended) sources is currently adequate, but threatened by potential weaknesses which may, if not corrected, result in the deterioration of the repayment prospects for the asset or in the Company's credit position loss at some future date.

- Substandard – Loans in this category are considered to have increased credit risk and servicing needs and generally require that the Company follow their performance very closely. The borrower's ability to repay is threatened by a clearly defined weakness which jeopardizes ultimate repayment of the loan.

- Doubtful – Loans in this category are considered to be doubtful or a loss to the Company in terms of principal and interest repayment. The borrower's ability to repay in full, on the basis of currently existing facts, conditions, and values, is generally highly questionable and improbable.

The following tables represent credit exposures by internally assigned grades for the years ended December 31, 2019 and 2018 (in thousands):

December 31, 2019	Real Estate Construction and Land Development	Real Estate Commercial	Real Estate Multi-Family	Real Estate 1-4 Family Residential	Commercial and Industrial Business	Consumer and Other Loans	Total
Pass	$ 1,106,773	$ 3,478,967	$ 239,099	$ 1,633,695	$ 1,560,041	$ 314,683	$8,333,258
Special Mention	12,613	15,155	692	4,295	6,752	—	39,507
Substandard	1,147	18,254	3,250	15,094	7,482	1,296	46,523
Doubtful	—	—	—	—	—	—	—
Total	$ 1,120,533	$ 3,512,376	$ 243,041	$ 1,653,084	$ 1,574,275	$ 315,979	$8,419,288
December 31, 2018							
Pass	$ 1,048,291	$ 3,217,386	$ 256,977	$ 1,612,970	$ 1,490,207	$ 310,364	$7,936,195
Special Mention	16,981	8,234	3,559	3,228	4,416	104	36,522
Substandard	1,967	15,720	451	10,698	15,741	939	45,516
Doubtful	—	—	—	—	—	—	—
Total	$ 1,067,239	$ 3,241,340	$ 260,987	$ 1,626,896	$ 1,510,364	$ 311,407	$8,018,233

Age Analysis of Past-Due Financing Receivables by Class

The following table includes an aging analysis of the recorded investment of past-due financing receivables as of December 31, 2019. Also included are loans that are 90 days or more past due as to interest and principal and still accruing, because they are (i) well-secured and in the process of collection, or (ii) real estate loans or loans exempt under regulatory rules from being classified as nonaccrual. Purchased impaired loans are included in the aging schedule, but are excluded from the disclosure of accruing loans more than 90 days past due as they are considered to be accruing due to the existence of the accretable yield and not based on consideration given to contractual interest payments (in thousands).

	Loans 30 - 59 Days Past Due	Loans 60 - 89 Days Past Due	Loans 90 or More Days Past Due	Nonaccrual Loans	Total Past Due and Nonaccruing	Current Loans	Total Loans Receivable	Accruing Loans More Than 90 Days Past Due
December 31, 2019								
Real estate - construction and development	$ 240	$ 323	$ —	$ 43	$ 606	$ 1,119,927	$ 1,120,533	$ —
Real estate - commercial	1,238	199	45	7,513	8,995	3,503,381	3,512,376	—
Real estate - multi-family	—	—	—	—	—	243,041	243,041	—
Real estate - residential 1-4 family	6,470	326	505	5,973	13,274	1,639,810	1,653,084	244
Commercial and industrial business	347	55	—	3,284	3,686	1,570,589	1,574,275	—
Consumer and other loans	1,289	148	65	624	2,126	313,853	315,979	65
Total	$ 9,584	$ 1,051	$ 615	$ 17,437	$ 28,687	$ 8,390,601	$ 8,419,288	$ 309
December 31, 2018								
Real estate - construction and development	$ 1,292	$ 452	$ 611	$ —	$ 2,355	$ 1,064,884	$ 1,067,239	$ —
Real estate - commercial	2,740	292	—	538	3,570	3,237,770	3,241,340	—
Real estate - multi-family	—	—	—	—	—	260,987	260,987	—
Real estate - residential 1-4 family	5,859	1,415	320	1,954	9,548	1,617,348	1,626,896	209
Commercial and industrial business	184	14	—	1,820	2,018	1,508,346	1,510,364	—
Consumer and other loans	1,462	623	185	437	2,707	308,700	311,407	185
Total	$ 11,537	$ 2,796	$ 1,116	$ 4,749	$ 20,198	$ 7,998,035	$ 8,018,233	$ 394

The following table includes an aging analysis of the recorded investment of purchased impaired loans included in the table above (in thousands):

	Loans 30 - 59 Days Past Due	Loans 60 - 89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due	Current Loans	Total Loans Receivable
December 31, 2019						
Real estate - construction and development	$ 13	$ —	$ —	$ 13	$ 642	$ 655
Real estate - commercial	—	—	45	45	26,880	26,925
Real estate - multi-family	—	—	—	—	5,846	5,846
Real estate - residential 1-4 family	313	129	260	702	17,963	18,665
Total	$ 326	$ 129	$ 305	$ 760	$ 51,331	$ 52,091

	Loans 30 - 59 Days Past Due	Loans 60 - 89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due	Current Loans	Total Loans Receivable
December 31, 2018						
Real estate - construction and development	$ 11	$ —	$ 611	$ 622	$ 12,645	$ 13,267
Real estate - commercial	424	—	—	424	19,010	19,434
Real estate - multi-family	—	—	—	—	12,258	12,258
Real estate - residential 1-4 family	83	315	111	509	21,471	21,980
Total	$ 518	$ 315	$ 722	$ 1,555	$ 65,384	$ 66,939

Impaired Loans

Management considers a loan to be impaired when, based on current information and events, it is determined that the Company will not be able to collect all amounts due according to the loan contract, including scheduled interest payments. Determination of impairment is treated the same across all classes of loans. When management identifies a loan as impaired, the impairment is measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate, except when the sole (remaining) source of repayment for the loan is the operation or liquidation of the collateral. In these cases, management uses the current fair value of the collateral, less selling costs when foreclosure is probable, instead of discounted cash flows. If management determines that the value of the impaired loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs, and unamortized premium or discount), impairment is recognized as a specific component to be provided for in the allowance for loan losses, or the impaired balance on collateral dependent loans is charged off if it is determined that such amount represents a confirmed loss. Smaller balance loans (under $1,000,000) are generally not individually assessed for impairment but are evaluated collectively.

When the ultimate collectability of the total principal of an impaired loan is in doubt and the loan is on nonaccrual status, all payments are applied to principal under the cost-recovery method. When the ultimate collectability of the total principal of an impaired loan is not in doubt and the loan is on nonaccrual status, contractual interest is credited to interest income when received under the cash-basis method.

The following table includes the recorded investment, excluding interest receivable, and unpaid principal balances for impaired financing receivables, excluding purchased impaired loans, with the associated allowance amount, if applicable (in thousands):

December 31, 2019	Unpaid Principal Balance	Recorded Investment	Specific Allowance	Average Recorded Investment	Interest Income Recognized
Loans without a specific valuation allowance					
Real estate - construction and development	$ 43	$ 43	$ —	$ 48	$ 2
Real estate - commercial	8,226	8,058	—	8,500	396
Real estate - multi-family	2,852	2,852	—	2,852	127
Real estate - residential 1-4 family	7,211	6,999	—	7,029	322
Commercial and industrial business	3,500	3,213	—	3,255	206
Consumer and other loans	—	—	—	—	—
Total	$ 21,832	$ 21,165	$ —	$ 21,684	$ 1,053
Loans with a specific valuation allowance					
Real estate - construction and development	$ 1,372	$ 1,372	$ 16	$ 1,386	$ 71
Real estate - commercial	13,216	13,065	472	13,395	737
Real estate - multi-family	1,089	1,089	39	1,124	71
Real estate - residential 1-4 family	8,423	8,106	427	9,114	509
Commercial and industrial business	2,277	2,170	267	2,293	131
Consumer and other loans	1,335	1,296	41	1,418	79
Total	$ 27,712	$ 27,098	$ 1,262	$ 28,730	$ 1,598
Total impaired loans					
Real estate - construction and development	$ 1,415	$ 1,415	$ 16	$ 1,434	$ 73
Real estate - commercial	21,442	21,123	472	21,895	1,133
Real estate - multi-family	3,941	3,941	39	3,976	198
Real estate - residential 1-4 family	15,634	15,105	427	16,143	831
Commercial and industrial business	5,777	5,383	267	5,548	337
Consumer and other loans	1,335	1,296	41	1,418	79
Total	$ 49,544	$ 48,263	$ 1,262	$ 50,414	$ 2,651

Included in the table above are accruing TDRs of $15.02 million, which the Company has designated as performing loans, while nonaccruing TDRs, which are also included in the above table of impaired loans, totaled $2.27 million.

December 31, 2018	Unpaid Principal Balance	Recorded Investment	Specific Allowance	Average Recorded Investment	Interest Income Recognized
Loans without a specific valuation allowance					
Real estate - construction and development	$ 452	$ 452	$ —	$ 397	$ 23
Real estate - commercial	5,441	5,441	—	5,483	274
Real estate - multi-family	—	—	—	—	—
Real estate - residential 1-4 family	2,457	2,456	—	2,375	89
Commercial and industrial business	10,893	10,605	—	11,363	582
Consumer and other loans	—	—	—	—	—
Total	$ 19,243	$ 18,954	$ —	$ 19,618	$ 968
Loans with a specific valuation allowance					
Real estate - construction and development	$ 1,137	$ 1,137	$ 13	$ 1,163	$ 62
Real estate - commercial	13,672	13,483	557	14,165	856
Real estate - multi-family	1,158	1,158	42	1,188	76
Real estate - residential 1-4 family	10,304	10,011	629	10,500	527
Commercial and industrial business	2,405	2,318	82	3,034	169
Consumer and other loans	971	938	29	1,096	50
Total	$ 29,647	$ 29,045	$ 1,352	$ 31,146	$ 1,740
Total impaired loans					
Real estate - construction and development	$ 1,589	$ 1,589	$ 13	$ 1,560	$ 85
Real estate - commercial	19,113	18,924	557	19,648	1,130
Real estate - multi-family	1,158	1,158	42	1,188	76
Real estate - residential 1-4 family	12,761	12,467	629	12,875	616
Commercial and industrial business	13,298	12,923	82	14,397	751
Consumer and other loans	971	938	29	1,096	50
Total	$ 48,890	$ 47,999	$ 1,352	$ 50,764	$ 2,708

Included in the table above are accruing TDRs of $21.20 million, which the Company has designated as performing loans, while nonaccruing TDRs, which are also included in the above table of impaired loans, totaled $0.90 million.

December 31, 2017	Unpaid Principal Balance	Recorded Investment	Specific Allowance	Average Recorded Investment	Interest Income Recognized
Loans without a specific valuation allowance					
Real estate - construction and development	$ 151	$ 151	$ —	$ 162	$ 13
Real estate - commercial	11,959	11,886	—	12,667	689
Real estate - multi-family	—	—	—	—	—
Real estate - residential 1-4 family	2,432	2,282	—	2,603	102
Commercial and industrial business	2,825	2,641	—	3,017	158
Consumer and other loans	—	—	—	—	—
Total	$ 17,367	$ 16,960	$ —	$ 18,449	$ 962
Loans with a specific valuation allowance					
Real estate - construction and development	$ 2,773	$ 2,401	$ 34	$ 2,799	$ 124
Real estate - commercial	10,384	10,296	789	10,840	524
Real estate - multi-family	1,218	1,218	30	1,252	80
Real estate - residential 1-4 family	12,353	12,177	938	13,893	667
Commercial and industrial business	1,726	1,612	47	1,847	105
Consumer and other loans	779	767	7	868	34
Total	$ 29,233	$ 28,471	$ 1,845	$ 31,499	$ 1,534
Total impaired loans					
Real estate - construction and development	$ 2,924	$ 2,552	$ 34	$ 2,961	$ 137
Real estate - commercial	22,343	22,182	789	23,507	1,213
Real estate - multi-family	1,218	1,218	30	1,252	80
Real estate - residential 1-4 family	14,785	14,459	938	16,496	769
Commercial and industrial business	4,551	4,253	47	4,864	263
Consumer and other loans	779	767	7	868	34
Total	$ 46,600	$ 45,431	$ 1,845	$ 49,948	$ 2,496

Included in the table above are accruing TDRs of $24.83 million, which the Company has designated as performing loans, while nonaccruing TDRs, which are also included in the above table of impaired loans, totaled $1.38 million.

