Oak Valley Bancorp
Form 10-Q
November 14, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2013

OR

o TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 001-34142

OAK VALLEY BANCORP

(Exact name of registrant as specified in its charter)

California	**26-2326676**

State or other jurisdiction of incorporation or organization	I.R.S. Employer Identification No.

125 N. Third Ave., Oakdale, CA 95361

(Address of principal executive offices)

(209) 848-2265

Issuer s telephone number

Not applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the issuer (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 o

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

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

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: 7,929,730 shares of common stock outstanding as of October 31, 2013.

Table of Contents

Oak Valley Bancorp

September 30, 2013

Table of Contents

Table of Contents

PART I FINANCIAL STATEMENTS

Item 1. Consolidated Financial Statements (Unaudited)

OAK VALLEY BANCORP

CONDENSED CONSOLIDATED BALANCE SHEETS

AT SEPTEMBER 30, 2013 (UNAUDITED) AND DECEMBER 31, 2012 (AUDITED)

		September 30, 2013		December 31, 2012
ASSETS				
Cash and due from banks	$	84,312,827	$	130,799,998
Federal funds sold		15,495,000		10,535,000
Cash and cash equivalents		99,807,827		141,334,998
Securities available for sale		117,142,396		103,865,881
Loans, net of allowance for loan loss of $7,669,305 and $7,974,975 at September 30, 2013 and December 31, 2012, respectively		405,544,603		382,411,361
Bank premises and equipment, net		12,607,621		13,182,451
Other real estate owned		916,205		0
Interest receivable and other assets		23,173,299		19,786,065
	$	659,191,951	$	660,580,756
LIABILITIES AND SHAREHOLDERS EQUITY				
Deposits	$	591,642,194	$	586,992,650
Interest payable and other liabilities		4,170,838		3,619,382
Total liabilities		595,813,032		590,612,032
Commitments and contingencies				
Shareholders equity				
Series B Preferred stock, no par value; $1,000 per share liquidation preference, 10,000,000 shares authorized, 6,750 shares issued and outstanding at December 31, 2012		0		6,750,000
Common stock, no par value; 50,000,000 shares authorized, 7,929,730 and 7,907,780 shares issued and outstanding at September 30, 2013 and December 31, 2012, respectively		23,758,210		23,673,210
Additional paid-in capital		2,483,466		2,341,814
Retained earnings		38,070,279		33,958,737
Accumulated other comprehensive (loss) income, net of tax		(933,036)		3,244,963
Total shareholders equity		63,378,919		69,968,724
	$	659,191,951	$	660,580,756

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

OAK VALLEY BANCORP

CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

FOR THE THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2013 AND SEPTEMBER 30, 2012

	THREE MONTHS ENDED SEPTEMBER 30, 2013	THREE MONTHS ENDED SEPTEMBER 30, 2012	NINE MONTHS ENDED SEPTEMBER 30, 2013	NINE MONTHS ENDED SEPTEMBER 30, 2012
INTEREST INCOME				
Interest and fees on loans	$ 5,275,934	$ 5,633,389	$ 15,818,856	$ 16,934,021
Interest on securities available for sale	893,472	860,565	2,550,412	2,572,096
Interest on federal funds sold	5,315	6,568	17,012	16,192
Interest on deposits with banks	49,268	28,327	160,809	83,114
Total interest income	6,223,989	6,528,849	18,547,089	19,605,423
INTEREST EXPENSE				
Deposits	193,547	274,963	643,319	870,925
FHLB advances				4,707
Total interest expense	193,547	274,963	643,319	875,632
Net interest income	6,030,442	6,253,886	17,903,770	18,729,791
PROVISION FOR LOAN LOSSES	100,000	300,000	300,000	900,000
Net interest income after provision for loan losses	5,930,442	5,953,886	17,603,770	17,829,791
OTHER INCOME				
Service charges on deposits	318,064	287,101	903,599	868,677
Earnings on cash surrender value of life insurance	100,660	105,000	306,207	315,000
Mortgage commissions	59,944	63,792	196,646	171,579
Gains on called securities	18,091	35,406	52,656	70,410
Other	368,807	299,150	1,008,802	868,169
Total non-interest income	865,566	790,449	2,467,910	2,293,835
OTHER EXPENSES				
Salaries and employee benefits	2,451,037	2,462,468	7,590,178	7,552,214
Occupancy expenses	738,937	766,401	2,220,320	2,260,483
Data processing fees	330,603	282,347	938,206	838,211
OREO expenses	1,409		2,193	18,358
Regulatory assessments (FDIC & DFI)	120,000	114,000	360,000	347,000
Other operating expenses	976,444	901,973	2,880,486	2,719,706
Total non-interest expense	4,618,430	4,527,189	13,991,383	13,735,972
Net income before provision for income taxes	2,177,578	2,217,146	6,080,297	6,387,654
PROVISION FOR INCOME TAXES	672,358	738,315	1,901,255	2,095,958
NET INCOME	$ 1,505,220	$ 1,478,831	$ 4,179,042	$ 4,291,696
Preferred stock dividends		84,375	67,500	367,500
NET INCOME AVAILABLE TO COMMON SHAREHOLDERS	$ 1,505,220	$ 1,394,456	$ 4,111,542	$ 3,924,196

