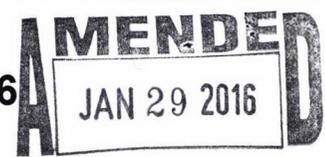


CORRECTED 1/24/2016

Board of Governors of the Federal Reserve System



Annual Report of Holding Companies—FR Y-6



Report at the close of business as of the end of fiscal year

This Report is required by law: Section 5(c)(1)(A) of the Bank Holding Company Act (12 U.S.C. § 1844 (c)(1)(A)); Section 8(a) of the International Banking Act (12 U.S.C. § 3106(a)); Sections 11(a)(1), 25 and 25A of the Federal Reserve Act (12 U.S.C. §§ 248(a)(1), 602, and 611a); Section 211.13(c) of Regulation K (12 C.F.R. § 211.13(c)); and Section 225.5(b) of Regulation Y (12 C.F.R. § 225.5(b)) and section 10(c)(2)(H) of the Home Owners' Loan Act. Return to the appropriate Federal Reserve Bank the original and the number of copies specified.

This report form is to be filed by all top-tier bank holding companies and top-tier savings and loan holding companies organized under U.S. law, and by any foreign banking organization that does not meet the requirements of and is not treated as a qualifying foreign banking organization under Section 211.23 of Regulation K (12 C.F.R. § 211.23). (See page one of the general instructions for more detail of who must file.) The Federal Reserve may not conduct or sponsor, and an organization (or a person) is not required to respond to, an information collection unless it displays a currently valid OMB control number.

NOTE: The *Annual Report of Holding Companies* must be signed by one director of the top-tier holding company. This individual should also be a senior official of the top-tier holding company. In the event that the top-tier holding company does not have an individual who is a senior official and is also a director, the chairman of the board must sign the report.

Date of Report (top-tier holding company's fiscal year-end):
December 31, 2015

Month / Day / Year

N/A

Reporter's Legal Entity Identifier (LEI) (20-Character LEI Code)

I, Embry Hines

Name of the Holding Company Director and Official

President

Title of the Holding Company Director and Official

attest that the *Annual Report of Holding Companies* (including the supporting attachments) for this report date has been prepared in conformance with the instructions issued by the Federal Reserve System and are true and correct to the best of my knowledge and belief.

Reporter's Name, Street, and Mailing Address

Chico Bancorp, Inc.

Legal Title of Holding Company

P.O. Box 5

(Mailing Address of the Holding Company) Street / P.O. Box

Chico TX 76431

City State Zip Code

201 S. Weatherford, Chico, TX 76431

Physical Location (if different from mailing address)

With respect to information regarding individuals contained in this report, the Reporter certifies that it has the authority to provide this information to the Federal Reserve. The Reporter also certifies that it has the authority, on behalf of each individual, to consent or object to public release of information regarding that individual. The Federal Reserve may assume, in the absence of a request for confidential treatment submitted in accordance with the Board's "Rules Regarding Availability of Information," 12 C.F.R. Part 261, that the Reporter and individual consent to public release of all details in the report concerning that individual.

Person to whom questions about this report should be directed:

Steve Holt Chief Financial Officer

Name Title

940-683-6300

Area Code / Phone Number / Extension

940-683-1807

Area Code / FAX Number

steve@fsbwise.com

E-mail Address

http://www.fsbwise.com

Address (URL) for the Holding Company's web page

Signature of Holding Company Director and Official

01/26/2016

Date of Signature

For holding companies not registered with the SEC—
Indicate status of Annual Report to Shareholders:
 is included with the FR Y-6 report
 will be sent under separate cover
 is not prepared

For Federal Reserve Bank Use Only
RSSD ID 2088208
C.I. _____

Does the reporter request confidential treatment for any portion of this submission?
 Yes Please identify the report items to which this request applies:
 In accordance with the instructions on pages GEN-2 and 3, a letter justifying the request is being provided.
 The information for which confidential treatment is sought is being submitted separately labeled "Confidential."
 No

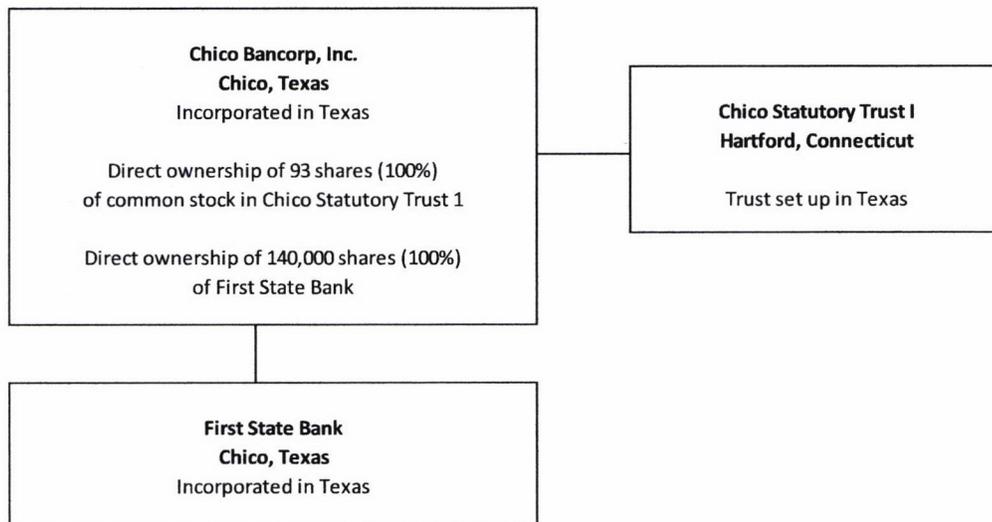
Form FR Y-6

CHICO BANCORP, INC
Chico, Texas
Fiscal Year Ending December 31, 2015

Report Item

- 1: a. The BHC is not required to file Form 10(k) with the SEC.
- b. The BHC does not prepare an annual report for its shareholders.

2. Organizational Chart



Note: No entity has a LEI

- 3. Domestic Branch Verification listing emailed to structure.verification@dal.frb.org 01/20/2016.

Results: A list of branches for your holding company: **CHICO BANCORP, INC. (2088208)** of **CHICO, TX**.
The data are as of **12/31/2015**. Data reflects information that was received and processed through **NDI/07/2016**.

Reconciliation and Verification Steps

1. In the **Data Action** column of each branch row, enter one or more of the actions specified below.
2. If required, enter the date in the **Effective Date** column.

Actions

OK: If the branch information is correct, enter 'OK' in the **Data Action** column.

Change: If the branch information is incorrect or incomplete, revise the data, enter 'Change' in the **Data Action** column and the date when this information first became valid in the **Effective Date** column.

Close: If a branch listed was sold or closed, enter 'Close' in the **Data Action** column and the sale or closure date in the **Effective Date** column.

Delete: If a branch listed was never owned by this depository institution, enter 'Delete' in the **Data Action** column.

Add: If a reportable branch is missing, insert a row, add the branch data, and enter 'Add' in the **Data Action** column and the opening or acquisition date in the **Effective Date** column.

If printing this list, you may need to adjust your page setup in MS Excel. Try using landscape orientation, page scaling, and/or legal sized paper.

Submission Procedure

When you are finished, send a saved copy to your FRB contact. See the detailed instructions on this site for more information.

If you are e-mailing this to your FRB contact, put your institution name, city and state in the subject line of the e-mail.

Note:

To satisfy the **FR Y-10 reporting requirements**, you must also submit FR Y-10 Domestic Branch Schedules for each branch with a **Data Action** of **Change, Close, Delete, or Add**.

The FR Y-10 report may be submitted in a hardcopy format or via the FR Y-10 Online application - <https://y10online.federalreserve.gov>.

* FDIC UNINUM, Office Number, and ID_RSSD columns are for reference only. Verification of these values is not required.

Data Action	Effective Date	Branch Service Type	Branch ID_RSSD*	Popular Name	Street Address	City	State	Zip Code	County	Country	FDIC UNINUM*	Office Number*	Head Office	Head Office ID_RSSD*	Comments
OK		Full Service (Head Office)	750154	FIRST STATE BANK	201 SOUTH WEATHERFORD	CHICO	TX	76431	WISE	UNITED STATES	11797	0	FIRST STATE BANK	750154	
OK		Full Service	2317832	BRIDGEPORT BRANCH	1709 9TH STREET	BRIDGEPORT	TX	76426	WISE	UNITED STATES	473979	4	FIRST STATE BANK	750154	
OK		Full Service	3604191	PARADISE BRANCH	630 MAIN STREET	PARADISE	TX	76073-274	WISE	UNITED STATES	464831	3	FIRST STATE BANK	750154	
OK		Full Service	2798673	RUNAWAY BAY BRANCH	102 PORT-O-CALL DRIVE	RUNAWAY BAY	TX	76426	WISE	UNITED STATES	243021	2	FIRST STATE BANK	750154	

CHICO BANCORP, INC. (2088208)
CHICO, TX

Fiscal Year Ending December 31, 2015

Report Item 3: Securities Holders			Securities Holders not listed in 3(1)(a) through (3)(1)(c) that had ownership, control or holdings of 5% or more with power to vote during the fiscal year ending 12-31-2015		
Current Securities Holders with ownership, control or holdings of 5% or more with power to vote as of fiscal year ending 12-31-2015					
(1)(a) Name & Address (City, State, Country)	(1)(b) Country of Citizenship or Incorporation	(1)(c) Number and Percentage of Each Class of Voting Securities	(2)(a) Name & Address (City, State, Country)	(2)(b) Country of Citizenship or Incorporation	(2)(c) Number and Percentage of Each Class of Voting Securities
Bailey Family Group Berniece Bailey Chico, TX, USA	USA	750 shares, 20.37% (common) 730 shares, 19.83% (common)	Perry Johnson Chico, TX	USA	757 shares, 20.57% (common)
Cyd Bailey Chico, TX, USA	USA	20 shares, 0.54% (common)			
Cook Family Group		472 shares, 12.82% (common)			
Jan Cook Bridgeport, TX	USA	467 shares, 12.69% (common)			
Jamie Cook Bridgeport, TX	USA	5 shares, 0.14% (common)			
Hines Family Group		587 shares, 15.95% (common)			
Georgia Family Holdings LP (Embry Hines) Runaway Bay, TX	USA	587 shares, 15.95% (common)			
Johnson Family Group		797 shares, 21.65% (common)			
Patsy Johnson Chico, TX	USA	757 shares, 20.57% (common)			
Patrick Johnson Chico, TX	USA	40 shares, 1.09% (common)			

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AUG 23 2016
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Form FR Y-6