Troubled Debt Restructurings

In order to maximize the collection of loan balances, the Company evaluates troubled loan accounts on a case-by-case basis to determine if a loan modification would be appropriate. Loan modifications may be utilized when there is a reasonable chance that an appropriate modification would allow our clients to continue servicing the debt. A loan is a troubled debt restructuring if both of the following exist: (i) a creditor has granted a concession to the debtor, and (ii) the debtor is experiencing financial difficulties. Nonaccruing loans that are modified can be placed back on accrual status when both principal and interest are current, there is a sustained repayment performance of six months or greater, and it is probable that we will be able to collect all amounts due (both principal and interest) according to the terms of the loan agreement. All restructured loans are considered impaired in the calendar year of restructuring. In subsequent years, a restructured loan may cease being classified as impaired if the loan was modified at a market rate and has performed according to the modified terms for at least six months.

The following table shows the loans modified in TDRs for the year ended December 31, 2019 (in thousands, except number of loans). For the year ended December 31, 2018, there were no loans modified in TDRs.:

	Year Ended December 31, 2019		
	Number of Loans	Pre-Modification Recorded Balance	Post-Modification Recorded Balance
Construction and land development	2	$ 275	$ 275
Multifamily real estate	1	2,852	2,852
Total	3	$ 3,127	$ 3,127

The restructured loans generally include terms to reduce the interest rate and extend payment terms. We have not forgiven any principal on the above loans. Two loans were restructured within the last 12 months and subsequently defaulted. Two loans that were modified in TDRs during 2019 were paid off subsequent to modification as a TDR.

The specific reserve portion of the allowance for loan losses on TDRs is determined by discounting the restructured cash flows at the original effective rate of the loan before modification, or is based on the underlying collateral value less costs to sell, if repayment of the loan is collateral-dependent. If the resulting amount is less than the recorded book value, the Company either establishes a valuation allowance as a component of the allowance for loan losses or charges off the impaired balance if it determines that such amount is a confirmed loss. This method is used consistently for all segments of the portfolio. At December 31, 2019, the large majority of impaired loans have been determined to be collateral-dependent.

Nonaccrual Loans

The Company generally places loans on nonaccrual status when the full and timely collection of interest or principal becomes uncertain, part of the principal balance has been charged off and no restructuring has occurred, or the loans reach a certain number of days past due. Commercial loans are placed on nonaccrual status when full collection of principal and interest becomes doubtful, or when any portion of principal or interest becomes 90 days past due, whichever occurs first, unless the debt is both well-secured and in the process of collection. Residential mortgage loans and other consumer loans are placed on nonaccrual status when full collection of principal and interest becomes doubtful, or when any portion of principal or interest becomes 120 days past due, whichever occurs first, unless the debt is both well-secured and in the process of collection. When loans are placed on nonaccrual status, interest receivable is reversed against interest income recognized in the current period, and any prior year unpaid interest is charged off against the allowance for loan losses. Interest payments received thereafter are applied as a reduction of the remaining principal balance so long as doubt exists as to the ultimate collection of the principal. Loans are removed from nonaccrual status when they become current as to both principal and interest and when the collection of principal or interest is no longer doubtful. Similarly, mortgage loans and other consumer loans are also placed on nonaccrual status when full collection of principal and interest becomes doubtful, or they become delinquent for a specified period of time.

NOTE 5: OTHER REAL ESTATE OWNED

The table below presents a summary of the activity related to OREO (in thousands):

	Year Ended December 31,	
	2019	2018
Beginning balance	$ 19,416	$ 23,288
Additions and capital improvements	3,738	3,177
Paragon merger	—	1,330
Sales	(8,041)	(9,334)
Net change in valuation allowance	—	(73)
Gain on sale and write-downs, net	247	1,028
Ending balance	$ 15,360	$ 19,416

As of December 31, 2019, the Company's recorded investment in OREO collateralized by residential real estate was $2.18 million. As of December 31, 2019, the Company's recorded investment in mortgage loans collateralized by residential real estate that are in the process of foreclosure was $0.90 million.

NOTE 6: PREMISES AND EQUIPMENT

A summary of the cost and accumulated depreciation of premises and equipment is as follows (in thousands):

	Useful Life	December 31,	
		2019	2018
Land and improvements	—	$ 42,840	$ 39,599
Buildings and improvements	10 to 45 years	167,758	146,250
Autos	3 to 5 years	7,750	7,014
Computer equipment	2 to 5 years	15,953	14,333
Equipment	5 to 10 years	29,626	26,755
Furniture and fixtures	5 to 20 years	60,126	53,742
Leasehold improvements	Lesser of lease term or 10 years	34,869	31,021
Construction in progress	—	123	7,247
		359,045	325,961
Less accumulated depreciation		(127,239)	(114,165)
Net premises and equipment		$ 231,806	$ 211,796

Depreciation and leasehold amortization expense for the years ended December 31, 2019, 2018, and 2017, was $16.07 million, $15.91 million, and $15.90 million, respectively.

NOTE 7. LEASES

We lease certain office space, land, and equipment. These leases were all classified as operating leases. Leases with an initial term of 12 months or less are not recorded on our Consolidated Balance Sheets; we recognize lease expenses for these leases over the lease term. Certain leases include one or more options to renew, with renewal terms that can extend the lease term up to 15 years. The exercise of lease renewal options is at our sole discretion. When it is reasonably certain that we will exercise our option to renew or extend the lease term, that option is included in estimating the value of the right-of-use asset and lease liability.

At December 31, 2019, we did not have any leases that had not yet commenced for which we had created a right-of-use asset and a lease liability. For our operating leases we have elected the practical expedient of not separating lease components from non-lease components and instead to account for each separate lease component and the non-lease components associated with that lease as a single lease component. Our lease agreements do not contain any material residual value guarantees or material restrictive covenants. Most of our lease agreements include periodic rate adjustments for inflation. The depreciable life of assets and leasehold improvements are limited to the expected lease term.

Leases

(In thousands)	December 31, 2019	
Assets		
Operating lease assets included in other assets	$	47,515
Liabilities		
Accrued liability operating leases included in other liabilities	$	50,246

Lease Cost

	Year Ended December 31,			
(In thousands)	2019		2018	
Operating lease cost (1) included in occupancy expense	$	14,400	$	12,299
Sublease income included in occupancy expense		(53)		(283)
Net lease cost	$	14,347	$	12,016

(1) Includes short-term leases, which are immaterial.

Maturity of Lease Liabilities

(In thousands)	Operating Leases (1)	
2020		10,618
2021		8,274
2022		7,175
2023		5,874
2024		4,111
Thereafter		33,011
Total lease payments	$	69,063
Less: interest		18,817
Present value of lease liabilities	$	50,246

(1) Operating lease payments include $20.14 million related to options to extend lease terms that are reasonably certain of being exercised.
Note: Minimum lease payments exclude payments to landlords for real estate taxes and common area maintenance.

Lease Term and Discount Rate

Weighted - average remaining lease term - operating leases (in years)	12.01
Weighted - average discount rate - operating leases	4.55%

Other Information

(In thousands)		Year Ended December 31, 2019
Cash paid for amounts included in the measurement of lease liabilities		
Operating cash flows for operating leases	$	11,595
Related Party Transactions (1)		
Rent expense included in occupancy expense	$	2,806

(1) The Company rents space for various financial centers from companies associated with its directors.

Rental income for the year ended December 31, 2019, was $1.36 million, compared to $0.99 million for 2018, and $0.93 million for 2017. Future minimum rental income by year and in the aggregate, under noncancellable operating leases, was as follows at December 31, 2019 (in thousands):

2020	$	1,692
2021		1,003
2022		814
2023		593
2024		256
Thereafter		753
	$	5,111

NOTE 8: GOODWILL AND INTANGIBLE ASSETS

The gross carrying amount and accumulated amortization for the Company's intangible assets (in thousands):

	December 31,			
	2019		2018	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Intangible assets subject to amortization				
Core deposit intangible	$ 31,339	$ 14,933	$ 31,339	$ 9,773
Non-compete agreements	2,085	1,320	1,910	969
Customer lists	63,826	31,209	55,985	24,351
Total intangible assets subject to amortization	97,250	47,462	89,234	35,093
Intangible assets not subject to amortization				
Trade names	1,380	—	1,380	—
Contractual agreements	3,231	—	3,231	—
Total intangible assets not subject to amortization	4,611	—	4,611	—
Total intangible assets	$ 101,861	$ 47,462	$ 93,845	$ 35,093

The aggregate amortization expense for intangible assets with finite lives for the year ended December 31, 2019, was $12.37 million, compared to $11.71 million for 2018, and $7.66 million for 2017. The estimated aggregate annual amortization expense for each of the five years subsequent to December 31, 2019, is as follows: 2020, $11.48 million; 2021, $10.09 million; 2022, $8.57 million; 2023, $6.90 million; and 2024, $4.92 million.

During 2019, the Company recorded an increase of $13.16 million to goodwill and an increase of $8.02 million in intangible assets. This represents the acquisitions of SIL, Angel, and other immaterial acquisitions. During 2018, the Company recorded $163.41 million in net increases to goodwill and $20.18 million in intangible assets. This represents the acquisitions of Paragon, Middle Peninsula Insurance Agency, Inc., Michael R. Bare, LLC, and other immaterial acquisitions. The intangible assets acquired are finite-lived, consisting primarily of customer list purchases.

Changes in the carrying amount of goodwill related to each of the Company's segments are as follows (in thousands):

	Bank	Realty	Insurance	Consolidated Totals
Balance, December 31, 2017	$ 194,913	$ 26,180	$ 49,157	$ 270,250
Additions to goodwill	146,539	1,747	12,175	160,461
Other adjustments	3,186	(239)	—	2,947
Balance, December 31, 2018	$ 344,638	$ 27,688	$ 61,332	$ 433,658
Additions to goodwill	75	—	13,104	13,179
Other adjustments	—	(21)	—	(21)
Balance, December 31, 2019	$ 344,713	$ 27,667	$ 74,436	$ 446,816

NOTE 9: BANK-OWNED LIFE INSURANCE POLICIES

The total carrying amount of bank-owned life insurance as of December 31, 2019, was $243.06 million. The Company had $237.37 million of BOLI at December 31, 2018, and $195.78 million at December 31, 2017. The Company recognized BOLI income, included in other noninterest income, of $9.22 million, $6.84 million, and $6.26 million for the years ended December 31, 2019, 2018, and 2017, respectively. The Company has a related retirement plan, which provides retirement benefits to the executives covered under the plan. Although the retirement plan is technically unfunded, the life insurance policies are available to finance future benefits. Refer to Note 13 for additional discussions regarding retirement plans.

NOTE 10: DEPOSITS

A summary of time deposits by maturity at December 31, 2019, is shown in the following chart (dollars in thousands):

Maturity	Total
2020	$ 1,688,920
2021	552,903
2022	151,780
2023	54,566
2024 and thereafter	8,954
	$ 2,457,123

At year-end 2019, TowneBank had a total of $337.54 million in no-penalty time deposits as compared to $426.13 million at December 31, 2018. The aggregate amount of time deposits of $250,000 or more was $905.37 million and $742.85 million at December 31, 2019 and 2018, respectively.

Some of the Company's officers and directors, and the respective companies in which the officers and directors have a financial interest, have deposit relationships with the Company. Related party deposits amounted to approximately $79.59 million and $96.44 million at December 31, 2019 and 2018, respectively.

NOTE 11: BORROWINGS

TowneBank is a member of the FHLB and may borrow funds based on criteria established by the FHLB. The FHLB may call these borrowings if the adjusted collateral balance falls below the borrowing level. The borrowing arrangements available from the FHLB could be either short- or long-term, depending on our related cost and needs.