NET INCOME PER COMMON SHARE	$	0.19	$	0.18	$	0.53	$	0.51
NET INCOME PER DILUTED COMMON SHARE	$	0.19	$	0.18	$	0.52	$	0.51

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

OAK VALLEY BANCORP

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME (UNAUDITED)

FOR THE THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2013 AND SEPTEMBER 30, 2012

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2013	2012	2013	2012
Net income	$ 1,505,220	$ 1,478,831	$ 4,179,042	$ 4,291,696
Available for sale securities:				
Gross unrealized (loss) gain arising during the period	(2,762,108)	671,119	(7,046,747)	1,537,797
Reclassification adjustment for gains realized in net income (net of income tax of $7,444 and $21,668 for the three and nine months ended September 30, 2013, respectively and $14,570 and $28,974 for the comparable 2012 periods)	(10,647)	(20,836)	(30,988)	(41,436)
Income tax benefit (expense) related to unrealized gains/losses	1,136,608	(276,166)	2,899,736	(632,804)
Other comprehensive (loss) gain	(1,636,147)	374,117	(4,177,999)	863,557
Comprehensive (loss) income	$ (130,927)	$ 1,852,948	$ 1,043	$ 5,155,253

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

OAK VALLEY BANCORP

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

FOR THE YEAR ENDED DECEMBER 31, 2012 AND THE NINE-MONTH PERIOD ENDED SEPTEMBER 30, 2013 (UNAUDITED)

YEAR ENDED DECEMBER 31, 2012 AND NINE MONTHS ENDED SEPTEMBER 30, 2013	Common Stock Shares	Common Stock Amount	Preferred Stock Shares	Preferred Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders Equity
Balances, January 1, 2012	7,718,469	$ 23,453,443	13,500	$ 13,500,000	$ 2,128,700	$ 28,629,757	$ 2,690,106	$ 70,402,006
Stock options exercised	54,436	219,767						219,767
Tax benefit on stock options exercised					37,218			37,218
Restricted stock issued	134,875							
Repurchase of Series B preferred stock			(6,750)	$ (6,750,000)				(6,750,000)
Preferred stock dividend payments						(451,875)		(451,875)
Stock based compensation					175,896			175,896
Other comprehensive income							554,857	554,857
Net income						5,780,855		5,780,855
Balances, December 31, 2012	7,907,780	$ 23,673,210	6,750	$ 6,750,000	$ 2,341,814	$ 33,958,737	$ 3,244,963	$ 69,968,724
Stock options exercised	11,250	85,000						85,000
Restricted stock issued	15,000							
Restricted stock cancelled	(4,300)							
Repurchase of Series B preferred stock			(6,750)	$ (6,750,000)				(6,750,000)
Preferred stock dividend payments						(67,500)		(67,500)
Stock based compensation					141,652			141,652
Other comprehensive loss							(4,177,999)	(4,177,999)
Net income						4,179,042		4,179,042
Balances, September 30, 2013	7,929,730	$ 23,758,210	0	$ 0	$ 2,483,466	$ 38,070,279	$ (933,036)	$ 63,378,919

The accompanying notes are an integral part of these consolidated financial statements