CHICO BANCORP, INC. (2088208)
CHICO, TX

Fiscal Year Ending December 31, 2015

Report Item 3: Securities Holders		Securities Holders not listed in 3(1)(a) through (3)(1)(c) that had ownership, control or holdings of 5% or more with power to vote during the fiscal year ending 12-31-2015	
Current Securities Holders with ownership, control or holdings of 5% or more with power to vote as of fiscal year ending 12-31-2015		(1)(c)	(2)(a)
(1)(a) Name & Address (City, State, Country)	(1)(b) Country of Citizenship or Incorporation	(1)(c) Number and Percentage of Each Class of Voting Securities	(2)(a) Name & Address (City, State, Country)
Reasoner Family Group		656 shares, 17.82% (common)	
Paul Reasoner Chico, TX	USA	588 shares, 15.97% (common)	(2)(b) Country of Citizenship or Incorporation
David Greg Reasoner Boyd, TX	USA	50 shares, 1.36% (common)	(2)(c) Number and Percentage of Each Class of Voting Securities
Dr. Alicia Sherea Reasoner Fort Worth, TX	USA	12 shares, 0.33% (common)	
Peggy E. Corbell Decatur, TX	USA	6 shares, 0.16% (common)	

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AUG 23 2016

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Form FR Y-6

CHICO BANCORP, INC. (2088208)
CHICO, TX

Fiscal Year Ending December 31, 2015

Report Item 4: Insiders

(1)(a)(b)(c) and (2)(a)(b)(c)

(1)	(2)	(3)(a)	(3)(b)	(3)(c)	(4)(a)	(4)(b)	(4)(c)
Names & Address (City, State, Country)	Principal Occupation if other than with holding company	Title & Position with holding company	Title & Position with Subsidiaries (include names of subsidiaries)	Title & Position with Other Businesses (include names of other businesses)	Percentage of Voting Securities in holding company	Percentage of Voting Securities in Subsidiaries (include names of subsidiaries)	List names of other companies (includes partnerships) if 25% or more of voting securities are held (List names of companies and percentage of voting securities held)
Berniece Bailey Chico, TX, USA	Retired - Banker	Principal Shareholder	N/A	N/A	19.832%	None	N/A
Cyd Bailey Chico, TX, USA	Banker	Director	Director (First State Bank)	N/A	0.540%	None	N/A
Georgia Family Holdings LP (Embry Hines) Runaway Bay, TX, USA	N/A	Principal Shareholder	N/A	N/A	15.947%	None	N/A
Patsy Johnson Chico, TX, USA	Retired Grocer/Retail Owner	Principal Shareholder	N/A	N/A	20.565%	None	N/A
Paul Reasoner Chico, TX, USA	Retired - Banker	Principal Shareholder	N/A	N/A	15.974%	None	N/A
J.P. Carpenter Bridgeport, TX, USA	Oil & Gas Servicing Company Owner	Director	Director (First State Bank)	Manager Bridgeport Truck Parts, LLC	2.988%	None	Bridgeport Truck Parts, LLC 100% Sholt 7/26/2016

AMENDED
JUL 26 2016

Form FR Y-6

CHICO BANCORP, INC. (2088208)
CHICO, TX

Fiscal Year Ending December 31, 2015

Report Item 4: Insiders

(1)(a)(b)(c) and (2)(a)(b)(c)

(1)	(2)	(3)(a)	(3)(b)	(3)(c)	(4)(a)	(4)(b)	(4)(c)
Names & Address (City, State, Country)	Principal Occupation if other than with holding company	Title & Position with holding company	Title & Position with Subsidiaries (include names of subsidiaries)	Title & Position with Other Businesses (include names of other businesses)	Percentage of Voting Securities in holding company	Percentage of Voting Securities in Subsidiaries (include names of subsidiaries)	List names of other companies (includes partnerships) if 25% or more of voting securities are held (List names of companies and percentage of voting securities held)
Jan Cook Bridgeport, TX, USA	Retired Trucking Company Manager	Director	Director (First State Bank)	N/A	12.687%	None	N/A
Jamie Cook Bridgeport, TX, USA	Banker	Director Vice President	Director & EVP (First State Bank)	N/A	0.136%	None	N/A
Embry Hines Runaway Bay, TX, USA	Banker	Director Chairman President	Director, President and Chief Executive Officer (First State Bank)	N/A	0.000%	None	N/A
Corey Ingram Bridgeport, TX, USA	Banker	Director	Director and Branch President, (First State Bank)	N/A	0.326%	None	N/A
Patrick Johnson Chico, TX, USA	Investments Farming/Ranching	Director	Director (First State Bank)	N/A	1.087%	None	N/A

AMENDED
JUL 26 2016

Form FR Y-6

CHICO BANCORP, INC. (2088208)
CHICO, TX

Fiscal Year Ending December 31, 2015

Report Item 4: Insiders

(1)(a)(b)(c) and (2)(a)(b)(c)

(1)	(2)	(3)(a)	(3)(b)	(3)(c)	(4)(a)	(4)(b)	(4)(c)
Names & Address (City, State, Country)	Principal Occupation if other than with holding company	Title & Position with Subsidiaries (include names of subsidiaries)	Title & Position with Other Businesses (include names of other businesses)	Percentage of Voting Securities in holding company	Percentage of Voting Securities in Subsidiaries (include names of subsidiaries)	Percentage of Voting Securities in Subsidiaries (include names of subsidiaries)	List names of other companies (includes partnerships) if 25% or more of voting securities are held (List names of companies and percentage of voting securities held)
Randy McComis Bridgeport, TX, USA	Insurance Agent	Director	Director (First State Bank)	Vice President - Meyers & McComis, Inc.	0.407%	None	Meyers & McComis, Inc. - 50% Meyers & McComis Partnership - 50% MMI Insurance Agency, LLC (70% owned by Meyers- McComis, Inc.
Shelly Prost Decatur, TX, USA	Banker	Director Secretary	Director and Branch President, (First State Bank)	N/A	1.413%	None	N/A

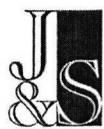
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FORM FR Y-6
Report Item 1:a.

**FIRST STATE BANKSHARES, INC.
AND SUBSIDIARY**

**FINANCIAL STATEMENTS AND
INDEPENDENT ACCOUNTANT'S REPORT**

December 31, 2015 and 2014

 **JOHNSON & SHELDON, PLLC**
CERTIFIED PUBLIC ACCOUNTANTS

FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

December 31, 2015 and 2014

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JOHNSON & SHELDON, PLLC

CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors
First State Bankshares, Inc. and Subsidiary
Spearman, Texas

INDEPENDENT ACCOUNTANT'S REPORT

We have reviewed the accompanying consolidated financial statements of **First State Bankshares, Inc. and Subsidiary** (the Company), which comprise the balance sheet as of December 31, 2015, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity and cash flows for the year then ended, and the related notes to the financial statements. A review includes primarily applying analytical procedures to management's financial data and making inquiries of management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, we do not express such an opinion.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement whether due to fraud or error.

Accountant's Responsibility

Our responsibility is to conduct the review engagement in accordance with Statements on Standards for Accounting and Review Services promulgated by the Accounting and Review Services Committee of the AICPA. Those standards require us to perform procedures to obtain limited assurance as a basis for reporting whether we are aware of any material modifications that should be made to the financial statements for them to be in accordance with accounting principles generally accepted in the United States of America. We believe that the results of our procedures provide a reasonable basis for our conclusion.

Accountant's Conclusion

Based on our review, we are not aware of any material modifications that should be made to the accompanying 2015 financial statements in order for them to be in accordance with accounting principles generally accepted in the United States of America.

Report on 2014 Financial Statements

The 2014 financial statements of **First State Bankshares, Inc. and Subsidiary** were audited by us and we expressed an unqualified opinion on those financial statements in our report, dated April 17, 2015, but we have not performed any auditing procedures since that date.

Johnson & Sheldon, PLLC

Johnson & Sheldon, PLLC

April 8, 2016

FINANCIAL STATEMENTS



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

December 31, 2015 and 2014

	(Reviewed)	
	2015	2014
Assets		
Cash and due from banks	\$ 2,862,873	\$ 3,342,101
Interest bearing deposits at other banks	31,191,866	23,229,692
Federal funds sold	765,000	-
Investment securities available for sale	27,994,671	30,827,797
Loans, net of allowance for loan loss of \$701,687 and \$645,628, respectively	73,178,264	78,321,292
Investments in restricted stock, at cost	371,600	379,600
Accrued interest receivable	1,008,250	831,727
Premises and equipment, net	394,940	429,658
Other assets	388,973	342,706
	<u>138,156,437</u>	<u>137,704,573</u>
Total Assets	\$ 138,156,437	\$ 137,704,573
Liabilities and Stockholders' Equity		
Liabilities		
Deposits:		
Demand - noninterest bearing	\$ 34,660,618	\$ 32,599,465
Demand - interest bearing	34,227,620	32,199,558
Savings	6,139,079	6,296,994
Time deposits, \$100,000 and over	29,356,898	28,843,283
Other time deposits	11,195,392	12,198,653
Total Deposits	115,579,607	112,137,953
Federal funds purchased	-	2,615,000
Pension benefit obligation	2,103,455	1,734,090
Accrued interest and other liabilities	378,861	381,173
Other borrowings	10,569,168	11,228,023
Total Liabilities	128,631,091	128,096,239
Stockholders' Equity		
Preferred stock	-	-
Common stock	200,000	200,000
Additional paid-in capital	7,315,786	7,315,786
Retained earnings	8,561,030	8,315,517
Accumulated other comprehensive income (loss)	(2,147,969)	(1,819,468)
	13,928,847	14,011,835
Treasury stock, at cost, 75,081 shares	(4,403,501)	(4,403,501)
Total Stockholders' Equity	9,525,346	9,608,334
Total Liabilities and Stockholders' Equity	\$ 138,156,437	\$ 137,704,573

See accompanying notes and independent accountant's report

FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME
Years Ended December 31, 2015 and 2014

	(Reviewed)	
	2015	2014
Interest Income		
Interest and fees on loans	\$ 3,629,965	\$ 3,075,451
Interest on investment securities	485,295	572,410
Interest on federal funds sold	1,489	1,667
Interest on deposits with banks	368,508	386,835
	<u>4,485,257</u>	<u>4,036,363</u>
Interest Expense		
Interest on deposits	364,510	360,778
Interest on borrowed funds	301,050	77,443
	<u>665,560</u>	<u>438,221</u>
Total Interest Expense	665,560	438,221
Net Interest Income	3,819,697	3,598,142
Provision (Credit) for Loan Losses	<u>55,310</u>	<u>(47,608)</u>
Net Interest Income after Provision (Credit) for Loan Losses	<u>3,764,387</u>	<u>3,645,750</u>
Other Income		
Service charges on deposit accounts	166,458	184,312
Other service charges and fees	136,422	138,532
Other income	120	6,884
	<u>303,000</u>	<u>329,728</u>
Total Other Income	303,000	329,728
Other Expenses		
Salaries and employee benefits	1,777,190	1,736,287
Occupancy expenses	210,055	170,765
Other expenses	835,279	830,535
	<u>2,822,524</u>	<u>2,737,587</u>
Total Other Expenses	2,822,524	2,737,587
Net Income	<u>\$ 1,244,863</u>	<u>\$ 1,237,891</u>