Advances from the FHLB for the years ended December 31 are summarized as follows (dollars in thousands):

	2019	2018
Balance outstanding at end of year	$ 471,687	$ 799,315
Average balance outstanding	$ 559,659	$ 849,988
Maximum outstanding at any month-end	$ 799,989	$ 873,923
Average interest rate during the year	1.74%	1.91%
Average interest rate at end of year	1.74%	2.11%

The scheduled maturity dates, call dates, and related fixed interest rates on advances from the FHLB at December 31, 2019, are summarized as follows (dollars in thousands):

Maturity Date	Interest Rate	Call/Reset Date	Outstanding Amount
11/15/2028	3.43%	—	$ 3,905
12/01/2028	2.83%	—	2,782
04/09/2020	1.75%	01/09/2020	115,000
11/12/2020	1.89%	02/12/2020	100,000
02/12/2020	1.69%	—	100,000
11/14/2022	1.58%	02/14/2020	100,000
01/07/2020	1.66%	—	50,000
			$ 471,687

Information concerning securities sold under agreements to repurchase and federal funds purchased is summarized as follows (dollars in thousands):

	2019	2018
Balance outstanding at end of year	$ 51,717	$ 46,439
Average balance outstanding	$ 48,801	$ 46,859
Maximum outstanding at any month-end	$ 55,681	$ 51,792
Average interest rate during the year	0.72%	0.43%
Average interest rate at end of year	0.62%	0.58%

REPOs totaled $51.72 million at December 31, 2019. All REPOs are overnight short-term investments and are not insured by the FDIC. Securities pledged as collateral under these REPO financing arrangements cannot be sold or repledged by the secured party and are therefore accounted for as a secured borrowing. Due to the overnight short-term nature of REPOs, potential risk due to a decline in the value of the pledged collateral is low. Collateral pledging requirements with REPOs are monitored daily. In addition, federal funds lines with other financial institutions of $155.00 million were available at December 31, 2019, for short-term funding needs. Federal funds purchased are overnight, unsecured borrowings.

At December 31, 2019 and 2018, the Company had an unused line of credit with the FHLB totaling $2.94 billion and $2.37 billion, respectively. The FHLB advances are secured by a blanket floating lien on certain 1-4 family residential, multifamily, HELOCs, second mortgages, and commercial mortgages with carrying values of $1.48 billion at December 31, 2019.

Further, the Company had loan participation lines and reverse repurchase agreements with various financial institutions available at December 31, 2019, which provide potential additional funding.

On July 17, 2017, the Company issued $250.0 million of fixed-to-floating rate subordinated notes due July 30, 2027 in a public offering. The Company received $247.07 million in net proceeds after deducting discounts and issuance costs. The subordinated notes accrue interest at a fixed rate of 4.50% for the first five years until July 30, 2022. From and including this date and for the remaining five years of the subordinated notes' term, interest will accrue at a floating rate of three-month LIBOR plus 2.550%. The Company may redeem the subordinated notes in whole or in part, on or after July 30, 2022. At December 31, 2019, the carrying value of the notes totaled $248.46 million, compared to $247.86 million at December 31, 2018.

NOTE 12: COMMITMENTS

TowneBank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit risk, which have not been recognized in the balance sheet. The contract amount of these instruments reflects the extent of the Company's involvement or "credit risk."

Our exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments. Unless noted otherwise, collateral or other security is required to support financial instruments with credit risk.

Our contractual amounts are as follows (in thousands):

December 31,	2019	2018
Financial instruments whose contract amounts represent credit risk:		
Commitments to extend credit	$ 3,094,615	$ 2,701,184
Standby letters of credit	140,630	119,380
	$ 3,235,245	$ 2,820,564

Commitments to extend credit are agreements to lend to a customer as long as there is not a violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the counter-party. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, income-producing commercial properties, and real estate.

Standby letters of credit are conditional commitments issued to guarantee performance of a customer to a third party. The letters of credit are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Collateral supporting those commitments is generally held, if deemed necessary. The Company provides an allowance for estimated losses from such provisions that management considered adequate at December 31, 2019. Management does not anticipate any material losses will arise from additional disbursements of the aforementioned lines or standby letters of credit.

Additionally, the Company had $1.57 billion in mortgage loans sold to investors with estimated recourse and warranty provisions totaling $54.85 million as of December 31, 2019.

NOTE 13: RETIREMENT PLANS

Defined Contribution Plans

The Company has a defined contribution 401(k) plan. All employees who are at least 18 years of age and have completed one month of service are eligible to participate. Under the plan, employees may contribute a percentage of their annual salary, subject to statutory limitations, and the Company will make a discretionary match of the employees' contributions up to 6% of their salary. The Company matched employee contributions up to 3.0% in 2019, 2018, and 2017. The Company may also make an additional discretionary contribution; there were no discretionary contributions for the years ended December 31, 2019, 2018, or 2017. The Company made matching contributions of $4.77 million, $4.58 million, and $4.35 million for the years ended December 31, 2019, 2018, and 2017, respectively.

The Company has a non-qualified deferred compensation plan that allows certain executives, senior officers, and other employees to defer payment of up to 100% of their base salary and annual bonus. The Company has the option to match an employee's combined non-qualified deferred compensation and 401(k) deferrals up to a maximum of 6% of his or her salary. The Company does not match contributions made by employees who are participants in the SERP, described below.

The funds for the non-qualified deferred compensation plan are held in a rabbi trust and invested in certificates of deposit, which are included in interest bearing deposits on the balance sheet. Changes in the obligation are recorded in compensation expense, which resulted in an increase in expenses of $0.46 million, $0.43 million, and $0.41 million for the years ended December 31, 2019, 2018, and 2017, respectively. The Company did not make matching contributions to the plan for the years ended December 31, 2019, 2018, or 2017.

Retirement Plans

The Company has a noncontributory, unfunded SERP for certain officers and key employees. The SERP is intended to provide retirement benefits and postretirement health benefits to individuals covered under the plan. The SERP agreements with the officers provide that upon attainment of retirement age, generally at age 65, the participating officer will be entitled to receive a retirement benefit equal to either (i) a designated percentage, ranging from 30% to 50% of their base salary depending on their level of seniority, with an annual 4% increase until retirement, or (ii) a fixed targeted benefit amount. The retirement benefit is payable over a 10-year, 15-year, or 20-year period, beginning upon the later of separation of service or the attainment of contractual retirement age. The SERP agreements provide for an annual vesting schedule until the participating officer reaches retirement age. In the case of a participating officer's voluntary termination of employment, disability, or termination for cause, the annual amount payable under the SERP is equal to the amount of the vested benefit earned as of the date of termination of employment. In the case of involuntary termination without cause or termination of employment for good reason by the participating officer, the participating officer becomes fully vested in the full retirement benefit. Upon termination of employment, payment of the retirement benefit generally does not begin until the participating officer reaches the designated retirement age set forth in the SERP agreement. In the event of death, the full amount of the retirement benefit is payable. We also provide postretirement benefits other than pensions for certain employees, which include health care, dental care, Medicare Part B reimbursement and life insurance benefits. Benefits under this plan are accounted for under the guidance of ASC 715 *Compensation - Retirement Benefits.*

The following table sets forth changes in benefit obligations and financial data relative to the retirement plans. The accrued liability is recorded on the Consolidated Balance Sheets as a component of other liabilities (in thousands):

	SERP		Other Postretirement Benefits	
December 31,	**2019**	**2018**	**2019**	**2018**
Change in benefit obligation				
Benefit obligation, beginning of year	$ 35,524	$ 35,105	$ 1,385	$ 1,345
Service cost	4,484	3,096	—	—
Interest cost	1,268	1,429	45	59
Net amortization	(57)	338	31	52
Benefits paid	(976)	(2,010)	(20)	(12)
Prior service cost	2,704	224	—	—
Net actuarial (gain) loss	2,757	(2,658)	23	(59)
Benefit obligation, end of year	$ 45,704	$ 35,524	$ 1,464	$ 1,385
Change in plan assets				
Fair value of plan assets, beginning of year	—	—	—	—
Employer contributions	976	2,010	20	12
Benefits paid	(976)	(2,010)	(20)	(12)
Fair value of plan assets, end of year	$ —	$ —	$ —	$ —
Funded status, end of year	$ (45,704)	$ (35,524)	$ (1,464)	$ (1,385)
Accumulated benefit obligation, end of year	$ 41,073	$ 32,720	$ 1,464	$ 230
Amounts recognized in other comprehensive income, pretax				
Prior service cost	$ 2,704	$ 224	$ —	$ —
Net actuarial (gain) loss	$ 2,757	$ (2,658)	$ 23	$ (59)

The components of the net periodic benefit cost are as follows (in thousands):

	SERP			Other Postretirement Benefits		
	2019	**2018**	**2017**	**2019**	**2018**	**2017**
Service cost	$ 4,484	$ 3,096	$ 3,336	$ —	$ —	$ 39
Interest cost	1,268	1,429	1,146	45	59	(41)
Prior service cost	613	305	288	—	—	—
Net amortization	(670)	32	148	31	52	8
Net periodic benefit cost	$ 5,695	$ 4,862	$ 4,918	$ 76	$ 111	$ 6

The service cost component of net periodic benefit costs is included in salaries and employee benefits. All other components of net periodic benefit costs are included in other expenses.

Amounts recognized as a component of accumulated other comprehensive income that have not yet been recognized as a component of net periodic benefit cost consist of the following (in thousands):

	SERP		Other Postretirement Benefits	
December 31,	2019	2018	2019	2018
Prior service cost	$ 4,120	$ 2,032	$ —	$ —
Net actuarial (gain) loss	1,045	(2,329)	154	132
Deferred tax benefit (expense)	(1,149)	65	(34)	(29)
Amounts included in accumulated other comprehensive income, net of tax	$ 4,016	$ (232)	$ 120	$ 103

Pre-tax amounts recorded in accumulated other comprehensive income as of December 31, 2019 that are expected to be recognized as a component of our net periodic benefit cost in 2020 consist of the following (in thousands):

	SERP	Other Postretirement Benefits
Net actuarial (gain) loss	$ 417	$ 12
Prior service cost	$ 613	$ —

The Company used certain weighted average assumptions to determine benefit obligations and net benefit costs, including discount rate and rate of increase in future compensation levels. The discount rate used to determine net periodic benefit cost and benefit obligation of the SERP was 3.14% in 2019, 4.45% in 2018, and 3.78% 2017. The rate of increase in future compensation levels used was 4.0% in 2019, 2018, and 2017. The discount rate used to determine net periodic benefit cost and benefit obligation of other postretirement benefits was 3.14% in 2019, 4.45% in 2018, and 3.78% 2017. When estimating the discount rate, we review yields available on high-quality, fixed-income debt instruments and use a yield curve model from which the discount rate is derived by applying the projected benefit payments under the plan to points on a published yield curve.

The following table sets forth expected future benefit payments, which include expected future service, for the periods indicated (in thousands):

Year	SERP	Other Postretirement Benefits
2020	$ 2,510	$ 55
2021	2,772	58
2022	2,900	62
2023	3,219	66
2024	3,144	68
2025-2029	20,906	403

In conjunction with its acquisition of Paragon, the Company assumed the liabilities related to Paragon's existing non-qualifying supplemental retirement contractual agreements with several key executives. The executives were fully vested in their benefits prior to the acquisition. The agreements typically require a fixed retirement benefit paid over a 20 year period following retirement.

The agreements are accounted for under ASC 710 *Compensation - General*. The following table sets forth changes in benefit obligations and financial data relative to the retirement plans. The accrued liability is recorded on the Consolidated Balance Sheets as a component of other liabilities (in thousands):

December 31,	2019	2018
Benefit obligation, beginning of year	$ 3,571	$ —
Accrued liability assumed at acquisition	—	3,317
Service cost	1,006	1,286
Interest cost	102	143
Benefits Paid	(690)	(1,175)
Benefit obligation, end of year	$ 3,989	$ 3,571

The discount rate used to determine net periodic benefit costs and benefit obligation of postretirement benefits was 3.14% in 2019, and 4.45% in 2018.

NOTE 14: SHARE-BASED COMPENSATION

The Company maintains a share-based compensation plan (“Plan”) that provides for the granting of incentive and non-statutory stock options and restricted common stock. The Plan is stockholder approved with an established termination date. In May 2017, stockholders approved the TowneBank 2017 Stock Incentive Plan ("2017 Plan"), which became effective May 24, 2017. This plan replaced the TowneBank 2008 Stock Incentive Plan ("2008 Plan") and no additional awards were made under the 2008 Plan after the effective date of the 2017 Plan. Except as specifically disclosed, the terms and limitations of the 2017 Plan and 2008 Plan are the same and shall be referred to collectively as the Plan.

The Plan is administered by the Compensation Committee of the Board of Directors (the “Compensation Committee”). The maximum aggregate number of shares that may be issued under the Plan may not exceed 2.50 million. The Company has a policy of using authorized and unissued common shares to satisfy share option exercises and vesting of restricted stock awards. At December 31, 2019, approximately 1.95 million common shares were available for issuance under the Plan.