Table of Contents

OAK VALLEY BANCORP

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

FOR THE NINE MONTH PERIODS ENDED SEPTEMBER 30, 2013 AND SEPTEMBER 30, 2012

	NINE MONTHS ENDED SEPTEMBER 30, 2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 4,179,042	$ 4,291,696
Adjustments to reconcile net earnings to net cash from operating activities:		
Provision for loan losses	300,000	900,000
Increase (decrease) in deferred fees/costs, net	42,674	(81,575)
Depreciation	860,624	848,181
Amortization of investment securities, net	194,852	166,228
Stock based compensation	141,652	128,036
Excess tax benefits from stock-based payment arrangements	0	(37,218)
Loss (gain) on sale of premises and equipment	31,650	(22,498)
Gain on sale of OREO	(16,629)	(3,548)
Gain on called available for sale securities	(52,656)	(70,410)
Earnings on cash surrender value of life insurance	(306,207)	(315,000)
Increase in interest payable and other liabilities	551,456	3,092,985
Increase in interest receivable	(100,634)	(76,105)
Increase in other assets	(58,989)	(644,782)
Net cash from operating activities	5,766,835	8,175,990
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of available for sale securities	(34,186,448)	(40,439,977)
Proceeds from maturities, calls, and principal paydowns of securities available for sale	13,668,334	25,174,459
Net (increase) decrease in loans	(25,357,546)	5,931,726
Purchase of FRB Stock	0	(1,450)
Redemption of FHLB stock	0	400,500
Proceeds from sale of OREO	982,054	247,923
Proceeds from sales of premises and equipment	5,625	22,498
Net purchases of premises and equipment	(323,069)	(453,125)
Net cash used in investing activities	(45,211,050)	(9,117,446)
CASH FLOWS FROM FINANCING ACTIVITIES:		
FHLB payments	0	(3,000,000)
Preferred stock dividend payment	(67,500)	(367,500)
Repurchase of Series B preferred stock	(6,750,000)	(6,750,000)
Net decrease in demand deposits and savings accounts	9,768,849	19,164,074
Net decrease in time deposits	(5,119,305)	(2,034,616)
Excess tax benefits from stock-based payment arrangements	0	37,218
Proceeds from sale of common stock and exercise of stock options	85,000	219,767
Net cash (used in) from financing activities	(2,082,956)	7,268,943
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(41,527,171)	6,327,487
CASH AND CASH EQUIVALENTS, beginning of period	141,334,998	101,084,775
CASH AND CASH EQUIVALENTS, end of period	$ 99,807,827	$ 107,412,262

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:				
Cash paid during the period for:				
Interest	$	653,682	$	931,745
Income taxes	$	1,520,000	$	965,000
NON-CASH INVESTING ACTIVITIES:				
Real estate acquired through foreclosure	$	1,881,630	$	0
Change in unrealized (loss)/gain on available-for-sale securities	$	(7,099,403)	$	1,467,387

The accompanying notes are an integral part of these consolidated financial statements.

Table of Contents

OAK VALLEY BANCORP

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 BASIS OF PRESENTATION

On July 3, 2008 (the Effective Date), a bank holding company reorganization was completed whereby Oak Valley Bancorp (the Company) became the parent holding company for Oak Valley Community Bank (the Bank). On the Effective Date, each outstanding share of the Bank was converted into one share of Oak Valley Bancorp and the Bank became a wholly-owned subsidiary of the holding company.

The accounting principles followed by the Company and the methods of applying these principles conform with accounting principles generally accepted in the United States of America (GAAP) and with general practices within the banking industry. In preparing financial statements in conformity with GAAP, management is required to make estimates and assumptions that affect the reported amounts in the financial statements. Actual results could differ significantly from those estimates. Material estimates common to the banking industry that are particularly susceptible to significant change in the near term include, but are not limited to, the determination of the allowance for loan losses, fair values of financial instruments, the estimation of compensation expense related to stock options granted to employees and directors, and valuation allowances associated with deferred tax assets, the recognition of which are based on future taxable income.

The interim consolidated financial statements included in this report are unaudited but reflect all adjustments which, in the opinion of management, are necessary for a fair presentation of the financial position and results of operations for the interim periods presented. All such adjustments are of a normal recurring nature. The results of operations for the three and nine month periods ended September 30, 2013 are not necessarily indicative of the results of a full year s operations. Certain prior year amounts have been reclassified to conform to the current year presentation. There was no effect on net income or shareholders equity. For further information, refer to the audited consolidated financial statements and footnotes included in the Company s Form 10-K for the year ended December 31, 2012.

NOTE 2 RECENT ACCOUNTING PRONOUNCEMENTS

In December 2011, the FASB issued ASU No. 2011-11, *Disclosures about Offsetting Assets and Liabilities.* The update requires an entity to offset, and present as a single net amount, a recognized eligible asset and a recognized eligible liability when it has an unconditional and legally enforceable right of setoff and intends either to settle the asset and liability on a net basis or to realize the asset and settle the liability simultaneously. The ASU requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. The amendments are effective for annual and interim reporting periods beginning on or after January 1, 2013 and did not have a material impact on the Company s consolidated financial statements.

In January 2013, the FASB issued ASU No. 2013-01, *Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities*. The Update clarifies that ASU. 2011-11 applies only to derivatives, including bifurcated embedded derivatives, repurchase agreements and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either offset or subject to an enforceable master netting arrangement or similar agreement. Entities with other types of financial assets and financial liabilities subject to a master netting arrangement or similar agreement are no longer subject to the disclosure requirements in ASU. 2011-11. The amendments are effective for annual and interim reporting periods beginning on or after January 1, 2013 and did not have a material impact on the Company s consolidated financial statements.