See accompanying notes and independent accountant's report



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
Years Ended December 31, 2015 and 2014

	(Reviewed) 2015	2014
Net income	\$ 1,244,863	\$ 1,237,891
Other comprehensive income:		
Securities available for sale:		
Unrealized holding gains (losses) on investment securities available for sale arising during the period	<u>23,079</u>	<u>(59,908)</u>
Total securities available for sale adjustments	<u>23,079</u>	<u>(59,908)</u>
Pension plan adjustments:		
Amortization of net transition obligation	65,032	65,032
Recognized net actuarial loss	136,493	77,732
Unrecognized net actuarial gains (losses)	<u>(553,104)</u>	<u>(570,345)</u>
Total pension plan adjustments	<u>(351,579)</u>	<u>(427,581)</u>
Net other comprehensive income (loss)	<u>(328,500)</u>	<u>(487,489)</u>
Net comprehensive income	<u><u>\$ 916,363</u></u>	<u><u>\$ 750,402</u></u>

See accompanying notes and independent accountant's report



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
Years Ended December 31, 2015 and 2014

	Preferred Stock	Common Stock	Additional Paid - In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders' Equity
Balance at December 31, 2013 (Reviewed)	\$ -	\$ 200,000	\$ 7,315,786	\$ 8,076,979	\$ (1,331,980)	\$ (4,403,501)	\$ 9,857,284
Net income for 2014	-	-	-	1,237,891	-	-	1,237,891
Other comprehensive income (loss)	-	-	-	-	(487,489)	-	(487,489)
Total comprehensive income	-	-	-	-	(487,489)	-	750,402
Distributions paid or declared	-	-	-	(999,353)	-	-	(999,353)
Balance at December 31, 2014	-	200,000	7,315,786	8,315,517	(1,819,469)	(4,403,501)	9,608,333
Net income for 2015	-	-	-	1,244,863	-	-	1,244,863
Other comprehensive income (loss)	-	-	-	-	(328,500)	-	(328,500)
Total comprehensive income	-	-	-	-	(328,500)	-	916,363
Distributions paid or declared	-	-	-	(999,350)	-	-	(999,350)
Balance at December 31, 2015 (Reviewed)	\$ -	\$ 200,000	\$ 7,315,786	\$ 8,561,030	\$ (2,147,969)	\$ (4,403,501)	\$ 9,525,346

See accompanying notes and independent accountant's report

FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31, 2015 and 2014

	(Reviewed) 2015	2014
Cash Flows from Operating Activities		
Net income	\$ 1,244,863	\$ 1,237,891
Adjustments to reconcile net income to net cash provided by (used for) operating activities:		
Depreciation	80,279	82,536
Provision (credit) for loan losses	55,310	(47,607)
(Gain) loss on disposal of assets	11,976	-
Pension contributions	(264,000)	(306,376)
Pension expense, net	281,784	244,445
Amortization (accretion) on investment securities, net	155,911	252,502
(Increase) decrease in accrued interest receivable	(176,523)	(33,230)
(Increase) decrease in other assets	(46,267)	26,358
Increase (decrease) in accrued liabilities	(22,312)	23,617
Net cash provided by operating activities	<u>1,321,021</u>	<u>1,480,136</u>
Cash Flows from Investing Activities		
Sales and maturities of investment securities	33,700,271	37,195,391
Purchases of investment securities	(30,999,977)	(36,879,012)
Purchases (sales) of restricted stock	8,000	(205,500)
(Increase) decrease in federal funds sold	(765,000)	1,000,000
(Increase) decrease in loans, net	5,087,718	(15,700,179)
(Increase) decrease in interest-bearing deposits with other banks	(7,962,174)	1,070,168
Purchases of equipment	(57,537)	(83,028)
Net cash used for investing activities	<u>(988,699)</u>	<u>(13,602,160)</u>
Cash Flows from Financing Activities		
Increase (decrease) in demand deposits, net	4,109,216	1,506,657
Increase (decrease) in savings deposits, net	(157,915)	1,192,031
Increase (decrease) in time deposits, net	(489,646)	(1,958,379)
Advances on other borrowed funds	(781,600)	18,308,030
Payments on other borrowed funds	122,745	(9,253,024)
(Increase) decrease in federal funds purchased	(2,615,000)	2,615,000
Dividends paid on common stock	(999,350)	(999,352)
Net cash provided by (used for) financing activities	<u>(811,550)</u>	<u>11,410,963</u>
Net Change in Cash and Due From Banks	<u>(479,228)</u>	<u>(711,061)</u>
Cash and Due From Banks, Beginning of Year	<u>3,342,101</u>	<u>4,053,162</u>
Cash and Due From Banks, End of Year	<u>\$ 2,862,873</u>	<u>\$ 3,342,101</u>
Supplemental Disclosure of Cash Flow Information		
Interest paid	<u>\$ 667,145</u>	<u>\$ 442,399</u>

See accompanying notes and independent accountant's report



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2015 and 2014

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Business

First State Bankshares, Inc. (the Company) is a single-bank holding company, which owns 100% of First State Bankshares of Delaware, Inc., which owns 100% of First State Bank. First State Bank (the Bank) is a commercial bank with operations primarily in Spearman, Texas. The Bank provides retail, mortgage and commercial loans, deposits, ATM and asset management services (trust), principally to customers in the northeastern panhandle of Texas. The Bank is subject to regulation by certain federal and state agencies and undergoes periodic examination by those regulatory authorities. Assets of trust accounts administered by the Bank are not assets of the Bank and are not included in these financial statements.

Principles of Consolidation

The financial statements of First State Bankshares, Inc., together with its intermediate subsidiary First State Bankshares of Delaware, Inc., and its subsidiary First State Bank, are presented on a consolidated basis. All significant intercompany accounts and transactions have been eliminated.

Basis of Financial Statement Presentation and Use of Accounting Estimates

The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America and general industry practices. In preparing the accompanying consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenue and expenses for the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and fair value of financial instruments.

Comprehensive Income

The Company reports comprehensive income under FASB Accounting Standards Codification (ASC) Topic 220-10 *Comprehensive Income*, which establishes the rules for reporting and display of comprehensive income and its components, but has no effect on the Company's net income or total stockholders' equity for regulatory capital purposes. It requires unrealized gains and losses on the Company's available for sale securities and unrecognized prior service cost on post-retirement benefits to be included in accumulated other comprehensive income.

Cash, Due From Banks and Cash Flows

For purposes of reporting cash flows, cash and due from banks includes cash on hand and amounts due from banks (including cash items in process of clearing). Cash flows from loans, deposits and federal funds purchased and sold are reported net.

Due to the nature of the Company's operations, amounts are maintained in correspondent bank accounts, which often exceed federally insured limits. No losses have been experienced or are anticipated in such accounts.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2015 and 2014

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investment Securities Available for Sale

Securities classified as available for sale are debt securities that the Company intends to hold for an indefinite period of time, but not necessarily to maturity, and marketable equity securities. Any decision to sell a security classified as available for sale would be based on various factors, including significant liquidity needs, regulatory capital considerations, and other similar factors.

Securities available for sale are reported at fair value with unrealized gains or losses reported as a separate component of other comprehensive income. The amortization of premiums and accretion of discounts, computed by the interest method over their estimated lives, are recognized in interest income.

Realized gains or losses, determined on the basis of the cost of specific securities sold, are included in income. Declines in the fair value of individual securities classified as either held to maturity or available for sale below their amortized cost that are determined to be other-than-temporary, result in write-downs of the individual securities to their fair value with the resulting write-downs included in current earnings.

Loans

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are stated at the amount of unpaid principal, reduced by deferred loan fees and the allowance for loan losses. Interest on loans is accrued based on interest rates applied to the principal amounts outstanding.

Loans are placed on nonaccrual status when management believes that the borrower's financial condition, after giving consideration to economic and business conditions and collection efforts, is such that collection of interest is doubtful. All interest accrued but not collected for loans that are placed on nonaccrual status or charged off loans is reversed against interest income. The interest collected on these loans is accounted for on the cash-basis or cost-recovery method, until the loans qualify for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. Loans are charged off against the allowance for loan losses when management believes that the collectability of the principal is unlikely.

Allowance for Loan Losses

The allowance for loan losses is established by provisions charged to expense and is reduced by charge-offs, net of recoveries. Management determines the adequacy of the allowance based upon reviews of individual credits, recent loss experience, current economic conditions and the risk characteristics of the various categories of loans and other pertinent factors. The allowance for loan losses is evaluated on a regular basis by management and includes both specific and general components. The specific component relates to loans that are considered impaired. The general component covers both classified and non-classified loans and is also based on historical loss experience.

A loan is impaired when it is probable the creditor will be unable to meet all contractual principal and interest payments due in accordance with the terms of the loan agreement. Impairment is generally measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent or in foreclosure, as required by ASC Topic 310-10-35-4, *Loan Impairment*. The amount of impairment, if any, and any subsequent changes are included in the allowance for loan losses, as specific reserves.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2015 and 2014

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization computed on the straight-line method over the estimated useful lives of the properties, generally ranging as follows:

Building (including components)	10 to 20 years
Equipment	3 to 10 years
Bank automobiles	5 to 10 years

Other Real Estate

Other real estate represents properties acquired through foreclosure or other proceedings. All acquisitions are held for sale and are carried at the lower of cost or fair value, minus estimated costs to sell. Any reduction in carrying amount is charged to the reserve for loan losses.

Significant property is appraised as determined necessary by management to ensure that the value reflected on the financial statements is not in excess of the current fair value. Valuation allowances are recorded as necessary to reduce the carrying amount to fair value less estimated disposal costs.

Income Taxes

The Company and its subsidiary, with the consent of its stockholders, have elected to be taxed under sections of federal income tax law, which provide that, in lieu of corporation Federal income taxes, the stockholders separately account for their pro rata shares of the Company's items of income, deductions, losses, and credits.

The Company complies with ASC Topic 740-10 which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements, and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Management evaluated the Company's tax positions and concluded that the Company had taken no uncertain tax positions that require adjustment to the consolidated financial statements to comply with the provisions of this guidance. With few exceptions, the Company is no longer subject to income tax examinations by the U.S. federal, state or local tax authorities for years before 2012.

Advertising Costs

It is the policy of the Company to expense advertising costs as incurred. Advertising expense charged to operations for the years ended December 31, 2015 and 2014 was approximately \$36,000 and \$37,000, respectively.

Subsequent Events

Subsequent events were evaluated through April 8, 2016, which is the date the financial statements were available to be issued. There are no material subsequent events reported through this date.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Recent Accounting Pronouncements

ASU 2016-01, *“Financial Instruments (Subtopic 825-10) – Recognition and Measurement of Financial Assets and Financial Liabilities”* ASU 2016-1, among other things, (1) requires equity investments, with certain exceptions, to be measured at fair value with changes in fair value recognized in net income, (2) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment, and (3) eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities. ASU 2016-1 generally will be effective for the Company on January 1, 2018. However, certain provisions are available for early adoption. The provision eliminating certain disclosure requirements for financial instruments measured at amortized cost was early-adopted by the Company effective January 1, 2016, was applied retrospectively, and eliminated previously presented disclosures of fair values for financial instruments measured at amortized cost.