Stock options: For stock options granted under the Plan, the stock option price cannot be less than the fair market value of the stock on the date granted. The Compensation Committee determines the exercise price for certain awards, and it can be based on future service. An option’s maximum contractual term is 10 years from the date of grant. Options and awards granted under the Plan are subject to vesting requirements ranging from two to 10 years.

The following tables summarize our stock option activity and related information:

For the Year Ended December 31,	2019		2018		2017	
	Number of Shares	Weighted-Average Exercise Price	Number of Shares	Weighted-Average Exercise Price	Number of Shares	Weighted-Average Exercise Price
Options outstanding, beginning balance	24,737	$ 14.14	46,391	$ 14.97	97,590	$ 16.24
Granted	—	—	—	—	—	—
Exercised	(13,540)	13.78	(20,624)	15.76	(50,066)	17.36
Expired	—	—	(1,030)	19.11	(824)	18.81
Forfeited	—	—	—	—	(309)	17.96
Options outstanding, ending balance	11,197	$ 14.59	24,737	$ 14.14	46,391	$ 14.97
Options exercisable at December 31,	6,047	$ 14.23	14,953	$ 13.74	30,171	$ 14.90

	Number of Shares	Weighted-Average Exercise Price
Unvested stock options, December 31, 2018	9,784	$ 14.77
Granted	—	—
Vested	(4,634)	14.51
Forfeited	—	—
Unvested stock options, December 31, 2019	5,150	$ 15.00

For the years ended December 31, 2019, 2018, and 2017, there were no stock options granted. In 2019, the total intrinsic value of options exercised was $0.18 million. In 2018, the total intrinsic value of options exercised was $0.29 million. In 2017, the total intrinsic value of options exercised was $0.73 million. Additional information pertaining to options outstanding at December 31, 2019, is as follows:

	Number of Shares	Weighted-Average Exercise Price	Aggregate Intrinsic Value	Weighted-Average Remaining Contractual Life
Options outstanding	11,197	$ 14.59	$ 148,171	.99
Options vested or expected to vest	11,122	$ 14.58	$ 147,216	.99
Options exercisable	6,047	$ 14.23	$ 82,148	.76

The grant-date fair value of each option grant is estimated using the Black-Scholes option pricing model. Use of a valuation model requires management to make certain assumptions with respect to selected model inputs. Expected volatility was calculated based on the historical volatility of the Company's stock over the most recent period of time equal to the expected term of the option. The average expected life was based on the contractual term of the option and expected employee exercise and post-vesting employment termination behavior based on historical patterns. The risk-free interest rate is based on the U.S. Treasury zero-coupon issues with a remaining term equal to the expected life assumed at the date of grant. Forfeitures are estimated based on historical voluntary termination behavior.

For the years ended December 31, 2019, 2018, and 2017, the tax benefit on cash paid for stock options exercised was $0.04 million, $0.06 million, and $0.25 million, respectively. Compensation expense related to stock options for the years ended December 31, 2019, 2018, and 2017, was $0.02 million, $0.02 million, and $0.06 million, respectively. As of December 31, 2019, there was $0.02 million of total unrecognized compensation cost related to unvested stock option awards; that cost is expected to be recognized over a period of 0.75 years.

Restricted stock awards ("RSAs") and restricted stock units ("RSUs"): Under the Plan, recipients of RSAs have full voting rights and are generally entitled to dividends on the common stock. RSAs issued under the 2008 Plan are also entitled to dividends as they are paid. Under the 2017 Plan, dividends on RSAs are accumulated and retained for the grantee by the Company until the stock vests. The accumulated cash and stock dividends on restricted stock awards are distributed with the award at vesting. Recipients of RSUs are entitled to receive shares of common stock after the applicable restrictions lapse. Additionally, recipients of RSUs are generally entitled to receive cash payments or additional shares of common stock equivalent to any dividends paid on the underlying common stock during the period the RSUs are outstanding, but are not entitled to voting rights. RSAs granted under the Plan are generally subject to vesting requirements ranging from two to 10 years. The shares are subject to forfeiture if vesting and other contractual provision requirements are not met. Generally, the value of RSAs and RSUs will equal the fair value of our common stock on the date of grant and the expense is recognized over the vesting period.

The following chart shows a summary of activity for RSAs and RSUs, assuming the weighted-average price being the weighted-average fair value at the date of grant for the year ended December 31, 2019:

	Restricted Stock Awards		Restricted Stock Units	
	Number of Shares	Weighted-Average Price	Number of Shares	Weighted-Average Price
Unvested, beginning balance	528,786	$ 26.46	—	$ —
Granted	155,654	26.85	84,844	27.54
Vested	(166,231)	24.64	—	—
Forfeited	(7,035)	28.07	—	—
Unvested, ending balance	511,174	$ 27.15	84,844	$ 27.54

Compensation expense related to awards for the years ended December 31, 2019, 2018, and 2017, was $5.77 million, $4.05 million, and $2.53 million, respectively. The total fair value of RSAs vested during 2019, 2018, and 2017 was $4.10 million, $2.61 million, and $2.32 million, respectively. No RSUs vested during 2019. No RSUs were issued prior to 2018. As of December 31, 2019, there was $9.20 million of total unrecognized compensation cost related to unvested RSAs; that cost is expected to be recognized over a period of 2.17 years. As of December 31, 2019, there was $2.15 million of total unrecognized compensation cost related to unvested RSUs; that cost is expected to be recognized over a period of 4.23 years.

The Company has a directors' deferred compensation plan whereby the directors may elect to defer up to 100% of their directors' fees. All deferred compensation is invested in the Company's common stock and is held in a rabbi trust. The stock is held in the nominee name of the trustee, and the principal and earnings of the trust are held separate and apart from other funds of the Company, and are used exclusively for the uses and purposes of the deferred compensation agreement. The accounts of the trust have been consolidated in the financial statements of the Company with common stock reported separately in a manner similar to treasury stock (that is, changes in fair value are not recognized) and a corresponding deferred compensation obligation reflected in additional paid-in capital of $15.56 million and $13.96 million at December 31, 2019 and 2018, respectively.

NOTE 15: STOCK PURCHASE AND DIVIDEND REINVESTMENT PLAN, AND DIVIDEND RESTRICTIONS

The Company has a Member Stock Purchase and Dividend Reinvestment Plan to raise additional capital by providing a convenient and cost-effective way for shareholders, customers, and employees to purchase shares of TowneBank common stock. In connection with the member stock purchase component of the plan for the year ended December 31, 2019, the Company entered the open market and acquired 98,279 shares at an average price of $27.30 per share. In connection with the dividend reinvestment component of the plan for the year ended December 31, 2019, the Company entered the open market and acquired 208,691 shares at an average price of $26.62 per share.

In connection with the member stock purchase component of the plan for the year ended December 31, 2018, the Company entered the open market and acquired 84,056 shares at an average price of $29.95 per share. In connection with the dividend reinvestment component of the plan for the year ended December 31, 2018, the Company entered the open market and acquired 170,268 shares at an average price of $31.19 per share.

TowneBank, as a Virginia banking corporation, may pay cash dividends only out of retained earnings. In February 2019, the Company declared a quarterly cash dividend of $0.16 per common share. In May, August, and November 2019, the Company declared quarterly cash dividends of $0.18 per common share. In February 2018, the Company declared a quarterly cash dividend of $0.14 per common share. In May, August, and November 2018, the Company declared quarterly cash dividends of $0.16 per common share. In February 2017, the Company declared a quarterly cash dividend of $0.13 per common share. In May, August, and November 2017, the Company declared quarterly cash dividends of $0.14 per common share. The quarterly dividends were paid on January 12, 2017; April 12, 2017; July 12, 2017; October 12, 2017; January 12, 2018; April 10, 2018; July 10, 2018; October 10 2018; January 11, 2019; April 10, 2019; July 10, 2019; October 10 2019; and January 10, 2020.

Declaration of future cash dividends will depend on our earnings, our capital position, and other factors. All dividends paid are limited by the requirement to meet capital guidelines issued by regulatory authorities, and future declarations are subject to financial performance and regulatory requirements.

NOTE 16: REVENUE

ASC 606 - *Revenue from Contracts with Customers,* requires the disaggregation of revenue from contracts with customers into categories that show how economic factors affect the nature, timing, and uncertainty of revenue and cash flows. Suggested categories of disaggregation included but were not limited to: (1) type of good or service, (2) geographical region, (3) market or type of customer, (4) type of contract, (5) contract duration, (6) timing of the transfer of goods or services, and (7) sales channels. The Company disaggregates revenue from contracts by major product line, a type of good or service.

The following table presents certain selected financial information for the periods indicated (dollars in thousands):

For the year ended December 31,	2019	2018
Revenue from Contracts with Customers:		
(1) Investment management income		
Investment commissions, net	$ 6,807	$ 6,354
Total	$ 6,807	$ 6,354
(2) Insurance income		
Property and casualty insurance income, net	$ 46,938	$ 38,327
Benefit insurance income, net	11,095	10,387
Travel insurance commissions, net	4,085	5,123
Total	$ 62,118	$ 53,837
(3) Real estate and property management income		
Real estate sales commissions, net	$ 9,865	$ 9,458
Real estate property management income, net	24,427	22,405
Total	$ 34,292	$ 31,863

(1) Investment management services are provided by TIG and TWM, which are included in the Banking segment of TowneBank. TIG and TWM market services to our customers on behalf of RJFS, a broker-dealer and investment advisory firm registered with the SEC and a member of the Financial Industry Regulatory Authority. RJFS provides our customers brokerage and investment advisory services for the purchase and sale of non-deposit investment and/or insurance products.

TIG and TWM earn revenue in the form of commissions and fees. TIG and TWM's performance obligation is related to the referral of business to a third party asset manager. Performance obligations are satisfied when a new customer enters into a contract with the third party asset manager and when the manager collects a fee from the customer. Commissions are typically collected shortly after fees are collected by the third party asset manager and there is no material over time recognition of revenue. In carrying out this performance obligation, TowneBank acts in the capacity of an agent.

(2) Insurance revenue is included in the Insurance segment. This segment earns revenue in the form of commissions by binding insured parties' insurance policies with external insurance companies. Insurance revenue is earned in the form of commissions received for selling insurance policies as an independent agent of external insurance companies who underwrite the insurance policies. The external insurance companies retain the risks associated with the insurance policies. The Insurance segment's performance obligation is related to the referral of business to third party insurance companies. Performance obligations are satisfied when a new customer enters into a contract with the third party insurance company. Commissions are typically collected shortly thereafter and there is no material over time recognition of revenue. Contingent income is estimated and recorded at the time of the sale of the insurance policy to the extent that it is probable that there will not be a material amount of the income reversed. In carrying out this performance obligation, TowneBank acts in the capacity of an agent.

(3) Real estate and property management revenue is mainly in the form of commissions, fee, and title income. The revenue is earned on both residential and commercial properties. Real estate and property management revenues fall within the Realty segment. Towne Realty, LLC provides real estate services, and residential and title insurance. Revenue is recognized as commissions and fee income are received. Performance obligations are satisfied with the receipt of commissions and fee income and there is no material over time recognition of revenue.

TowneBank's performance obligation related to the property management business is to market the property, take reservations (including the collection of rent) and provide facility management services. The performance obligation to take reservations is satisfied when a customer makes a booking. Facility management services obligations are ongoing until a customer vacates a property. Fees are typically collected half upon booking and half upon a customer vacating a property. Materially all of the value of the performance obligation is related to the booking of the reservation, therefore, the Company recognizes the commission at the time the reservation is confirmed via the receipt of deposit. In carrying out these performance obligations, TowneBank acts in the capacity of an agent.

Remaining performance obligations related to ASC 606 application to the above revenue streams represent performance obligations with an original contract term greater than one year, which are fully or partially unsatisfied at the end of the period. The Company applies the practical expedient in ASC paragraph 606-10-50-14(a) and does not disclose information about remaining performance obligations that are part of a contract with an original expected duration of one year or less. The timing of revenue billings and cash collections may result in contract assets (the Company performing on its obligations prior to receiving payment unrelated to the passage of time) and contract liabilities (the Company receiving payment from a customer prior to performing on its obligation to that customer) on the Consolidated Balance Sheets.

The Company had no material contract assets or contract liabilities recorded on the Consolidated Balance Sheets as of December 31, 2019.

This disclosure includes only revenue from contracts with third party customers. See Note 27 for additional information regarding other revenue streams, primarily from revenue between the Company's consolidated subsidiaries and lines of business, in addition to those included in the table above.