In February 2013, the FASB issued ASU No. 2013-02*, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. The Update requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component and to present either on the face of the statement where net income is presented, or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income, but only if the amount reclassified is required to be reclassified to net income in its entirety in the same reporting period. The amendments are effective for annual and interim reporting periods beginning on or after December 15, 2012 and did not have a material impact on the Company s consolidated financial statements.

In February 2013, the FASB issued ASU No. 2013-04, *Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation Is Fixed at the Reporting Date.* The Update requires an entity to measure obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of this guidance is fixed at the reporting date, as the sum of the following: 1) The amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors, and 2) Any additional amount the reporting entity expects to pay on behalf of its co-obligors. The guidance in this Update also requires an entity to disclose the nature and amount of the obligation as well as other information about those obligations. The amendments in this Update are effective for fiscal years, and interim periods within those years, beginning after December 15, 2013, and are applied retrospectively to all prior periods presented for those obligations resulting from joint and several liability arrangements within the Update s scope that exist at the beginning of an entity s fiscal year of adoption. The adoption of ASU No. 2013-04 is not expected to have a material impact on the Company s consolidated financial statements.

Table of Contents

In July 2013, the FASB issued ASU No. 2013-10, *Inclusion of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a Benchmark Interest Rate for Hedge Accounting Purposes*. ASU No. 2013-10 permits the use of the Fed Funds Effective Swap Rate (OIS) to be used as a U.S. benchmark interest rate for hedge account purposes. The amendment is effective prospectively for qualifying new or redesiginated hedging relationships entered into on or after July 17, 2013. The adoption of ASU No. 2013-10 is not expected to have a material impact on the Company s consolidated financial statements

In July 2013, the FASB issued ASU No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*. ASU No. 2013-11 requires an entity to present an unrecognized tax benefit, or a portion of an unrecognized tax benefit, as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, except to the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. No new recurring disclosures are required. The amendments are effective for annual and interim reporting periods beginning on or after December 15, 2013 and are to be applied prospectively to all unrecognized tax benefits that exist at the effective date. Retrospective application is permitted. The adoption of ASU No. 2013-11 is not expected to have a material impact on the Company s consolidated financial statements.

NOTE 3 PREFERRED STOCK REPURCHASE AND WARRANT REDEMPTION

In August 2011, the Company repurchased the $13,500,000 of Series A Preferred Stock originally issued to the U.S. Treasury in December 2008 in connection with the Company s participation in the Capital Purchase Program (CPP). The Company simultaneously issued $13,500,000 in Series B Preferred Stock to the U.S. Treasury under the Small Business Lending Funding (SBLF) program. Subsequently, the Company fully redeemed a warrant to purchase 350,346 shares of its Common Stock, at the exercise price of $5.78 per share that the Company had granted to the U.S. Treasury pursuant to the CPP, for a purchase price of $560,000, which settled in September 2011.

In May 2012, the Company repurchased from the U.S. Treasury 6,750 shares of Series B Preferred Stock for aggregate consideration of $6.75 million. In March 2013, the Company repurchased the remaining 6,750 shares of Series B Preferred Stock for aggregate consideration of $6.75 million plus $67,500 for accrued interest. As of September 30, 2013, there are no outstanding shares of Series B Preferred Stock.

NOTE 4 SECURITIES

The amortized cost and estimated fair values of debt securities as of September 30, 2013 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				
U.S. agencies	$ 52,622,388	$ 1,953,129	$ (1,264,298)	$ 53,311,218

Collateralized mortgage obligations	10,195,441	301,335	(68,859)	10,427,918
Municipalities	41,318,794	898,084	(3,379,578)	38,837,299
SBA Pools	1,102,217	0	(4,730)	1,097,487
Corporate debt	4,690,201	107,445	0	4,797,646
Asset Backed Securities	5,849,203	18,872	(19,555)	5,848,520
Mutual Fund	2,949,126	0	(126,819)	2,822,308
	$ 118,727,370	$ 3,278,865	$ (4,863,839)	$ 117,142,396

Table of Contents

The following tables detail the 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 at September 30, 2013.

	Less than 12 months		12 months or more		Total	
Description of Securities	**Fair Value**	**Unrealized Loss**	**Fair Value**	**Unrealized Loss**	**Fair Value**	**Unrealized Loss**
U.S. agencies	$ 20,097,272	$ (1,015,959)	$ 1,747,229	$ (248,339)	$ 21,844,501	$ (1,264,298)
Collateralized mortgage obligations	1,672,944	(68,859)	0	0	1,672,944	(68,859)
Municipalities	26,848,775	(3,254,021)	1,024,109	(125,557)	27,872,884	(3,379,578)
SBA Pools	847,113	(3,598)				