ASU 2015-01, *“Income Statement – Extraordinary and Unusual Items (Subtopic 225-20) – Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items.”* ASU 2015-01 eliminates from GAAP the concept of extraordinary items, which, among other things, required an entity to segregate extraordinary items considered to be unusual and infrequent from the results of ordinary operations and show the item separately in the income statement, net of tax, after income from continuing operations. ASU 2015-01 is effective for the Company beginning January 1, 2016, though early adoption is permitted. ASU 2015-01 is not expected to have a significant impact on the Company’s financial statements.

ASU 2015-02, *“Consolidation (Topic 810) – Amendments to the Consolidation Analysis.”* ASU 2015-02 implements changes to both the variable interest consolidation model and the voting interest consolidation model. ASU 2015-02 (1) eliminates certain criteria that must be met when determining when fees paid to a decision maker or service provider do not represent a variable interest, (2) amends the criteria for determining whether a limited partnership is a variable interest entity and (3) eliminates the presumption that a general partner controls a limited partnership in the voting model. ASU 2015-02 will be effective for the Company on January 1, 2016 and is not expected to have a significant impact on the Company’s financial statements.

NOTE 2 - RESTRICTIONS ON CASH AND DUE FROM BANKS

The Bank is required to maintain reserve balances in cash or on deposit with the Federal Reserve Bank, based on a percentage of deposits. The total of those reserve balances was approximately \$949,000 and \$1,091,000 at December 31, 2015 and 2014, respectively.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 3 - INVESTMENT SECURITIES AVAILABLE FOR SALE

Amortized cost and fair value of securities available for sale are summarized as follows:

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
As of December 31, 2015				
U.S. Agency securities	\$ 6,180,460	\$ -	\$ 30,300	\$ 6,150,160
Municipal debt securities	11,589,108	256,659	18,638	11,827,129
U.S. Treasury	9,931,120	74,540	-	10,005,660
Other securities	<u>4,000</u>	<u>7,722</u>	<u>-</u>	<u>11,722</u>
Totals	<u>\$ 27,704,688</u>	<u>\$ 338,921</u>	<u>\$ 48,938</u>	<u>\$ 27,994,671</u>
As of December 31, 2014				
U.S. Agency securities	\$ 8,252,160	\$ 1,820	\$ 66,760	\$ 8,187,220
Municipal debt securities	12,381,341	336,846	64,902	12,653,285
Mortgage-backed securities	20,162	-	102	20,060
U.S. Treasury	9,903,230	53,290	-	9,956,520
Other securities	<u>4,000</u>	<u>6,712</u>	<u>-</u>	<u>10,712</u>
Totals	<u>\$ 30,560,893</u>	<u>\$ 398,668</u>	<u>\$ 131,764</u>	<u>\$ 30,827,797</u>

The following table presents contractual maturity information for securities available for sale at December 31, 2015. Expected maturities may differ from contractual maturities because borrowers have the right to call or prepay obligations with or without penalties:

	Amortized Cost	Percentage of Amortized Cost	Fair Value
Less than one year	\$ 1,848,406	7%	\$ 1,855,452
One to five years	25,473,485	92	25,731,772
After five years	<u>378,797</u>	<u>1</u>	<u>395,725</u>
	27,700,688	100%	27,982,949
Other equity securities	<u>4,000</u>	<u>-</u>	<u>11,722</u>
Total securities available for sale	<u>\$ 27,704,688</u>	<u>100%</u>	<u>\$ 27,994,671</u>



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 3 - INVESTMENT SECURITIES AVAILABLE FOR SALE (continued)

Unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous loss position, as of December 31, 2015 and 2014, respectively are summarized as follows:

	Continuous Unrealized Losses Existing for Less Than 12 Months		Continuous Unrealized Losses Existing for Greater Than 12 Months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
As of December 31, 2015				
U.S. agency securities	\$ 6,150,160	\$ 30,300	\$ -	\$ -
Municipal debt securities	<u>575,278</u>	<u>6</u>	<u>2,422,035</u>	<u>18,633</u>
Totals	<u>\$ 6,725,438</u>	<u>\$ 30,306</u>	<u>\$ 2,422,035</u>	<u>\$ 18,633</u>
As of December 31, 2014				
U.S. Agency securities	\$ 1,988,840	\$ 8,140	\$ 4,196,560	\$ 58,620
Municipal debt securities	834,575	683	3,527,415	64,220
Mortgage-backed securities	<u>-</u>	<u>-</u>	<u>20,060</u>	<u>101</u>
Totals	<u>\$ 2,823,415</u>	<u>\$ 8,823</u>	<u>\$ 7,744,035</u>	<u>\$ 122,941</u>

The Company did not record any unrealized losses shown above as other-than-temporary impairment, as management believes they were primarily attributable only to changes in market interest rates and temporary market conditions. Investment securities with unrealized losses are evaluated by management to determine if any impairment is other than temporary, requiring a write-down to fair value. Management considers the percentage loss on a security, duration of loss, average life of the security, credit rating and payment performance when evaluating securities for losses other than temporary. The Bank has the ability and intent to hold securities available for sale for a period of time sufficient for a recovery of cost.

Securities available for sale with a fair value of approximately \$10,252,000 as of December 31, 2015 were pledged to secure public deposits and for other purposes required and permitted by law.

NOTE 4 - INVESTMENTS IN RESTRICTED STOCK

Non-marketable equity investments consist of non-controlling restricted common stock investments in the Independent Bankers Financial Corporation (IBFC) and in the Federal Home Loan Bank (FHLB). No ready market exists for these securities and these investments have no quoted market values. These investments are carried at historical cost which does not exceed estimated net realizable value, as follows at December 31:

Investee	Type of Interest	2015	2014
IBFC	Common stock	\$ 75,000	\$ 75,000
FHLB	Common stock	<u>296,600</u>	<u>304,600</u>
Total investments in restricted stock		<u>\$ 371,600</u>	<u>\$ 379,600</u>



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 5 - LOANS

Major classifications of loans, most of which originate in Spearman, Texas and the surrounding area, are as follows at December 31:

	2015	2014
<u>Commercial Real Estate:</u>		
Commercial agriculture	\$ 7,779,373	\$ 6,080,484
Commercial non-agriculture	5,181,421	4,208,773
Commercial construction	3,410,041	5,180,630
	<u>16,370,835</u>	<u>15,469,887</u>
<u>Consumer Real Estate:</u>		
Home equity	175,542	85,713
1-4 family residential mortgages	1,957,764	3,006,552
	<u>2,133,306</u>	<u>3,092,265</u>
<u>Commercial and Industrial:</u>		
Agriculture	42,320,506	44,800,227
Non-Agriculture	11,002,036	12,760,885
	<u>53,322,542</u>	<u>57,561,112</u>
<u>Consumer and Other</u>	<u>2,053,268</u>	<u>2,843,656</u>
Totals	<u>\$ 73,879,951</u>	<u>\$ 78,966,920</u>

The Bank has certain lending policies and procedures in place that are designed to maximize loan income within an acceptable level of risk. Management reviews and approves these policies and procedures on a regular basis. A reporting system supplements the review process by providing management with frequent reports related to loan production, loan quality, concentrations of credit, loan delinquencies and non-performing and potential problem loans. Diversification in the loan portfolio is a means of managing risk associated with fluctuations in economic conditions.

Commercial Real Estate Loans

Loans in the commercial real estate portfolio are generally secured by a first lien on improved real estate, including farm land and improved business properties. The Bank requires equity in the collateral position being taken with a general standard of advancing no more than 75% of value. Term financing is generally equated to the expected life of the asset. Real estate term loans are generally considered on a 15-20 year amortization with call provisions not to extend over 5 years. Collateral values are supported by real estate appraisals. Creditworthiness is determined by considering the character, experience, management and financial strength of the borrower, and the ability of the property to generate adequate funds to cover both operating expenses and debt service.

Consumer Real Estate Loans

Loans in the consumer real estate portfolio are generally collateralized by properties located in the Bank's market area and generally have fixed rates of interest, and require monthly payments. The Bank requires equity in the collateral position of 80% of the appraised value. The Bank generally does not escrow, but requires the borrower to have adequate casualty insurance and proof of paid taxes.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 5 - LOANS (continued)

Commercial and Industrial Loans

Loans in the commercial and industrial portfolio are made to all types of business for a variety of purposes, including a significant number of loans to agricultural borrowers. The terms of these loans are generally for less than five years and carry variable interest rates. The overall strength of the borrower is evaluated through the credit underwriting process which includes a variety of analytical activities including the review of historical and projected cash flows, historical financial performance, financial strength of the principals and guarantors, assessment of management skills and establishing collateral values. Most commercial and industrial loans are secured by the assets being financed or other business assets such as inventory or receivables.

Consumer and Other Loans

Loans in the consumer portfolio consist primarily of automobile loans, overdraft loans, loans secured by deposits and securities, and unsecured personal loans. The Bank's procedures for underwriting consumer loans include an assessment of the borrower's credit history and ability to meet other existing debt obligations, as well as payments of principal and interest on the proposed loans. The borrower's creditworthiness is the primary consideration, and is generally assessed through reviewing work history, obtaining credit agency reports, and review of financial statements.