NOTE 17: OTHER EXPENSES

The following chart shows a summary of other expenses (in thousands):

Year Ended December 31,	2019	2018	2017
Acquisition-related expenses	$ 657	$ 8,428	$ 2,268
Bank franchise tax/SCC fees	7,251	5,647	5,303
Charitable contributions	9,339	5,104	5,550
Directors' expense	2,136	1,991	1,734
FDIC and other insurance	3,119	5,047	4,249
Foreclosed property expenses	985	820	782
Other	15,807	15,275	13,336
Stationery and office supplies	2,962	3,217	2,730
Telephone and postage	6,426	6,788	6,907
Travel/Meals/Entertainment	3,834	3,636	2,820
	$ 52,516	$ 55,953	$ 45,679

NOTE 18: REGULATORY CAPITAL REQUIREMENTS

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

In July 2013, the FDIC and other federal bank regulatory agencies approved final rules known as the "Basel III Capital Rules," which substantially revised the risk-based capital and leverage capital requirements applicable to bank holding companies and depository institutions, including the Company. The Basel III Capital Rules, which became fully phased in on January 1, 2019, require banking organizations to maintain (i) a minimum ratio of CET1 to risk-weighted assets of at least 4.5%, plus a 2.5% "capital conservation buffer" (which is added to the 4.5% CET1 ratio, effectively resulting in a minimum ratio of CET1 to risk-weighted assets of at least 7.0%); (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0%, plus the capital conservation buffer (which is added to the 6.0% Tier 1 capital ratio, effectively resulting in a minimum Tier 1 capital ratio of 8.5%); (iii) a minimum ratio of total capital (that is, Tier 1 plus Tier 2 capital) to risk-weighted assets of at least 8.0%, plus the capital conservation buffer (which is added to the 8.0% total capital ratio, effectively resulting in a minimum total capital ratio of 10.5%); and (iv) a minimum leverage ratio of 4.0%, calculated as the ratio of Tier 1 capital to adjusted average quarterly assets.

In addition, the Federal Deposit Insurance Act, as amended, requires among other things, the federal bank regulatory agencies to take "prompt corrective action" against depository institutions that do not meet minimum capital requirements. The Federal Deposit Insurance Act includes the following five capital tiers: "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized."

In order to be adequately capitalized for purposes of the prompt corrective action rules, a banking organization is required to have at least an 8% total risk-based capital ratio, a 6% Tier 1 risk-based capital ratio, a 4.5% CET1 risk-based capital ratio, and a 4% Tier 1 leverage ratio. To be well-capitalized, a banking organization is required to have at least a 10% total risk-based capital ratio, an 8% Tier 1 risk-based capital ratio, a 6.5% CET1 risk-based capital ratio, and a 5% Tier 1 leverage ratio. An institution may be downgraded to, or deemed to be in, a capital category that is lower than indicated by its capital ratios if it is determined to be in an unsafe or unsound condition or if it receives an unsatisfactory examination rating with respect to certain matters. A bank's capital category is determined solely for the purpose of applying prompt corrective action regulations, and the capital category may not constitute an accurate representation of the bank's overall financial condition or prospects for other purposes.

A summary of our required and actual capital components follow (dollars in thousands):

As of December 31, 2019	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Action Provisions	
	Amount	Ratio %	Amount	Ratio %	Amount	Ratio %
Common equity Tier 1						
(to risk-weighted assets)	$ 1,135,886	11.46%	$ 446,220	4.50%	$ 694,120	6.50%
Tier 1 capital						
(to risk-weighted assets)	$ 1,139,107	11.49%	$ 594,960	6.00%	$ 842,860	8.00%
Total risk-based capital						
(to risk-weighted assets)	$ 1,445,799	14.58%	$ 793,280	8.00%	$ 1,041,180	10.00%
Tier 1 leverage ratios						
(to average assets)	$ 1,139,107	9.95%	$ 458,090	4.00%	$ 572,613	5.00%

As of December 31, 2018	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Action Provisions	
	Amount	Ratio %	Amount	Ratio %	Amount	Ratio %
Common equity Tier 1						
(to risk-weighted assets)	$ 1,050,018	11.51%	$ 410,632	4.50%	$ 638,762	7.00%
Tier 1 capital						
(to risk-weighted assets)	$ 1,053,030	11.54%	$ 547,510	6.00%	$ 775,639	8.50%
Total risk-based capital						
(to risk-weighted assets)	$ 1,352,985	14.83%	$ 730,013	8.00%	$ 958,142	10.50%
Tier 1 leverage ratios						
(to average assets)	$ 1,053,030	9.87%	$ 426,611	4.00%	$ 533,263	5.00%

NOTE 19: FAIR VALUE DISCLOSURES

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. A three-level valuation hierarchy was established for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

Level 1 Valuation is based on quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 Valuation is based on observable inputs, other than Level 1 prices, that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Valuation is based on unobservable inputs that are supported by little or no market activity and which are significant to the fair value of the assets or liabilities.

The following is a description of the valuation methodologies used for instruments measured at fair value on a recurring basis.

Securities available for sale: Fair values are based on published market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Loans held for sale - mandatory delivery: Effective July 1, 2019, TowneBank elected to carry mortgages it intends to sell in the mandatory delivery program at fair value. Intent is established for these residential real estate mortgage loans when TowneBank enters into a loan commitment or interest rate lock with the customer. As of this effective date, any loan closed and held for sale within the mandatory program will be carried at fair value. For additional information about loans held for sale refer to Note 20.

Derivative Financial Instruments: Interest rate lock commitments, related to the origination of mortgage loans held for sale, are recorded at estimated fair value based on the value of the underlying loan, which in turn is based on quoted prices for similar loans in the secondary market. However, this value is adjusted by a factor which considers the likelihood that the loan in a lock position will ultimately close. This factor, the fall-out rate, is derived from the Company's internal data and is adjusted using significant management judgment. The fall-out rate is largely dependent on the processing stage that a loan is currently in and the change in prevailing interest rates from the time of the rate lock. As such, interest rate lock commitments are classified as recurring Level 3. For the years ended December 31, 2019 and 2018, the Company used weighted average fall-out rates of 13.16%, and 14.90%, respectively.

To mitigate the effect of the interest rate risk inherent in providing rate lock commitments to borrowers, the Company enters into a TBA mortgage-backed security under mandatory delivery. The Company has not formally designated these derivatives as a qualifying hedge relationship, accordingly, changes to fair value are recorded to earnings each period. These valuations fall into a Level 2 category.

Assets and liabilities measured at fair value on a recurring basis are summarized below (in thousands):

	December 31, 2019			
	Level 1	Level 2	Level 3	Total
U.S. agency securities	$ —	$ 129,038	$ —	$ 129,038
U.S. Treasury notes	$ —	$ 1,000	$ —	$ 1,000
Municipal securities	$ —	$ 223,106	$ —	$ 223,106
Mortgage-backed securities issued by GSEs	$ —	$ 1,034,797	$ —	$ 1,034,797
Trust preferred and other corporate securities	$ —	$ 53,367	$ —	$ 53,367
Other equity securities	$ —	$ 6,462	$ —	$ 6,462
Loans held for sale - mandatory delivery	$ —	$ 340,915	$ —	$ 340,915
Derivative assets	$ —	$ 439	$ 1,525	$ 1,964
Derivative liabilities	$ —	$ 940	$ —	$ 940

	December 31, 2018			
	Level 1	Level 2	Level 3	Total
U.S. agency securities	$ —	$ 358,542	$ —	$ 358,542
U.S. Treasury notes	$ —	$ 1,246	$ —	$ 1,246
Municipal securities	$ —	$ 87,308	$ —	$ 87,308
Mortgage-backed securities issued by GSE	$ —	$ 617,251	$ —	$ 617,251
Trust preferred and other corporate securities	$ —	$ 30,992	$ —	$ 30,992
Other equity securities	$ —	$ 4,797	$ —	$ 4,797
Loans held for sale - mandatory delivery	$ —	$ —	$ —	$ —
Derivative assets	$ —	$ 1,996	$ 1,200	$ 3,196
Derivative liabilities	$ —	$ 1,507	$ —	$ 1,507

The Company may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with GAAP. These adjustments to fair value usually result from application of lower-of-cost-or-market accounting or write-downs of individual assets. For assets measured at fair value on a nonrecurring basis that were still held in the balance sheet at year-end, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related assets (in thousands):

December 31, 2019	Level 1	Level 2	Level 3	Total
Impaired loans	$ —	$ —	$ 3,204	$ 3,204
Other real estate owned and other nonperforming assets	$ —	$ —	$ 15,360	$ 15,360

December 31, 2018	Level 1	Level 2	Level 3	Total
Impaired loans	$ —	$ —	$ 5,896	$ 5,896
Other real estate owned and other nonperforming assets	$ —	$ —	$ 19,416	$ 19,416

The following is a description of valuation methodologies used for assets measured on a nonrecurring basis.

Loans: Impaired loans for which repayment of the loan is expected to be provided solely by the value of the underlying collateral are considered collateral dependent and are valued based on the fair value of such collateral. Collateral values are estimated using inputs based on observable market data, where available, or inputs based on customized discounting criteria. In cases where such inputs were unobservable, specifically discounts applied to appraisal values to adjust such values to current market conditions or to reflect net realizable value, the impaired loan balance is reflected within Level 3 of the hierarchy. These discounts ranged from 5.84% to 100%, with a weighted average of 17.67%.

Loans held for sale: Loans closed and held for sale within the mandatory program are carried at fair value. Loans held for sale within the best efforts program are carried at the lower of cost or fair value. Fair values of loans held for sale are based on commitments on hand from investors or, if commitments have not yet been obtained, prevailing market rates. For additional information about loans held for sale refer to Note 20.

Other real estate owned and other nonperforming assets: The fair value of foreclosed property is measured at fair value on a nonrecurring basis (upon initial recognition or subsequent impairment) and is classified within Level 3 of the valuation hierarchy. When transferred from the loan portfolio, other real estate is adjusted to fair value less estimated selling costs and is subsequently carried at the lower of carrying value or fair value less estimated selling costs. The fair value is generally determined using an external appraisal process and is discounted based on internal criteria when deemed necessary.

The following methods and assumptions were used in estimating fair value for the remaining classes of our financial instruments.

Cash and due from banks, interest-bearing deposits in financial institutions, and federal funds sold: The carrying amount approximates fair value.

Securities held to maturity: Fair values are based on published market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Loans: For loan receivables with short-term and/or variable characteristics, the total receivable outstanding approximates fair value. The fair value of other loans is estimated by discounting the future cash flows using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality.

Interest receivable and interest payable: The carrying amount approximates fair value.

Deposits: The fair value of noninterest-bearing deposits and deposits with no defined maturity is estimated by discounting anticipated future cash flows using current borrowing rates. The fair value of certificates of deposit is estimated by discounting the future cash flows using the current rates at which similar deposits would be made.

Advances from the FHLB: The fair value of advances from the FHLB is determined using the discounted cash flow method with the discount rate being equal to the rate currently offered on similar products.

Repurchase agreements: The carrying amount approximates fair value.

Commitments to extend and standby letters of credit: These financial instruments are generally not sold or traded. The estimated fair values of off-balance-sheet credit commitments, including standby letters of credit and guarantees written, are not readily available due to the lack of cost-effective and reliable measurement methods for these instruments.