Non-Accrual and Past Due Loans

Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due. Loans are placed on non-accrual status when, in management's opinion, the borrower may be unable to meet payment obligations as they become due, as well as when required by regulatory provisions. Loans may be placed on non-accrual status regardless of whether or not such loans are considered past due. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received in excess of principal due. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

There were no non-accrual loans at December 31, 2015 and 2014.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 5 - LOANS (continued)

An age analysis of past due loans segregated by class of loans, as of December 31, 2015 is as follows:

	30-89	Greater Than 90	Total Past Due	Current	Total Loans	90 Days Past Due Accruing
<u>Commercial Real Estate:</u>						
Commercial agriculture	\$ -	\$ -	\$ -	\$ 7,779,373	\$ 7,779,373	\$ -
Commercial non-agriculture	-	-	-	5,181,421	5,181,421	-
Commercial construction	-	-	-	3,410,041	3,410,041	-
	-	-	-	16,370,835	16,370,835	-
<u>Consumer Real Estate:</u>						
Home equity	-	-	-	175,542	175,542	-
1-4 family residential mortgages	-	-	-	1,957,764	1,957,764	-
	-	-	-	2,133,306	2,133,306	-
<u>Commercial and Industrial:</u>						
Agriculture	205,411	-	205,411	42,115,095	42,320,506	-
Non-Agriculture	59,132	-	59,132	10,942,904	11,002,036	-
	264,543	-	264,543	53,057,999	53,322,542	-
<u>Consumer and Other</u>						
	4,241	-	4,241	2,049,027	2,053,268	-
Totals	\$ 268,784	\$ -	\$ 268,784	\$ 73,611,167	73,879,951	\$ -

An age analysis of past due loans segregated by class of loans, as of December 31, 2014 is as follows:

	30-89	Greater Than 90	Total Past Due	Current	Total Loans	90 Days Past Due Accruing
<u>Commercial Real Estate:</u>						
Commercial agriculture	\$ -	\$ -	\$ -	\$ 6,080,484	\$ 6,080,484	\$ -
Commercial non-agriculture	-	-	-	4,208,773	4,208,773	-
Commercial construction	-	-	-	5,180,630	5,180,630	-
	-	-	-	15,469,887	15,469,887	-
<u>Consumer Real Estate:</u>						
Home equity	-	-	-	85,713	85,713	-
1-4 family residential mortgages	-	-	-	3,006,552	3,006,552	-
	-	-	-	3,092,265	3,092,265	-
<u>Commercial and Industrial:</u>						
Agriculture	-	-	-	44,800,227	44,800,227	-
Non-Agriculture	-	-	-	12,760,885	12,760,885	-
	-	-	-	57,561,112	57,561,112	-
<u>Consumer and Other</u>						
	24,123	-	24,123	2,819,533	2,843,656	-
Totals	\$ 24,123	\$ -	\$ 24,123	\$ 78,942,797	\$ 78,966,920	\$ -



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 5 - LOANS (continued)

Impaired Loans

Loans are considered impaired when, based on current financial information and events, it is probable the Bank will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. Impairment is evaluated on an individual basis for all loans. If a loan is impaired, a specific valuation allowance is allocated, if necessary, so that the loan is reported net, at the present value of estimated future cash flows using the loan's existing rate, or at the fair value of the collateral if repayment is expected solely from the collateral. Interest payments on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case interest is recognized on a cash basis. Impaired loans, or portions thereof, are charged off when deemed uncollectible.

At December 31, 2015, the following loans were classified as troubled debt restructurings:

	Number of Loans	Balance at Restructure	Balance at Year End
<u>Commercial Real Estate:</u>			
Commercial agriculture	-	\$ -	\$ -
Commercial non-agriculture	-	-	-
Commercial construction	-	-	-
<u>Consumer Real Estate:</u>			
Home equity	-	-	-
1-4 family residential mortgages	-	-	-
<u>Commercial and Industrial:</u>			
Agriculture	-	-	-
Non-agriculture	1	716,984	636,573
<u>Consumer and Other</u>	1	13,431	13,342
Totals	2	\$ 730,415	\$ 649,915

At December 31, 2014, there were no loans classified as troubled debt restructurings.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 5 - LOANS (continued)

Impaired loans as of December 31, 2015 and 2014 are included in the following tables:

	December 31, 2015					
	Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
<u>Commercial Real Estate:</u>						
Commercial agriculture	\$ 6,568	\$ 6,568	\$ -	\$ 6,568	\$ -	\$ 13,784
Commercial non-agriculture	143,097	143,097	-	143,097	-	81,407
Commercial construction	-	-	-	-	-	-
	149,665	149,665	-	149,665	-	95,191
<u>Consumer Real Estate:</u>						
Home equity	-	-	-	-	-	-
1-4 family residential mortgages	-	-	-	-	-	-
	-	-	-	-	-	-
<u>Commercial and Industrial:</u>						
Agriculture	492,113	492,113	-	492,113	-	247,675
Non-Agriculture	647,582	647,582	-	647,582	-	323,791
	1,139,695	1,139,695	-	1,139,695	-	571,466
<u>Consumer and Other</u>						
	13,342	13,342	-	13,342	-	18,560
	13,342	13,342	-	13,342	-	18,560
Totals	\$ 1,302,702	\$ 1,302,702	\$ -	\$ 1,302,702	\$ -	\$ 685,217



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 5 - LOANS (continued)

December 31, 2014

	Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
<u>Commercial Real Estate:</u>						
Commercial agriculture	\$ 20,999	\$ 20,999	\$ -	\$ 20,999	\$ -	\$ 29,117
Commercial non-agriculture	19,717	19,717	-	19,717	-	517,965
Commercial construction	-	-	-	-	-	-
	<u>40,716</u>	<u>40,716</u>	<u>-</u>	<u>40,716</u>	<u>-</u>	<u>547,082</u>
<u>Consumer Real Estate:</u>						
Home equity	-	-	-	-	-	-
1-4 family residential mortgages	-	-	-	-	-	-
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
<u>Commercial and Industrial:</u>						
Agriculture	3,237	3,237	-	3,237	-	71,619
Non-Agriculture	-	-	-	-	-	-
	<u>3,237</u>	<u>3,237</u>	<u>-</u>	<u>3,237</u>	<u>-</u>	<u>71,619</u>
<u>Consumer and Other</u>	<u>23,778</u>	<u>23,778</u>	<u>-</u>	<u>23,778</u>	<u>-</u>	<u>11,889</u>
Totals	<u>\$ 67,731</u>	<u>\$ 67,731</u>	<u>\$ -</u>	<u>\$ 67,731</u>	<u>\$ -</u>	<u>\$ 630,590</u>

As part of the on-going monitoring of the credit quality of the Bank's loan portfolio, management categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt and comply with various terms of their loan agreements. The Bank considers current financial information, historical payment experience, credit documentation, public information and current economic trends. Generally, all sizeable credits received a financial review no less than annually to monitor and adjust, if necessary, the credit's risk profile. For special mention, substandard and doubtful credit classifications, the frequency of review is increased to no less than quarterly in order to determine potential impact on credit loss estimates.

The Bank categorizes loans into the following risk categories based on relevant information about the ability of borrowers to service their debt:

Pass: A pass loan is one which represents a reasonable credit risk requiring no more than normal loan officer attention. There are no discernible significant problems present, and any unfavorable factors are more than offset by strengths.

Special Mention: Loans classified as special mention warrant more than the ordinary amount of attention but have not yet reached the point of concern for loss of liquidation of collateral. Loans in this category may be reaching the point where they would have difficulty in refinancing and show one or more of the following characteristics: high leverage, sporadic profitability, high susceptibility to economic change, declining liquidity, shortage of reliable information, and some ratios incompatible with industry norms.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014**

NOTE 5 - LOANS (continued)

Substandard: Loans classified as substandard are deteriorating situations exhibiting a number of well-defined weaknesses which bring normal repayment into jeopardy. The characteristics exhibited are one or more of the following: unprofitable or poor earnings trend, lack of liquidity, excessive debt, significant unfavorable industry comparisons, inappropriate loan structuring, secondary repayment source unavailable, and questionable prior loan repayment record.

Doubtful: Loans classified as doubtful exhibit the same weaknesses used to describe a Substandard credit; however, the traits are more pronounced. Loans in this classification are frozen, and collection in full is improbable. Loans in this category are not yet rated as Loss because certain actions may yet occur which would salvage the loan.

Loss: Loans classified as loss are considered uncollectible and are charged off against the allowance immediately.

The following table presents risk ratings, grouped by the five major categories described above, by class of loan, as of December 31, 2015:

	Pass	Special Mention	Substandard	Doubtful	Totals
<u>Commercial Real Estate:</u>					
Commercial agriculture	\$ 7,642,805	\$ 130,000	\$ 6,568	\$ -	\$ 7,779,373
Commercial non-agriculture	5,024,333	13,991	143,097	-	5,181,421
Commercial construction	3,410,041	-	-	-	3,410,041
	<hr/> 16,077,179	<hr/> 143,991	<hr/> 149,665	<hr/> -	<hr/> 16,370,835
<u>Consumer Real Estate:</u>					
Home equity	175,542	-	-	-	175,542
1-4 family residential mortgages	1,957,764	-	-	-	1,957,764
	<hr/> 2,133,306	<hr/> -	<hr/> -	<hr/> -	<hr/> 2,133,306
<u>Commercial and Industrial:</u>					
Agriculture	40,904,745	923,648	492,113	-	42,320,506
Non-Agriculture	10,354,454	-	647,582	-	11,002,036
	<hr/> 51,259,199	<hr/> 923,648	<hr/> 1,139,695	<hr/> -	<hr/> 53,322,542
<u>Consumer and Other</u>	<hr/> 2,022,351	<hr/> 17,575	<hr/> 13,342	<hr/> -	<hr/> 2,053,268
 Totals	 <hr/> \$ 71,492,035	 <hr/> \$ 1,085,214	 <hr/> \$ 1,302,702	 <hr/> \$ -	 <hr/> \$ 73,879,951



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 5 - LOANS (continued)

The following table presents risk ratings, grouped by the five major categories described above, by class of loan, as of December 31, 2014:

	Pass	Special Mention	Substandard	Doubtful	Totals
<u>Commercial Real Estate:</u>					
Commercial agriculture	\$ 6,059,485	\$ -	\$ 20,999	\$ -	\$ 6,080,484
Commercial non-agriculture	4,189,056	-	19,717	-	4,208,773
Commercial construction	5,180,630	-	-	-	5,180,630
	<u>15,429,171</u>	<u>-</u>	<u>40,716</u>	<u>-</u>	<u>15,469,887</u>
<u>Consumer Real Estate:</u>					
Home equity	85,713	-	-	-	85,713
1-4 family residential mortgages	3,006,552	-	-	-	3,006,552
	<u>3,092,265</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>3,092,265</u>
<u>Commercial and Industrial:</u>					
Agriculture	44,725,008	71,982	3,237	-	44,800,227
Non-Agriculture	12,760,885	-	-	-	12,760,885
	<u>57,485,893</u>	<u>71,982</u>	<u>3,237</u>	<u>-</u>	<u>57,561,112</u>
<u>Consumer and Other</u>	<u>2,814,031</u>	<u>5,847</u>	<u>23,778</u>	<u>-</u>	<u>2,843,656</u>
Totals	<u>\$ 78,821,360</u>	<u>\$ 77,829</u>	<u>\$ 67,731</u>	<u>\$ -</u>	<u>\$ 78,966,920</u>

The allowance for loan losses (allowance) is an estimate of loan losses inherent in the Bank's loan portfolio. The allowance is established through a provision for loan losses which is charged to expense. Additions to the allowance are expected to maintain the adequacy of the total allowance after loan losses and loan growth. Loan losses are charged off against the allowance when the Bank determines the loan balance to be uncollectible. Consumer loan accounts are charged-off automatically based on regulatory requirements. Cash received on previously charged off amounts is recorded as a recovery to the allowance. The allowance consists of two primary components, general reserves and specific reserves related to impaired loans.