The estimated fair values of our financial instruments required to be disclosed under ASC 825, *Financial Instruments*, and the level within the fair value hierarchy at which such assets and liabilities are measured on a recurring basis, are as follows (in thousands):

December 31, 2019	Carrying Value	Estimated Fair Value	Level 1	Level 2	Level 3
Cash and due from banks	$ 97,593	$ 97,593	$ 97,593	$ —	$ —
Interest-bearing deposits at FRB Richmond	$ 322,505	$ 322,505	$ 322,505	$ —	$ —
Interest-bearing deposits in financial institutions	$ 22,518	$ 22,518	$ 22,518	$ —	$ —
Securities available for sale	$ 1,441,308	$ 1,441,308	$ —	$ 1,441,308	$ —
Securities held to maturity	$ 43,688	$ 46,177	$ —	$ 46,177	$ —
Other equity securities	$ 6,462	$ 6,462	$ —	$ 6,462	$ —
Mortgage loans held for sale	$ 419,233	$ 419,420	$ —	$ 419,420	$ —
Loans, net	$ 8,361,054	$ 8,365,959	$ —	$ —	$ 8,365,959
Interest receivable	$ 33,126	$ 33,126	$ —	$ 33,126	$ —
Non-maturity deposits	$ 6,813,794	$ 6,732,178	$ —	$ 6,732,178	$ —
Time deposits	$ 2,457,123	$ 2,468,979	$ —	$ 2,468,979	$ —
Advances from the FHLB	$ 471,687	$ 472,029	$ —	$ 472,029	$ —
Subordinated debentures	$ 248,458	$ 254,993	$ —	$ 254,993	$ —
Repurchase agreements and other borrowings	$ 52,391	$ 49,958	$ —	$ 49,958	$ —
Interest payable	$ 13,563	$ 13,563	$ —	$ 13,563	$ —

December 31, 2018	Carrying Value	Estimated Fair Value	Level 1	Level 2	Level 3
Cash and due from banks	$ 94,604	$ 94,604	$ 94,604	$ —	$ —
Interest-bearing deposits at FRB Richmond	$ 570,425	$ 570,425	$ 570,425	$ —	$ —
Interest-bearing deposits in financial institutions	$ 21,667	$ 21,667	$ 21,667	$ —	$ —
Securities available for sale	$ 1,095,339	$ 1,095,339	$ —	$ 1,095,339	$ —
Securities held to maturity	$ 50,598	$ 51,268	$ —	$ 51,268	$ —
Other equity securities	$ 4,797	$ 4,797	$ —	$ 4,797	$ —
Mortgage loans held for sale	$ 220,986	$ 221,086	$ —	$ 221,086	$ —
Loans, net	$ 7,966,139	$ 7,894,198	$ —	$ —	$ 7,894,198
Interest receivable	$ 33,080	$ 33,080	$ —	$ 33,080	$ —
Non-maturity deposits	$ 6,020,094	$ 5,609,446	$ —	$ 5,609,446	$ —
Time deposits	$ 2,350,328	$ 2,339,663	$ —	$ 2,339,663	$ —
Advances from the FHLB	$ 799,315	$ 795,871	$ —	$ 795,871	$ —
Subordinated debentures	$ 247,861	$ 248,750	$ —	$ 248,750	$ —
Repurchase agreements and other borrowings	$ 47,156	$ 46,449	$ —	$ 46,449	$ —
Interest payable	$ 9,638	$ 9,638	$ —	$ 9,638	$ —

Fair Value Option

Effective July 1, 2019, TowneBank elected the fair value option for loans held for sale within the mandatory delivery program. This election allows for a more effective offset of the changes in fair values of the loans and the derivative instruments used to economically hedge them without the burden of complying with the requirements for hedge accounting. TowneBank has not elected the fair value option for other loans held for sale primarily because they are not actively hedged. Fair values of loans held for sale are recorded in mortgage loans held for sale in the Consolidated Balance Sheets.

The following table summarizes the difference between the aggregate fair value and the aggregate unpaid principal balance for mortgage loans held for sale measured at fair value at December 31, 2019 (in thousands):

December 31, 2019	Aggregate Fair Value		Aggregate Unpaid Principal		Aggregate Fair Value less Aggregate Unpaid Principal	
Mortgage loans held for sale, at fair value	$	340,915	$	339,831	$	1,084

Interest income on mortgage loans held for sale is recognized based on contractual rates and is reflected in interest income on mortgage loans held for sale in the Consolidated Statements of Income. The following table details net gains and losses resulting from changes in fair value of these loans, which were recorded in residential mortgage banking income, net in the Consolidated Statements of Income for the periods presented.

Net Gains (Losses) Resulting from Changes in Fair Value

(in thousands)	Twelve Months Ended December 31, 2019	
Mortgage loans held for sale, at fair value	$	1,084

NOTE 20. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company enters into interest rate lock commitments with its mortgage customers. The Company is also a party to sales of TBA MBSs. When the interest rate is locked with the borrower, the rate lock commitment and mortgage-backed security position are undesignated derivatives and marked to fair value through earnings. The fair value of the rate lock derivative is based on quoted prices for similar loans in the secondary market adjusted by a factor which considers the likelihood that the loan in a lock position will ultimately close. Both the rate lock commitment and the corresponding TBA MBS are considered derivatives, but are not accounted for using hedge accounting. As such, changes in the estimated fair value of the derivatives are recorded in current earnings and included in net residential mortgage banking income in the Consolidated Statements of Income.

We sell mortgage loans under both “mandatory” and "best efforts" delivery programs. Under the mandatory delivery system, loans with interest rate locks with respective borrowers are paired with the sales of TBA MBSs bearing similar attributes. We commit to deliver loans to an investor at an agreed-upon price upon the closing of such loans. This differs from “best efforts” delivery transactions, which set the sale price with the investor on a loan-by-loan basis at the time each loan is locked with the respective borrower.

The following table reflects the amount and market value of mortgage banking derivatives included in the Consolidated Balance Sheets as of the period end (in thousands):

	December 31, 2019				December 31, 2018			
	Notional Amount		Fair Value		Notional Amount		Fair Value	
Interest rate contracts included in other assets	$	367,073	$	1,964	$	397,240	$	3,196
Interest rate contracts included in other liabilities	$	315,912	$	940	$	181,262	$	1,507

Gains and losses from mortgage banking derivatives are included in residential mortgage banking income, net on the Consolidated Statements of Income. For the years ended December 31, 2019, and December 31, 2018, the Company recognized gains of $2.56 million and $1.15 million, respectively.

NOTE 21: VARIABLE INTEREST ENTITIES

In the normal course of business, the Company is involved with various entities that are considered to be Variable Interest Entities. A VIE is an entity that has either a total equity investment that is insufficient to permit the entity to finance its activities without additional subordinated financial support, or whose equity investors lack the characteristics of a controlling financial interest. In accordance with existing accounting guidance, we are required to consolidate any VIE of which we are determined to be the primary beneficiary. The primary beneficiary is the entity that has (i) the power to direct the activities of a VIE that most significantly impact the entity's economic performance; and (ii) the obligation to absorb losses of the entity that could potentially be significant to the VIE, or the right to receive benefits from the entity that could potentially be significant to the VIE. We review all significant interests in the VIEs we are involved with, including the amounts and types of financial and other support, including equity investments, debt financing, and guarantees. We also consider the activities of the VIEs that most significantly impact the VIEs' economic performance and whether we have control over those activities. We assess whether or not we are the primary beneficiary of a VIE on an ongoing basis. To provide the necessary disclosures, we aggregate similar VIEs based on the nature and purpose of the entities.

Low Income Housing Tax Credit Partnerships

As part of its community reinvestment initiatives, the Company invests within its footprint in multifamily affordable housing developments as a limited partner. The Company receives tax credits for its partnership investments. The Company has determined that these partnerships are VIEs when it does not own 100% of the entity, because the holders of the equity investment at risk do not have the power through voting rights or similar rights to direct the activities of the entity that most significantly impact the entity's economic performance. Accordingly, the Company's limited partner interests are variable interests that the Company evaluates for purposes of determining whether the Company is the primary beneficiary.

For each of the partnerships, the Company acts strictly in a limited partnership capacity. The Company has determined that it is not the primary beneficiary of these partnerships because it does not have the power to direct the activities of the entity that most significantly impact the entity's economic performance. The Company accounts for its limited partner interests in accordance with the accounting guidance for investments in affordable housing projects. Partnership assets of $229.01 million and $151.84 million were not included in the Consolidated Balance Sheets at December 31, 2019 and 2018, respectively. These limited partner interests had carrying values of $59.38 million and $33.03 million at December 31, 2019 and 2018, respectively, and are recorded in other assets on the Company's Consolidated Balance Sheets. The Company's maximum exposure to loss for these limited partner investments totaled $62.24 million and $42.34 million at December 31, 2019 and 2018, respectively. As of December 31, 2019, the Company has $62.75 million in funding commitments that are dependent on certain contractual milestones and $27.65 million in loans, unfunded short-term construction loans, or letters of credit commitments. For the year ended December 31, 2019, a tax benefit totaling $1.55 million, net of amortization of $7.10 million, was recognized as a component of income tax expense.

NOTE 22: INCOME TAXES

Current income tax expense represents the amounts expected to be reported on the Company's income tax returns, and deferred tax expense or benefit represents the change in net deferred tax assets and liabilities. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax basis of assets and liabilities as measured by the enacted tax rates that will be in effect when these differences reverse. Valuation allowances are recorded as appropriate to reduce deferred tax assets to the amount considered likely to be realized.

On December 22, 2017, the President of the United States signed into law the Tax Act. The legislation made key changes to U.S. tax law, including the reduction of the U.S. federal corporate tax rate from 35% to 21%, effective January 1, 2018.

The Company uses the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to reverse. As a result of the reduction in the U.S. corporate income tax rate from 35% to 21% under the Tax Act, the Company revalued its ending net deferred tax assets at December 31, 2017, and recognized a provisional $10.11 million tax expense in the Company's consolidated statement of income for the year ended December 31, 2017. An additional expense of $0.70 million was recognized in 2018 due to the finalization of the provisional component of the Tax Act.

The provision for income taxes charged to operations is listed in the following chart (in thousands):

For the Year Ended December 31,	**2019**	**2018**	**2017**
Current income tax expense			
Federal	$ (34,927)	$ (30,867)	$ (51,925)
State	(2,452)	(2,060)	(2,318)
Total current tax expense	(37,379)	(32,927)	(54,243)
Deferred income tax (expense) benefit			
Federal	4,707	(1,013)	9,210
State	76	409	332
Revaluation of deferred taxes	—	(696)	(10,112)
Total deferred income tax expense (benefit)	4,783	(1,300)	(570)
Income tax expense	$ (32,596)	$ (34,227)	$ (54,813)

Differences between income tax expense calculated at the statutory rate and shown on the Consolidated Statements of Income are summarized as follows (dollars in thousands):

	2019		**2018**		**2017**	
For the Year Ended December 31,	**$**	**Rate**	**$**	**Rate**	**$**	**Rate**
Federal income tax expense at statutory rate	$ (35,990)	(21.00)%	$ (35,284)	(21.00)%	$ (49,867)	(35.00)%
Revaluation of deferred taxes	—	— %	(696)	(0.41)%	(10,112)	(7.10)%
State income tax expense, net of federal benefit	(1,800)	(1.05)%	(1,667)	(0.99)%	(1,507)	(1.06)%
Tax advantaged income	4,209	2.46 %	3,469	2.06 %	5,062	3.55 %
Low income housing tax credit, net of amortization	1,819	1.06 %	874	0.52 %	1,750	1.23 %
Other	(834)	(0.49)%	(923)	(0.55)%	(139)	0.16 %
Income tax expense	$ (32,596)	(19.02)%	$ (34,227)	(20.37)%	$ (54,813)	(38.22)%

Significant components of deferred tax assets and deferred tax liabilities follow (in thousands):

Year Ended December 31,	**2019**	**2018**
Deferred tax assets:		
Allowance for loan losses	$ 12,837	$ 11,581
Stock-based compensation	680	491
Accrued expenses	1,352	1,759
Retirement plan	11,975	9,849
Unrealized loss on securities available for sale	—	2,591
Deferred compensation	7,040	4,866
Operating lease liabilities	11,077	—
Assets acquired in acquisitions	6,118	8,511
Other	3,979	2,902
Total deferred tax assets	55,058	42,550
Deferred tax liabilities:		
Depreciation	13,277	12,647
Noncompete and intangibles	6,044	7,761
Basis differences due to tax credits and partnerships	(761)	(116)
Unrealized gain on securities available for sale	4,293	—
Operating lease right-of-use assets	10,475	—
Other	1,627	1,197
Total deferred tax liabilities	34,955	21,489
Net deferred tax assets	$ 20,103	$ 21,061

As of December 31, 2019 and December 31, 2018, the Company did not have any unrecognized tax benefits. The Company does not expect the total amount of unrecognized tax benefits to significantly increase or decrease in the next 12 months. The Company recognizes interest and penalties related to unrecognized tax benefits as “Interest Expense” and “Other Expense,” respectively, and not as part of the tax provision. The Company is no longer subject to examination for federal and state purposes for tax years prior to 2016.

NOTE 23: ACCUMULATED OTHER COMPREHENSIVE INCOME

The following table summarizes the components of accumulated other comprehensive income (loss) at December 31, 2019, 2018, and 2017, and changes during the years then ended. The amounts reclassified from accumulated other comprehensive income for the securities available for sale are included in gain on investment securities, net on the Consolidated Statements of Income, while the amounts reclassified from accumulated other comprehensive income for the defined benefit retirement plan are a component of salaries and employee benefits expense on the Consolidated Statements of Income.

(in thousands)	Unrealized Gains (Losses) on Securities (a)	Pension and Postretirement Plans (b)	Accumulated Other Comprehensive Income (Loss), Net of Tax
Balance, December 31, 2016	$ (3,109)	$ (877)	$ (3,986)
Other comprehensive loss before reclassifications, net of tax	(1,069)	(926)	(1,995)
Amounts reclassified from AOCI, net of tax	1	288	289
Net change	(1,068)	(638)	(1,706)
Balance, December 31, 2017	(4,177)	(1,515)	(5,692)
Impact from adoption of new accounting standards	(851)	(309)	(1,160)
Other comprehensive income (loss) before reclassifications, net of tax	(4,287)	1,646	(2,641)
Amounts reclassified from AOCI, net of tax	(2)	305	303
Net change	(4,289)	1,951	(2,338)
Balance, December 31, 2018	(9,317)	127	(9,190)
Other comprehensive income (loss) before reclassifications, net of tax	24,090	(4,245)	19,845
Amounts reclassified from AOCI, net of tax	668	(21)	647
Net change	24,758	(4,266)	20,492
Balance, December 31, 2019	$ 15,441	$ (4,139)	$ 11,302

(a) For additional information about securities, refer to Note 3.
(b) For additional information about retirement plans, refer to Note 13.

NOTE 24: LEGAL CONTINGENCIES

Various legal actions arise from time to time in the normal course of our business. There were no significant asserted claims or assessments at December 31, 2019. Management was not aware of any unasserted claims or assessments that may be probable of assertion at December 31, 2019.

NOTE 25: OTHER RELATED PARTY TRANSACTIONS

Loans are made to the Company's executive officers and directors and their associates during the ordinary course of business. The aggregate amount of loans to such related parties totaled $324.60 million, $341.09 million, and $363.08 million as of December 31, 2019, 2018, and 2017, respectively. During 2019, new advances on all commitments to such parties totaled $81.92 million, and repayments amounted to $557.21 million. Included in the loans to related parties, at December 31, 2019, we had $134.24 million in unfunded commitments to extend credit to such related parties.

The Company rents space for various financial centers from companies associated with its directors. Rent expense related to these leases was $2.81 million, $2.96 million, and $2.92 million for the years ended December 31, 2019, 2018, and 2017, respectively.

In the ordinary course of business, the Company acquired certain goods and services from companies associated with its directors and employees, including purchases of automobiles, construction of Company-owned facilities, and maintenance and furnishing of Company facilities. Amounts paid to these companies during the years ended December 31, 2019, 2018, and 2017, approximated $5.12 million, $7.55 million, and $1.28 million, respectively.

NOTE 26: QUARTERLY FINANCIAL DATA (UNAUDITED)

Summarized unaudited quarterly financial data for the years ended December 31, 2019 and 2018, is as follows (in thousands, except per share data):

2019	Fourth	Third	Second	First
Interest income	$ 116,475	$ 119,637	$ 117,883	$ 113,830
Interest expense	26,516	28,534	28,064	26,356
Provision for loan losses	3,601	1,508	2,824	1,438
Noninterest income	49,712	54,845	54,718	47,158
Net gain on investment securities	—	(69)	—	(776)
Noninterest expense	92,336	97,287	96,556	92,123
Income before income tax expense and noncontrolling interest	43,734	47,084	45,157	40,295
Income tax expense	7,786	7,684	8,915	8,211
Net income	35,948	39,400	36,242	32,084
Noncontrolling interest	(873)	(1,741)	(1,604)	(673)
Net income attributable to TowneBank	$ 35,075	$ 37,659	$ 34,638	$ 31,411
Net income per common share				
Basic	$ 0.49	$ 0.52	$ 0.48	$ 0.44
Diluted	$ 0.49	$ 0.52	$ 0.48	$ 0.44
Dividends	$ 0.18	$ 0.18	$ 0.18	$ 0.16

2018	Fourth	Third	Second	First
Interest income	$ 114,307	$ 110,394	$ 105,256	$ 91,866
Interest expense	25,099	21,697	18,433	15,521
Provision for loan losses	2,292	1,241	3,056	1,952
Noninterest income	42,209	49,217	50,235	49,929
Net gain on investment securities	—	—	—	3
Noninterest expense	82,337	88,262	89,221	92,304
Income before income tax expense and noncontrolling interest	46,788	48,411	44,781	32,021
Income tax expense	10,348	9,159	8,643	6,077
Net income	36,440	39,252	36,138	25,944
Noncontrolling interest	(450)	(959)	(1,334)	(1,238)
Net income attributable to TowneBank	$ 35,990	$ 38,293	$ 34,804	$ 24,706
Net income per common share				
Basic	$ 0.50	$ 0.53	$ 0.48	$ 0.36
Diluted	$ 0.50	$ 0.53	$ 0.48	$ 0.36
Dividends	$ 0.16	$ 0.16	$ 0.16	$ 0.14

NOTE 27: SEGMENT REPORTING

The Company has three reportable segments: Banking, Realty, and Insurance. The Banking segment provides loan and deposit services to retail and commercial customers throughout Richmond, Virginia, the Greater Hampton Roads area in southeastern Virginia, northeastern North Carolina, and the Greensboro, Greenville, Raleigh and Charlotte metropolitan areas in North Carolina. The Realty segment provides residential real estate services, resort property management, originations of a variety of mortgage loans, and commercial and residential title insurance. Mortgage loans are originated and sold principally in the secondary market through purchase commitments from investors. The Insurance segment provides full-service commercial and retail insurance, employee benefit services and travel insurance.

All the segments are service-based. The Banking segment offers a distribution and referral network for the realty and insurance services, and the Realty and Insurance divisions offer a similar network for the Banking segment due largely to overlapping geographic markets. A major distinction is the source of income. The Realty and Insurance businesses are fee-based, while the Banking segment is driven principally by net interest income.

Segment profit and loss is measured by net income after income tax. Inter-segment transactions are recorded at cost and eliminated as part of the consolidation process. Because of the interrelationships of the various segments, the information presented is not indicative of how the segments would perform if they operated as independent entities.

Information about reportable segments and reconciliation of such information to the Consolidated Financial Statements follows (dollars in thousands):

For the Year Ended December 31, 2019	Bank	Realty	Insurance	Consolidated Totals
Net interest income	$ 351,969	$ 6,386	$ —	$ 358,355
Provision for loan losses	9,371	—	—	9,371
Net interest income after provision for loan losses	342,598	6,386	—	348,984
Residential mortgage banking income, net	(1,631)	68,443	—	66,812
Real estate brokerage and property management income, net	—	34,292	—	34,292
Insurance commissions and other title fees and income, net	248	2,111	62,119	64,478
Other noninterest income	35,448	1,854	2,704	40,006
Noninterest expense	233,263	94,726	50,313	378,302
Income before income tax, corporate allocation, and noncontrolling interest	143,400	18,360	14,510	176,270
Corporate allocation	2,011	(1,163)	(848)	—
Income before income tax provision and noncontrolling interest	145,411	17,197	13,662	176,270
Income tax provision	25,706	3,707	3,183	32,596
Net income	119,705	13,490	10,479	143,674
Noncontrolling interest	2	(3,711)	(1,182)	(4,891)
Net income attributable to TowneBank	$ 119,707	$ 9,779	$ 9,297	$ 138,783
Net income as percentage of total	86.25%	7.05%	6.70%	100.00%
Assets	$ 10,953,815	$ 673,996	$ 319,852	$ 11,947,663
Efficiency ratio	60.29%	83.76%	77.62%	66.98%

For the Year Ended December 31, 2018	**Bank**	**Realty**	**Insurance**	**Consolidated Totals**
Net interest income	$ 329,584	$ 11,489	$ —	$ 341,073
Provision for loan losses	8,541	—	—	8,541
Net interest income after provision for loan losses	321,043	11,489	—	332,532
Residential mortgage banking income, net	(1,592)	66,696	—	65,104
Real estate brokerage and property management income, net	—	31,863	—	31,863
Insurance commissions and other title fees and income, net	449	1,877	53,838	56,164
Other noninterest income	35,403	2,091	968	38,462
Noninterest expense	208,149	101,216	42,759	352,124
Income before income tax, corporate allocation, and noncontrolling interest	147,154	12,800	12,047	172,001
Corporate allocation	1,736	(1,091)	(645)	—
Income before income tax provision and noncontrolling interest	148,890	11,709	11,402	172,001
Income tax provision	28,880	2,892	2,455	34,227
Net income	120,010	8,817	8,947	137,774
Noncontrolling interest	(8)	(2,398)	(1,575)	(3,981)
Net income attributable to TowneBank	$ 120,002	$ 6,419	$ 7,372	$ 133,793
Net income as percentage of total	89.69%	4.80%	5.51%	100.00%
Assets	$ 10,475,712	$ 441,282	$ 246,036	$ 11,163,030
Efficiency ratio	57.21%	88.77%	78.02%	66.11%

For the Year Ended December 31, 2017	**Bank**	**Realty**	**Insurance**	**Consolidated Totals**
Net interest income	$ 251,003	$ 10,118	$ —	$ 261,121
Provision for loan losses	5,426	—	—	5,426
Net interest income after provision for loan losses	245,577	10,118	—	255,695
Residential mortgage banking income, net	(394)	76,245	—	75,851
Real estate brokerage and property management income, net	—	27,487	—	27,487
Insurance commissions and other title fees and income, net	468	1,877	49,588	51,933
Other noninterest income	29,573	2,311	966	32,850
Noninterest expense	158,854	99,930	37,430	296,214
Income before income tax, corporate allocation, and noncontrolling interest	116,370	18,108	13,124	147,602
Corporate allocation	1,828	(1,210)	(618)	—
Income before income tax provision and noncontrolling interest	118,198	16,898	12,506	147,602
Income tax provision	44,584	5,791	4,438	54,813
Net income	73,614	11,107	8,068	92,789
Noncontrolling interest	1	(3,756)	(1,371)	(5,126)
Net income attributable to TowneBank	$ 73,615	$ 7,351	$ 6,697	$ 87,663
Net income as percentage of total	83.97%	8.39%	7.64%	100.00%
Assets	$ 7,842,558	$ 504,516	$ 175,102	$ 8,522,176
Efficiency ratio	56.60%	84.66%	74.04%	65.94%

The following table provides the change in net income and total assets for each segment, comparing the years ended December 31, 2019 and 2018 (dollars in thousands):

	Banking	Realty	Insurance	Consolidated
Net Income ($)	$ (295)	$ 3,360	$ 1,925	$ 4,990
Net Income (%)	(0.25)%	52.34%	26.11%	3.73%
Total Assets ($)	$ 478,103	$ 232,714	$ 73,816	$ 784,633
Total Assets (%)	4.56 %	52.74%	30.00%	7.03%

NOTE 28: EARNINGS PER SHARE

The following chart summarizes information related to the computation of basic and diluted earnings per share (dollars in thousands, except per share data):

Year Ended December 31,	**2019**	**2018**	**2017**
Basic			
Net income available to common shareholders	$ 138,783	$ 133,793	$ 87,663
Weighted average common shares outstanding	72,063,150	71,148,230	62,168,455
Basic earnings per common share	$ 1.93	$ 1.88	$ 1.41
Diluted			
Net income available to common shareholders, for diluted EPS	$ 138,783	$ 133,793	$ 87,663
Weighted average common shares outstanding	72,063,150	71,148,230	62,168,455
Effect of dilutive securities:			
Stock compensation plans (1)	125,880	144,899	225,827
Weighted average diluted shares outstanding	72,189,030	71,293,129	62,394,282
Diluted earnings per common share	$ 1.92	$ 1.88	$ 1.41

(1) Stock options and restricted stock shares totaling 7,684; 75,742; and 13,643 were excluded from the computation of diluted earnings per share during 2019, 2018, and 2017, respectively, because their inclusion would be antidilutive.

TOWNEBANK
SHAREHOLDER INFORMATION

ANNUAL MEETING

TowneBank's Annual Meeting of Stockholders will be held at 11:30 a.m. on Wednesday, May 20, 2020, at the Virginia Beach Convention Center, 1000 19th Street, Virginia Beach, Virginia 23451.

COMMON STOCK

The Company's Common Stock is listed on the Nasdaq Global Select Market under the symbol TOWN.