The general reserve component covers non-impaired loans and is based on historical losses adjusted for current factors. The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Bank over the most recent ten years. This actual loss experience is adjusted for certain portfolio trends and concentrations based on the risks present for each portfolio segment. Management evaluates the degree of risk that each one of these components has on the quality of the loan portfolio on a quarterly basis. These factors are inherently subjective and are driven by the repayment risk associated with each portfolio segment.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 5 - LOANS (continued)

The allowances established or probable losses on specific loans are based on a regular analysis and evaluation of problem loans. Loan officers and committees analyze the loan to determine whether the loan is impaired and, if impaired, the need to specifically allocate a portion of the allowance for possible loan losses to the loan. Specific valuation allowances are determined by analyzing the borrower's ability to repay amounts owed, collateral deficiencies, the relative risk grade of the loan and economic conditions affecting the borrower's industry, among other things.

Although management believes the allowance to be adequate, ultimate losses may vary from its estimates. At least quarterly, the Board of Directors reviews the adequacy of the allowance, including consideration of the relevant risks in the portfolio, current economic conditions and other factors. If the Board of Directors and management determine that changes are warranted based on those reviews, the allowance is adjusted. In addition, the Bank's primary regulator reviews the adequacy of the allowance, and may require additions to the allowance based on their judgment about information available at the time of their examination.

The following table details activity in the allowance for possible loan losses by portfolio segment for the years ended December 31, 2015 and 2014. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories. The following table also details the Bank's recorded investment in loans related to each balance in the allowance for loan losses by portfolio segment and is disaggregated on the basis of the Bank's impairment methodology:

December 31, 2015

	Commercial Real Estate	Consumer Real Estate	Commercial and Industrial	Consumer and Other	Totals
<u>Allowance for Loan Losses:</u>					
Beginning balance	\$ 206,904	\$ 3,509	\$ 411,429	\$ 23,786	\$ 645,628
Provision (credit) for possible loan losses	17,725	301	35,245	2,039	55,310
Charge-offs	(97)	-	-	-	(97)
Recoveries	846	-	-	-	846
Ending balance	<u>\$ 225,378</u>	<u>\$ 3,810</u>	<u>\$ 446,674</u>	<u>\$ 25,825</u>	<u>\$ 701,687</u>
Ending allowance on loans individually evaluated for impairment	\$ -	\$ -	\$ -	\$ -	\$ -
Ending allowance on loans collectively evaluated for impairment	<u>225,378</u>	<u>3,810</u>	<u>446,674</u>	<u>25,825</u>	<u>701,687</u>
Ending balance	<u>\$ 225,378</u>	<u>\$ 3,810</u>	<u>\$ 446,674</u>	<u>\$ 25,825</u>	<u>\$ 701,687</u>
<u>Loans and Leases:</u>					
Ending balance individually evaluated for impairment	\$ 293,657	\$ -	\$ 2,063,343	\$ 30,916	\$ 2,387,916
Ending balance collectively evaluated for impairment	<u>16,077,178</u>	<u>2,133,306</u>	<u>51,259,199</u>	<u>2,022,352</u>	<u>71,492,035</u>
Totals	<u>\$ 16,370,835</u>	<u>\$ 2,133,306</u>	<u>\$ 53,322,542</u>	<u>\$ 2,053,268</u>	<u>\$ 73,879,951</u>



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 5 - LOANS (continued)

	December 31, 2014				
	Commercial Real Estate	Consumer Real Estate	Commercial and Industrial	Consumer and Other	Totals
<u>Allowance for Credit Losses:</u>					
Beginning balance	\$ 127,234	\$ 3,810	\$ 446,663	\$ 25,822	\$ 603,529
Provision (credit) for possible loan losses	(10,037)	(301)	(35,234)	(2,036)	(47,608)
Charge-offs	(2,613)	-	-	-	(2,613)
Recoveries	92,320	-	-	-	92,320
Ending balance	<u>\$ 206,904</u>	<u>\$ 3,509</u>	<u>\$ 411,429</u>	<u>\$ 23,786</u>	<u>\$ 645,628</u>
Ending allowance on loans individually evaluated for impairment	\$ -	\$ -	\$ -	\$ -	\$ -
Ending allowance on loans collectively evaluated for impairment	<u>206,904</u>	<u>3,509</u>	<u>411,429</u>	<u>23,786</u>	<u>645,628</u>
Ending balance	<u>\$ 206,904</u>	<u>\$ 3,509</u>	<u>\$ 411,429</u>	<u>\$ 23,786</u>	<u>\$ 645,628</u>
<u>Loans and Leases:</u>					
Ending balance individually evaluated for impairment	\$ 40,716	\$ -	\$ 75,219	\$ 29,625	\$ 145,560
Ending balance collectively evaluated for impairment	<u>15,429,171</u>	<u>3,092,265</u>	<u>57,485,893</u>	<u>2,814,031</u>	<u>78,821,360</u>
Totals	<u>\$ 15,469,887</u>	<u>\$ 3,092,265</u>	<u>\$ 57,561,112</u>	<u>\$ 2,843,656</u>	<u>\$ 78,966,920</u>

NOTE 6 - PREMISES AND EQUIPMENT

Major classifications of premises and equipment are summarized as follows at December 31:

	2015	2014
Land	\$ 100,000	\$ 100,000
Buildings	1,310,561	1,310,561
Aircraft	732,714	728,554
Equipment	<u>759,916</u>	<u>784,800</u>
Total premises and equipment	2,903,191	2,923,915
Less accumulated depreciation	<u>(2,508,251)</u>	<u>(2,494,257)</u>
Premises and equipment, net	<u>\$ 394,940</u>	<u>\$ 429,658</u>

Depreciation and amortization of premises and equipment recognized during 2015 and 2014 was approximately \$80,000 and \$83,000, respectively.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 7 - DEPOSITS

At December 31, 2015 and 2014, overdraft demand deposits reclassified to loans totaled approximately \$13,000 and \$19,000, respectively.

At December 31, 2015, the scheduled maturities of certificates of deposit are as follows:

2016	\$ 35,352,676
2017	5,170,932
2018	<u>28,682</u>
	<u>\$ 40,552,290</u>

NOTE 8 - OTHER BORROWINGS

Other borrowings consist of the following at December 31:

	2015	2014
FHLB note payable	\$ 2,122,745	\$ 2,000,000
Related party note payable (stockholder)	140,000	140,000
Secured borrowings (LIFO Participations)	<u>8,306,423</u>	<u>9,088,023</u>
Totals	<u>\$ 10,569,168</u>	<u>\$ 11,228,023</u>

At December 31, 2015 under the FHLB advance credit agreement, the Bank had outstanding advances of approximately \$2,100,000. At December 31, 2015, the Bank had approximately \$18,483,000 of total available credit under the advance agreement with the Federal Home Loan Bank, secured by certain loans from the Bank's loan portfolio. The remaining net available credit to the Bank under this agreement was \$16,360,000 at December 31, 2015. The following is a summary of the promissory notes outstanding to the FHLB at December 31, 2015:

Note Date	08/31/2015	02/28/2015
Maturity Date	02/16/2016	03/01/2030
Interest Rate	0.44%	2.675%
Monthly Payments	\$ 864	\$ -

Scheduled maturities for the years ended December 31:

2016	\$ 10,369	\$ 2,000,000
2017	10,369	-
2018	10,369	-
2019	10,369	-
2020 and after	<u>81,269</u>	<u>-</u>
Totals	<u>\$ 122,745</u>	<u>\$ 2,000,000</u>



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 8 - OTHER BORROWINGS (continued)

Secured borrowings (LIFO participation) consist of loan participations that were purchased from the Bank by a related party bank director and shareholder, and other banks. The terms of the participation agreements require payments to be allocated to participants on a last-in-first-out basis which does not allow for sale treatment under ASC Topic 860-10 *Transfers and Servicing of Financial Assets*. The underlying securities are commercial loans secured by farmland, with a total original participated balance of approximately \$11,050,000, interest rates from 4.75% to 6.00%, and maturity dates in October 2016 (\$6,264,234) and November 2016 (\$2,042,188). The outstanding participated balance at December 31, 2015 and 2014 was approximately \$8,306,000 and \$9,088,000, respectively.

First State Bankshares of Delaware, Inc, at December 31, 2015 and 2014, had an outstanding note payable due to a stockholder of \$140,000. This note is unsecured, and has a 2.0% interest rate, with a maturity date of December 2016, and annual interest payments.

Also at December 31, 2015, the Bank had available various federal fund credit lines of approximately \$9,000,000 with various other institutions. These lines include variable interest rates, funding limitations, and approval conditions by each individual institution.

NOTE 9 - RETIREMENT PLANS

The Bank sponsors a noncontributory defined benefit pension plan, whose participants are entitled to an annual benefit upon retirement based upon a participant's highest three year average compensation. The maximum annual benefit is reduced for participants who have less than 10 years of service. Effective January 18, 2008, the Plan was frozen to new participants and benefit accrual. No employees have become eligible to participate in the Plan since that date.

Under most circumstances employees are vested after five years of service. Benefits are payable monthly commencing on the latter of age 65 or the participant's date of retirement.

Contributions to the pension plan fund are sufficient to finance the plan on a sound actuarial basis, as determined by the Board of Directors. The following table sets forth the estimated funded status of the plan at December 31, based upon an independent actuarial valuation of the benefit obligation as of the end of year:

	2015	2014
Fair value of plan assets	\$ 3,857,535	\$ 3,641,920
Projected Benefit obligation	<u>5,960,990</u>	<u>5,376,010</u>
Funded (Under-Funded) Status	<u>\$ (2,103,455)</u>	<u>\$ (1,734,090)</u>

Significant assumptions used in the accounting for net pension expense at December 31 were:

	2015	2014
Discount rate	4.10%	4.00%
Expected return on plan assets	6.00%	6.00%
Rate of compensation increase	0.00%	0.00%



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 9 - RETIREMENT PLANS (continued)

Change in plan assets were as follows for the years ended December 31:

	2015	2014
Fair value of plan assets at beginning of year	\$ 3,641,920	\$ 3,346,247
Employer contributions	264,000	306,376
Actual return on plan assets	88,932	96,376
Benefits paid	<u>(137,317)</u>	<u>(107,079)</u>
Fair Value of Plan Assets at End of Year	<u>\$ 3,857,535</u>	<u>\$ 3,641,920</u>

The Bank complies with the fair value guidance requiring disclosures of the fair value measurement for pension plan assets. In accordance with this guidance, the Bank categorizes Plan assets within the fair value hierarchy. Following is a description of the valuation methodologies used for assets measured and reported at fair value.

Cash and Cash Equivalents

For these short-term instruments, the carrying value is a reasonable estimate of fair value.

Fixed Income Securities

These investments consist of U.S. Agency mortgage backed obligations, all of which are primarily brokered and priced based on observable market based inputs or unobservable inputs that are corroborated by market data.

Real Estate Notes Receivable

For variable interest rate loans that re-price frequently and with no significant change in credit risk, fair values are based on carrying values.