INVESTOR RELATIONS

Our Annual Report, Form 10-K, and other corporate publications are available to shareholders on request, without charge, by writing:

TowneBank
6001 Harbour View Boulevard
Suffolk, Virginia 23435
email: investor.relations@townebank.net

These reports are also available on our website at http://www.townebank.com/investor_relations.

INDEPENDENT AUDITORS

Dixon Hughes Goodman LLP
1400 Wells Fargo Center
440 Monticello Avenue
Norfolk, Virginia 23510

TRANSFER AGENT

Computershare Shareholder Services
P.O. Box 30170
College Station, Texas 77842-3170
800-368-5948
www.computershare.com/investor

CORPORATE COUNSEL

Williams Mullen
200 South 10th Street, Suite 1600
Richmond, Virginia 23219

Troutman Sanders L.L.P.
222 Central Park Avenue, Suite 2000
Virginia Beach, Virginia 23462

Exhibit (14)

TOWNEBANK
CHIEF EXECUTIVE OFFICER, EXECUTIVE OFFICERS and SENIOR FINANCIAL OFFICERS
CODE OF ETHICAL CONDUCT

Preface

The honesty, integrity, and sound judgment of the Chief Executive Officer ("CEO"), executive and senior financial officers are fundamental to the reputation and success of TowneBank. While all employees, officers, and directors are required to adhere to the TowneBank ***Standards of Conduct***, the professional and ethical conduct of the CEO, executive and senior financial officers is essential to the proper function and success of TowneBank as a leading financial services provider.

The CEO, executive and senior financial officers hold an important and elevated role in corporate governance. These individuals are key members of the management team, who are uniquely capable and empowered to ensure that the interests of stakeholders (including shareholders, clients, employees, suppliers, and citizens of the communities in which TowneBank operates) are appropriately balanced, protected, and preserved. The CEO, executive and senior financial officers fulfill this responsibility by prescribing and enforcing the policies and procedures employed in TowneBank's financial operations.

Code of Ethical Conduct

General standards of ethical behavior

The CEO, executive and senior financial officers of TowneBank performing accounting, audit, financial management, or similar functions must:

- Act with honesty and integrity, avoiding actual or apparent conflicts of interest in personal and professional relationships.
- Provide colleagues with information that is accurate, complete, objective, relevant, timely, and understandable.
- Comply with applicable laws, rules, and regulations of federal, state, and local governments (both United States and foreign) and other appropriate private and public regulatory agencies.
- Act in good faith, with due care, competence, and diligence, without misrepresenting material facts or allowing independent judgment to be subordinated.
- Respect the confidentiality of information acquired in the course of employment.
- Share knowledge and maintain skills necessary and relevant to TowneBank's needs.

- Proactively promote ethical and honest behavior within the workplace.

- Assure responsible use of and control of all assets, resources, and information in possession of TowneBank.

- Keep management informed of financial information of importance, including departures from sound policy, practice and accounting norms.

Standards regarding financial records and reporting
The CEO, executive and senior financial officers of TowneBank performing accounting, audit, financial management, or similar functions must:

- Establish systems and procedures to ensure business transaction are recorded in accordance with Generally Accepted Accounting Principles, company policy and appropriate regulatory pronouncements and guidelines.

- Protect and maintain accounting records and information as required by applicable law, regulation, or regulatory guidelines.

- Inform the Board of Directors and the Audit Committee of any material information that affects the disclosures made by the Bank in its public filings.

- Report to the Board of Directors and the Audit Committee concerning (a) significant deficiencies in the design and operation of internal controls or (b) any fraud involving management or other employees with a significant role in the Bank's financial reporting, disclosures or internal controls.

The CEO, executive and senior financial officers are expected to adhere to both the TowneBank ***Standards of Conduct*** and the ***TowneBank Chief Executive Officer and Senior Financial Officers Code of Ethical Conduct*** at all times. The board of directors shall have the sole and absolute discretionary authority to approve any deviation or waiver from the ***Code of Ethical Conduct***. Any waiver and the grounds for such waiver for the CEO, executive or senior financial officer shall be promptly disclosed through a filing with the Federal Deposit Insurance Corporation on Form 8-K. Additionally, any change of this ***Code of Ethical Conduct*** shall be promptly disclosed to stockholders.

The policy is applicable to the Chief Executive Officer (CEO), Chief Financial Officer (CFO), Controller, Corporate Treasurer, Internal Audit members, any person Assistant Vice President and above in an Accounting/ Financial position, Senior Financial Analyst, any Regulation O Executive Officers along with any person serving in an equivalent position regardless of whether or not they are designated as executive officers for Regulation O purposes, or any persons serving in equivalent positions within the Bank or any of its subsidiaries.

TOWNEBANK
CHIEF EXECUTIVE OFFICER, EXECUTIVE OFFICERS and SENIOR FINANCIAL OFFICERS
CODE OF ETHICAL CONDUCT

Please indicate that you have received, read and will abide by the ***TowneBank Chief Executive Officer, Executive Officer and Senior Financial Officers Code of Ethical Conduct*** by signing your name and dating the attached acknowledgment and returning it promptly to the Chairman and CEO of TowneBank.

ACKNOWLEDGMENT

I certify that I have received and read and that I will abide by the ***TowneBank Chief Executive Officer, Executive Officer and Senior Financial Officers Code of Ethical Conduct*** distributed to me on this _____________ day of _____________, 20___.

____
OFFICER

____
DATE

Exhibit (21)

Subsidiaries of TowneBank

Subsidiary	State of Incorporation or Organization
TowneBank Investment Corporation	Virginia
Towne Investments, LLC	Virginia
TowneBank Woodview Investment Co., LLC	Virginia
TowneBank Woodview Investment Co. II, LLC	Virginia
TowneBank Heritage Forest, LLC	Virginia
TowneBank Cromwell House Affordable Housing, LLC	Virginia
TowneBank Pavilion Place Affordable Housing, LLC	Virginia
TowneBank Westbury Cottages Affordable Housing, LLC	Virginia
TB Affordable Housing Equity Fund XX, LLC	Virginia
TowneBank Catalina Crossing Affordable Housing, LLC	Virginia
Hamilton Place Towne I, LLC	Virginia
Hamilton Place Towne II, LLC	Virginia
TowneBank VCDC Fund 18, LLC	Virginia
TowneBank VCDC Fund 19, LLC	Virginia
TowneBank VCDC Fund 20, LLC	Virginia
TB Affordable Housing Equity Fund XX, LLC	Virginia
TB Affordable Housing Equity Fund XXI, LLC	Virginia
TB Affordable Housing Equity Fund XXII, LLC	Virginia
TB Affordable Housing Equity Fund XXIII, LLC	Virginia
TB Forrest Landing II Affordable Housing, LLC	Virginia
TB Foundry Affordable Housing, LLC	Virginia
TB HFHWC, LLC	Virginia
TB Lake View Affordable Housing, LLC	Virginia
TB Lake View II Affordable Housing, LLC	Virginia
TB Dale II Affordable Housing, LLC	Virginia
TB NC Affordable Housing Equity Fund XXIII, LLC	Virginia
TB NC Affordable Equity Fund XXIV, LLC	Virginia
TB NMF Affordable Housting, LLC	Virginia
TB Renaissance I Affordable Housing, LLC	Virginia
TB Renaissance II Affordable Housing, LLC	Virginia
TB Sunset Hampton Affordable Housing, LLC	Virginia
TB York Senior Affordable Housing, LLC	Virginia
TB Suffolk Senior Affordable Housing, LLC	Virginia
TB Shoulders Hill Senior Affordable Housing, LLC	Virginia
Towne Financial Services Group, LLC	Virginia
GSH Residential Real Estate Corporation	Virginia
Towne Oak Island RE, LLC	Virginia
Towne Vacations Oak Island, LLC, t/a Oak Island Accommodations	Virginia
Towne Vacations, LLC, t/a Beach Properties of Hilton Head	Virginia
Palmetto Sands, LLS	Virginia
Towne Vacations Deep Creek, LLC t/a Railey Mountain Lake Vacations	Virginia
Towne Deep Creek RE, LLC	Virginia

Subsidiaries of TowneBank (continued)

Subsidiary	State of Incorporation or Organization
Deep Creek Lodging, LLC	Virginia
GSH NC Realty, LLC	Virginia
Towne Realty LLC, t/a Berkshire Hathaway HomeServices Towne Realty	Virginia
Lawyers Escrow & Title Agency, LLC	Virginia
Eastern Title Company, Inc.	Virginia
PTR Referral, LLC	Virginia
Virginia Home Title and Settlements, LLC	Virginia
Towne Insurance Agency, LLC	Virginia
The Frieden Agency LLC, t/a Towne Benefits	Virginia
Benefit Design Group, LLC	Virginia
Beneflex Management, LLC	Virginia
Towne Insurance Agency of North Carolina, LLC	North Carolina
Out of Towne, LLC, t/a Red Sky Insurance	Virginia
TowneBank Commercial Mortgage, LLC	Virginia
Towne Hall, LLC	Virginia
Towne 1031 Exchange, LLC	Virginia
Towne Security, LLC	Virginia
Towne Mortgage, LLC	Virginia
NewTowne Mortgage, LLC	Virginia
SimonTowne Mortgage, LLC	Virginia
Coastal Towne Mortgage, LLC	Virginia
Advance Financial Group, LLC	Virginia
Towne First Mortgage, LLC	Virginia
Franklin Service Corporation	Virginia
Homesale Mortgage, LLC	Virginia
Mayberry Real Estate Holdings, LLC	Virginia
PCB Trustee, INC.	Virginia
Reality Holdings, LLC	Virginia
Reality I, LLC	Virginia
Reality X, LLC	Virginia
Southeastern Virginia Investment Properties, LLC	Virginia
Southeastern Virginia Coastal Properties I, LLC	Virginia
Southeastern Virginia Properties, LLC	Virginia
Southeastern Virginia Properties at Uncles Neck, LLC	Virginia
Towne Mortgage of the Carolinas, LLC	North Carolina
Northeastern North Carolina Properties, LLC	North Carolina
Northeastern North Carolina Properties at Bermuda Bay, LLC	Virginia
Northeastern North Carolina Properties at Hamilton Cay, LLC	North Carolina
Northeastern North Carolina Properties Corolla Soundside, LLC	North Carolina
Northeastern North Carolina Properties Oceanside Villas, LLC	North Carolina
Virginia Hotel Properties, LLC	Virginia
Virginia Properties Apartment and Land, LLC	Virginia
CPF Partners, LLC	Virginia
TBNCT, LLC	North Carolina
TBVAT, LLC	Virginia
West Suffolk Properties, LLC	Virginia
TB Travel Services, LLC	Virginia

Subsidiaries of TowneBank (continued)

Subsidiary	State of Incorporation or Organization
TB Acquisition, LLC	Virginia
Monarch Investment, LLC	Virginia
Real Estate Security Agency, LLC	Virginia

TOWNEBANK

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, J. Morgan Davis, President and Chief Executive Officer, certify that:

1. I have reviewed this annual report on Form 10-K of TowneBank;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

TOWNEBANK

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize, and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

February 28, 2020	/s/ J. Morgan Davis
Date	J. Morgan Davis President/Chief Executive Officer

TOWNEBANK

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, William B. Littreal, Senior Executive Vice President and Chief Financial Officer, certify that:

1. I have reviewed this annual report on Form 10-K of TowneBank;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

TOWNEBANK

CERTIFICATION PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize, and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

February 28, 2020	/s/ William B. Littreal
Date	William B. Littreal
	Senior Executive Vice President/CFO

Exhibit (32)

Certification Pursuant to 18 U.S.C. Section 1350,
As Adopted By
Section 906 of The Sarbanes-Oxley Act of 2002

Pursuant to 18 U.S.C. §1350, as adopted by §906 of the Sarbanes-Oxley Act of 2002, each of the undersigned officers of TowneBank (the "Bank"), do hereby certify, to such officer's knowledge, that:

1. Our Annual Report on Form 10-K for the year ended December 31, 2019 (the "Report") fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934; and

2. The information contained in the Report presents fairly, in all material respects, our financial condition and results of operations as of and for the period covered by the Report.

February 28, 2020	/s/ J. Morgan Davis
Date	J. Morgan Davis President/Chief Executive Officer

February 28, 2020	/s/ William B. Littreal
Date	William B. Littreal Senior Executive Vice President/CFO

A signed original of this written statement required by Section 906 has been provided to TowneBank and will be retained by TowneBank and furnished to the Federal Deposit Insurance Corporation or its staff upon request.