The following table sets forth by level within the fair value hierarchy, pension plan assets at their fair values, as of December 31:

Asset Class	December 31, 2015			
	Fair Value Measurements Using			
	Total	Level 1	Level 2	Level 3
Cash and cash equivalents	\$ 496,855	\$ 496,855	\$ -	\$ -
Mortgage backed securities	1,691,477	-	1,691,477	-
Real estate notes receivable	<u>1,669,203</u>	<u>-</u>	<u>-</u>	<u>1,669,203</u>
Total	<u>\$ 3,857,535</u>	<u>\$ 496,855</u>	<u>\$ 1,691,477</u>	<u>\$ 1,669,203</u>



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 9 - RETIREMENT PLANS (continued)

Asset Class	December 31, 2014			
	Fair Value Measurements Using			
	Total	Level 1	Level 2	Level 3
Cash and cash equivalents	\$ 1,935,304	\$ 1,935,304	\$ -	\$ -
Real estate notes receivable	1,706,616	-	-	1,706,616
Total	<u>\$ 3,641,920</u>	<u>\$ 1,935,304</u>	<u>\$ -</u>	<u>\$ 1,706,616</u>

Level 3 Gains and Losses

The table below sets forth a summary of changes in the fair value of the plan's level 3 assets for the year ended December 31, 2015 and 2014.

	2015	2014
Real Estate Loans		
Balance, beginning of year	\$ 1,706,616	\$ 2,056,182
Principal repayments	(37,413)	(349,566)
Purchase of loans	-	-
Balance, year end	<u>\$ 1,669,203</u>	<u>\$ 1,706,616</u>

A summary of changes in benefit obligations during the year ended December 31 is as follows:

	2015	2014
Obligations at beginning of year	\$ 5,376,010	\$ 4,714,687
Service cost	90,281	87,032
Interest on projected benefit obligation	212,294	221,405
Actuarial gain (loss)	419,721	459,965
Benefits paid	(137,316)	(107,079)
Benefit obligation at end of year	<u>\$ 5,960,990</u>	<u>\$ 5,376,010</u>

Amounts recognized in the balance sheet at December 31 are as follows:

	2015	2014
Projected benefit obligation	\$ 5,960,990	\$ 5,376,010
Less: fair value of plan assets	<u>3,857,535</u>	<u>3,641,920</u>
Over (Under) funded status of Plan	(2,103,455)	(1,734,090)
Accrued (prepaid) benefit costs	<u>(334,497)</u>	<u>(352,281)</u>
Accumulated Other Comprehensive Income (Loss)	<u>\$ (2,437,952)</u>	<u>\$ (2,086,371)</u>

The basis used to determine the overall expected long-term return on plan assets was based on the composition of plan assets and a consensus of estimates from similarly managed portfolios of expected future returns.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 9 - RETIREMENT PLANS (continued)

The Plan's investment strategy is principally to safeguard plan assets while also earning a reasonable rate of return. This is accomplished through investment in real estate notes, government backed securities, and insured bank deposits.

The Bank also maintains a defined contribution 401(k) plan, for the benefit of its employees. Under its provisions, eligible employees may contribute amounts (limited by IRC guidelines) of their annual compensation, with contributions being matched by the Bank at a rate of 100% of the employees' contributions up to 3%, plus 50% of employee contributions between 3% and 5%, up to a maximum of 5% of each employee's compensation, as defined. Participants are immediately vested in their salary deferral contributions and employer matching contributions. The Bank's employer contributions under this feature of the plan during 2015 and 2014 was approximately \$43,000 and \$44,000, respectively.

NOTE 10 - COMMON AND PREFERRED STOCKS

Each share of \$1.00 par value preferred stock of First State Bankshares, Inc. is entitled to one vote. Total authorized shares are 10,000,000, none of which were issued or outstanding at December 31, 2015 or 2014.

Each share of \$1.00 par value common stock of First State Bankshares, Inc. is entitled to one vote. Total authorized shares are 1,000,000, of which 200,000 shares were issued and outstanding at December 31, 2015 and 2014.

Each share of \$1.00 par value common stock of First State Bankshares of Delaware, Inc. is entitled to one vote. All 1,000 authorized shares were issued and outstanding at December 31, 2015 and 2014.

Each share of \$5.00 par value common stock of First State Bank of Spearman is entitled to one vote. All 200,000 authorized shares were issued and outstanding at December 31, 2015 and 2014.

NOTE 11 - OTHER COMPREHENSIVE INCOME

Balances of the components comprising accumulated other comprehensive income (loss), included in stockholders' equity, at December 31, 2015 and 2014, respectively, are as follows:

	Unrealized Gain/(Loss) on Securities	Defined Benefit Pension Plan	Accumulated Other Comprehensive Income
Balance at December 31, 2013	\$ 326,811	\$ (1,658,791)	\$ (1,331,980)
Change for 2014	<u>(59,908)</u>	<u>(427,581)</u>	<u>(487,489)</u>
Balance at December 31, 2014	266,903	(2,086,372)	(1,819,469)
Change for 2015	<u>23,079</u>	<u>(351,579)</u>	<u>(328,500)</u>
Balance at December 31, 2015	<u>\$ 289,982</u>	<u>\$ (2,437,951)</u>	<u>\$ (2,147,969)</u>



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 12 - COMMITMENTS, CONTINGENT LIABILITIES AND CONCENTRATIONS

In the normal course of business, the Bank makes various commitments, and incurs certain contingent liabilities, which are not reflected in the accompanying consolidated financial statements. Commitments include various guarantees, commitments to extend credit, and letters of credit. The Bank uses the same credit policies in making these commitments as it does for on-balance sheet instruments. The amount of collateral obtained, if deemed necessary, is based on management's credit evaluation. 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 exposure to credit loss in the event of nonperformance by the other parties to the commitments to extend credit is represented by the contractual amount. The Bank does not anticipate any material losses as a result of these transactions.

Commitments to extend credit amounted to approximately \$12,494,000 and \$12,929,000 as of December 31, 2015 and 2014, respectively.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of a letter of credit, is based on management's credit evaluation of the customer. Collateral held varies but may include certificates of deposit, accounts receivable and inventory. Standby letters of credit amounted to approximately \$528,000 and \$723,000 at December 31, 2015 and 2014, respectively.

The Bank has a concentration of funds on deposit at Amarillo National Bank and City Bank in Lubbock, Texas of approximately \$570,000 and \$1,300,000, respectively, at December 31, 2015.

Although the Bank's loan portfolio is diversified, there is a relationship in this region between the agricultural economies and the economic performance of loans made to nonagricultural customers. The Bank's lending policies for both agricultural and nonagricultural customers require loans to be well-collateralized and supported by cash flows. Loans to agricultural customers also often require margin requirements, periodic inspections, loan agreements and borrowing base certificates. Credit losses from loans related to the agricultural economies are consistent with credit losses experienced in the loan portfolio as a whole and are taken into consideration in the determination of the allowance for loan losses.

NOTE 13 - RELATED PARTY TRANSACTIONS

In the ordinary course of business, related parties, such as certain executive officers, directors and principal shareholders are also customers of the Bank, either personally or through corporations or firms of which they are officers or have an ownership interest. At December 31, 2015 and 2014, loans of approximately \$54,000 and \$73,000, respectively, were made directly and indirectly to related parties. Deposits from related parties held by the Bank at December 31, 2015 and 2014, amounted to approximately \$2,673,000 and \$2,153,000, respectively.



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014**

NOTE 14 - REGULATORY MATTERS

The Bank is subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Net unrealized gain or loss on available for sale securities, is not included in computing regulatory capital. Capital amounts and ratios for December 31, 2014 are calculated using Basel I rules. Management believes as of December 31, 2015, the Bank meets all capital adequacy requirements to which it is subject.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. At year-end 2015 and 2014, the most recent notification from the FDIC categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since the notification that management believes have changed the Bank's category.

The Bank's actual capital amounts and ratios are also presented in the table (in thousands):

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2015						
Common Tier I (to Risk-weighted Assets)	\$ 11,581	14.6%	\$ 3,572	4.5%	\$ 5,159	6.5%
Total Capital (to Risk-weighted Assets)	\$ 12,287	15.5%	\$ 6,350	8%	\$ 7,937	10%
Tier I Capital (to Risk-weighted Assets)	\$ 11,581	14.6%	\$ 3,175	6%	\$ 6,350	8%
Tier I Capital (to Average Assets)	\$ 11,581	8.5%	\$ 5,446	4%	\$ 6,808	5%
As of December 31, 2014						
Total Capital (to Risk-weighted Assets)	\$ 11,948	14.6%	\$ 6,559	8%	\$ 8,199	10%
Tier I Capital (to Risk-weighted Assets)	\$ 11,299	13.8%	\$ 3,280	4%	\$ 4,920	6%
Tier I Capital (to Average Assets)	\$ 11,299	8.7%	\$ 5,186	4%	\$ 6,483	5%



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 15 - FAIR VALUE DISCLOSURES

The FASB's authoritative guidance on fair value measurements establishes a framework for measuring fair value, and expands disclosure about fair value measurements. The guidance enables the reader of the financial statements to assess the inputs used to develop those measurements by establishing a hierarchy for ranking the quality and reliability of the information used to determine fair values. Under this guidance, assets and liabilities carried at fair value must be classified and disclosed in one of the following three categories:

Level 1: Quoted prices in active markets for identical assets and liabilities.

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are not corroborated by market data.

The following methods, assumptions, and valuation techniques were used by the Bank to measure different financial assets and liabilities at fair value and in estimating its fair value disclosures for financial instruments.

Investment securities available for sale

The Company obtains fair value measurements from an independent pricing service. The fair value measurement considers observable data that may include dealer quotes, market spreads, actual trade data, and credit information, among other things.

Because assumptions are inherently subjective in nature, the net realizable value could be materially different from the estimates presented below. Accordingly, the aggregate fair value amounts presented most certainly do not represent management's estimation of the underlying value of the Company.

In determining the appropriate levels, the Company performs a detailed analysis of the financial assets and liabilities that are subject to fair value disclosures. The following table summarizes the financial assets and liabilities measured at fair value on a recurring basis at December 31, 2015:

(in thousands)	Fair Value Measurements Using			
	Total	Level 1	Level 2	Level 3
Investment securities available for sale				
U.S. Agency Securities	\$ 6,150	\$ -	\$ 6,150	\$ -
Municipal debt securities	11,827	-	11,827	-
U.S. Treasury	10,006	10,006	-	-
Other securities	<u>12</u>	<u>-</u>	<u>12</u>	<u>-</u>
Totals	\$ <u>27,995</u>	\$ <u>10,006</u>	\$ <u>17,989</u>	\$ <u>-</u>



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2015 and 2014

NOTE 15 - FAIR VALUE DISCLOSURES (continued)

The following table summarizes the financial assets and liabilities measured at fair value on a recurring basis at December 31, 2014:

(in thousands)	Fair Value Measurements Using			
	Total	Level 1	Level 2	Level 3
Investment securities available for sale				
U.S. Agency Securities	\$ 8,187	\$ -	\$ 8,187	\$ -
Municipal debt securities	12,653	-	12,653	-
Mortgage-backed securities	20	-	20	-
U.S. Treasury	9,957	9,957	-	-
Other securities	<u>11</u>	<u>-</u>	<u>11</u>	<u>-</u>
Totals	\$ <u>30,828</u>	\$ <u>9,957</u>	\$ <u>20,871</u>	\$ <u>-</u>

Certain financial assets and liabilities are measured at fair value on a nonrecurring basis, that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). Adjustments to the fair market value of these assets usually result from the application of lower-of-cost-or-market accounting or write-downs of individual assets.



SUPPLEMENTAL INFORMATION



FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

BALANCE SHEET CONSOLIDATION SCHEDULE

December 31, 2015

(with Comparative Totals for 2014)

ASSETS	Consolidated Totals		Eliminations	First State Bankshares, Inc.	First State Bankshares of Delaware, Inc.	First State Bank
	2014	2015				
Cash and due from banks	\$ 3,342,101	\$ 2,862,873	\$ (12,175)	\$ 12,175	\$ 26,344	\$ 2,836,529
Interest-bearing deposits at other banks	23,229,692	31,191,866	-	-	-	31,191,866
Federal funds sold	-	765,000	-	-	-	765,000
Investment securities available-for-sale	30,827,797	27,994,671	-	-	-	27,994,671
Loans	78,966,920	73,879,951	-	-	-	73,879,951
Less allowance for credit losses	(645,628)	(701,687)	-	-	-	(701,687)
Net loans	78,321,292	73,178,264	-	-	-	73,178,264
Investments in restricted stock, at cost	379,600	371,600	-	-	-	371,600
Accrued interest receivable	831,727	1,008,250	-	-	-	1,008,250
Premises and equipment, net	429,658	394,940	-	250,000	188,653	206,287
Other assets	342,706	388,973	(500,000)	9,513,008	254,301	384,672
Investment in subsidiaries	-	-	(18,946,718)	9,775,183	9,433,710	-
Total Assets	\$ 137,704,573	\$ 138,156,437	\$ (19,458,893)	\$ 9,775,183	\$ 9,903,008	\$ 137,937,139

LIABILITIES AND STOCKHOLDERS' EQUITY

Liabilities:

Deposits						
Demand deposits - noninterest bearing	\$ 32,599,465	\$ 34,660,618	\$ (12,175)	\$ -	\$ -	\$ 34,672,793
Demand deposits - interest bearing	32,199,558	34,227,620	-	-	-	34,227,620
Savings deposits	6,296,994	6,139,079	-	-	-	6,139,079
Time deposits, \$100,000 and over	28,843,283	29,356,898	-	-	-	29,356,898
Other time deposits	12,198,653	11,195,392	-	-	-	11,195,392
Total deposits	112,137,953	115,579,607	(12,175)	-	-	115,591,782
Federal funds purchased	2,615,000	-	-	-	-	-
Pension benefit obligation	1,734,090	2,103,455	-	-	-	2,103,455
Accrued interest and other liabilities	381,173	378,861	(500,000)	249,838	250,000	379,023
Other borrowings	11,228,023	10,569,168	-	-	140,000	10,429,168
Total Liabilities	128,096,239	128,631,091	(512,175)	249,838	390,000	128,503,428

Stockholders' Equity:

Preferred stock, \$1 par value, 10,000,000 shares authorized, no shares issued

Common stock, \$1 par value, 1,000,000 shares authorized, 200,000 issued

Additional paid-in capital

Retained earnings

Accumulated other comprehensive income (loss)

Preferred stock, at cost, 75,081 shares	-	-	-	-	-	-
Common stock	200,000	200,000	(1,001,000)	200,000	1,000	1,000,000
Additional paid-in capital	7,315,786	7,315,786	(16,229,921)	7,315,786	12,229,921	4,000,000
Retained earnings	8,315,517	8,561,030	(6,011,735)	8,561,029	(569,944)	6,581,680
Accumulated other comprehensive income (loss)	(1,819,468)	(2,147,969)	4,295,938	(2,147,969)	(2,147,969)	(2,147,969)
Treasury stock, at cost, 75,081 shares	14,011,835	13,928,847	(18,946,718)	13,928,846	9,513,008	9,433,711
Total Stockholders' Equity	(4,403,501)	(4,403,501)	-	(4,403,501)	-	-
Total Liabilities and Stockholders' Equity	9,608,334	9,525,346	(18,946,718)	9,525,345	9,513,008	9,433,711
Total Liabilities and Stockholders' Equity	\$ 137,704,573	\$ 138,156,437	\$ (19,458,893)	\$ 9,775,183	\$ 9,903,008	\$ 137,937,139

See independent accountant's report

FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

STATEMENT OF INCOME CONSOLIDATION SCHEDULE
 Year Ended December 31, 2015
 (with Comparative Totals for 2014)

	Consolidated Totals		Eliminations	First State Bankshares, Inc.	First State Bankshares of Delaware, Inc.	First State Bank
	2014	2015				
Interest income:						
Interest and fees on loans	\$ 3,075,451	\$ 3,629,965	\$ -	\$ -	\$ -	\$ 3,629,965
Interest on investment securities	572,410	485,295	-	-	-	485,295
Interest on fed funds sold	1,667	1,489	-	-	-	1,489
Interest on deposits with banks	386,835	368,508	-	-	-	368,508
Total interest income	4,036,363	4,485,257	-	-	-	4,485,257
Interest expense:						
Interest on deposits	360,778	364,510	-	-	-	364,510
Interest on borrowed funds	77,443	301,050	-	-	-	301,050
Total interest expense	438,221	665,560	-	-	-	665,560
Net interest income	3,598,142	3,819,697	-	-	-	3,819,697
Provision (Credit) for loan losses	(47,608)	55,310	-	-	-	55,310
Net interest income after provision (credit) for loan losses	3,645,750	3,764,387	-	-	-	3,764,387
Other income:						
Service charges on deposit accounts	184,312	166,458	-	-	-	166,458
Other service charges and fees	138,532	136,422	-	-	-	136,422
Other income	6,884	120	(2,585,416)	1,251,519	1,333,917	100
Total other income	329,728	303,000	(2,585,416)	1,251,519	1,333,917	302,980
Other expenses:						
Salaries and employee benefits	1,736,287	1,777,190	-	-	-	1,777,190
Occupancy expense	170,765	210,055	-	-	43,113	166,942
Other expense	830,535	835,279	-	6,655	39,286	789,338
Total other expense	2,737,587	2,822,524	-	6,655	82,399	2,733,470
Net income	\$ 1,237,891	\$ 1,244,863	\$ (2,585,416)	\$ 1,244,864	\$ 1,251,518	\$ 1,333,897

See independent accountant's report

FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

STATEMENT OF CASH FLOWS CONSOLIDATION SCHEDULE
 Year Ended December 31, 2015
 (with Comparative Totals for 2014)

	Consolidated Totals		Eliminations	First State Bankshares, Inc.	First State Bankshares of Delaware, Inc.	First State Bank
	2014	2015				
Cash Flows from Operating Activities						
Net income	\$ 1,237,891	\$ 1,244,863	\$ (2,585,416)	\$ 1,244,864	\$ 1,251,518	\$ 1,333,897
Adjustments to reconcile net income to net cash provided by operating activities:						
Depreciation	82,536	80,279	-	-	43,113	37,166
Provision (credit) for loan losses	(47,607)	55,310	-	-	-	55,310
(Gain) loss on disposal of assets	-	11,976	-	-	-	11,976
Pension contributions	(306,376)	(264,000)	-	-	-	(264,000)
Pension expense, net	244,445	281,784	-	-	-	281,784
Amortization (accretion) on investment securities, net	252,502	155,911	-	-	-	155,911
(Increase) decrease in accrued interest receivable	(33,230)	(176,523)	-	-	-	(176,523)
(Increase) decrease in other assets	26,358	(46,267)	(20,000)	-	27,525	(53,792)
Increase (decrease) in accrued liabilities	23,617	(22,312)	-	-	-	(22,312)
Undistributed earnings of subsidiaries	-	-	535,418	(246,521)	(288,897)	-
Net Cash Provided by Operating Activities	1,480,136	1,321,021	(2,069,998)	998,343	1,033,259	1,359,417
Cash Flows from Investing Activities						
Sales and maturities of investment securities	37,195,391	33,700,271	-	-	-	33,700,271
Purchases of investment securities	(36,879,012)	(30,999,977)	-	-	-	(30,999,977)
Purchases (sales) of restricted stock	(205,500)	8,000	-	-	-	8,000
(Increase) decrease in federal funds sold	1,000,000	(765,000)	-	-	-	(765,000)
(Increase) decrease in loans, net	(15,700,179)	5,087,718	-	-	-	5,087,718
(Increase) decrease in interest-bearing deposits with other banks	1,070,168	(7,962,174)	-	-	-	(7,962,174)
Purchases of equipment	(83,028)	(57,537)	-	-	(4,160)	(53,377)
Net Cash Used for Investing Activities	(13,602,160)	(988,699)	-	-	(4,160)	(984,539)

See independent accountant's report

FIRST STATE BANKSHARES, INC. AND SUBSIDIARY

STATEMENT OF CASH FLOWS CONSOLIDATION SCHEDULE
 Year Ended December 31, 2015
 (with Comparative Totals for 2014)

	Consolidated Totals		Eliminations	First State Bankshares, Inc.	First State Bankshares of Delaware, Inc.	First State Bank
	2014	2015				
(continued)						
Cash Flows from Financing Activities						
Increase (decrease) in demand deposits, net	1,506,657	4,109,216	21,008	-	-	4,088,208
Increase (decrease) in savings deposits, net	1,192,031	(157,915)	-	-	-	(157,915)
Increase (decrease) in time deposits, net	(1,958,379)	(489,646)	-	-	-	(489,646)
Advances on other borrowed funds	18,308,030	(781,600)	-	-	-	(781,600)
Payments on other borrowed funds	(9,253,024)	122,745	-	-	-	122,745
(Increase) decrease in federal funds purchased	2,615,000	(2,615,000)	-	-	-	(2,615,000)
Dividends paid on common stock	(999,352)	(999,350)	2,049,998	(999,350)	(1,004,999)	(1,044,999)
Net Cash Provided by (Used for) Financing Activities	11,410,963	(811,550)	2,071,006	(999,350)	(1,004,999)	(878,207)
Net Change in Cash and Due From Banks	(711,061)	(479,228)	1,007	(1,007)	24,100	(503,329)
Cash and Due From Banks, beginning of year	4,053,162	3,342,101	(13,182)	13,182	2,244	3,339,857
Cash and Due From Banks, end of year	\$ 3,342,101	\$ 2,862,873	\$ (12,175)	\$ 12,175	\$ 26,344	\$ 2,836,528
Supplemental Disclosures of Cash Flow Information						
Interest paid	\$ 442,399	\$ 667,145	\$ -	\$ -	\$ 2,800	\$ 664,345

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