

OLD POINT FINANCIAL CORP  
Form 10-Q  
August 04, 2006  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

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**FORM 10-Q**

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(Mark One)

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

For the quarterly period ended June 30, 2006

or

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

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

Commission File Number: 000-12896

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**OLD POINT FINANCIAL CORPORATION**

(Exact name of registrant as specified in its charter)

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**VIRGINIA**  
(State or other jurisdiction of  
incorporation or organization)

**54-1265373**  
(I.R.S. Employer  
Identification No.)

**1 West Mellen Street, Hampton, Virginia 23663**  
(Address of principal executive offices) (Zip Code)  
**(757) 722-7451**

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(Registrant's telephone number, including area code)

**Not Applicable**

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

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

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

3,991,531 shares of common stock (\$5.00 par value) outstanding as of July 31, 2006

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## Consolidated Balance Sheets

|  | June 30,<br>2006<br>(unaudited) | December 31,<br>2005 |
|--|---------------------------------|----------------------|
| <b>Assets</b>  |                                 |                      |
| Cash and due from banks  | \$ 17,594,483                   | \$ 13,601,677        |
| Federal funds sold   | 5,450,975                       | 2,004,347            |
| Cash and cash equivalents  | 23,045,458                      | 15,606,024           |
| Securities available-for-sale, at fair value   | 186,064,965                     | 192,942,880          |
| Securities held-to-maturity (fair value approximates \$3,308,280 and \$3,140,957)                | 3,323,000                       | 3,122,994            |
| Loans, net of allowance for loan losses of \$4,548,937 and \$4,447,524                           | 544,905,460                     | 490,248,868          |
| Premises and equipment, net  | 21,477,609                      | 21,276,974           |
| Bank owned life insurance  | 10,324,950                      | 9,660,818            |
| Other assets   | 7,879,148                       | 7,134,661            |
|  | \$ 797,020,590                  | \$ 739,993,219       |
| <b>Liabilities &amp; Stockholders Equity</b>   |                                 |                      |
| Deposits:  |                                 |                      |
| Noninterest-bearing deposits   | \$ 97,951,492                   | \$ 98,685,836        |
| Savings and interest-bearing demand deposits   | 200,145,477                     | 195,833,551          |
| Time deposits  | 258,712,364                     | 242,224,814          |
| Total deposits   | 556,809,333                     | 536,744,201          |
| Federal funds purchased, repurchase agreements and other borrowings                              | 51,186,216                      | 50,621,569           |
| Federal Home Loan Bank advances  | 115,000,000                     | 80,000,000           |
| Accrued expenses and other liabilities   | 2,437,853                       | 1,571,403            |
| Total liabilities  | 725,433,402                     | 668,937,173          |
| Commitments and contingencies  |                                 |                      |
| Stockholders Equity:   |                                 |                      |
| Common stock, \$5 par value, 10,000,000 shares authorized; 3,991,305 and 4,013,553 shares issued | 19,956,525                      | 20,067,765           |
| Additional paid-in capital   | 14,619,872                      | 14,319,580           |
| Retained earnings  | 40,264,975                      | 39,074,325           |
| Accumulated other comprehensive loss, net  | (3,254,184)                     | (2,405,624)          |
| Total stockholders equity  | 71,587,188                      | 71,056,046           |
|  | \$ 797,020,590                  | \$ 739,993,219       |

See Notes to Consolidated Financial Statements.



**Table of Contents****Old Point Financial Corporation and Subsidiaries**

## Consolidated Statements of Income

|   | Three Months Ended |                  | Six Months Ended |                  |
|---|--------------------|------------------|------------------|------------------|
|   | June 30,<br>2006   | June 30,<br>2005 | June 30,<br>2006 | June 30,<br>2005 |
|   | (unaudited)        |                  |                  |                  |
| <b>Interest and Dividend Income:</b>  |                    |                  |                  |                  |
| Interest and fees on loans  | \$ 9,005,132       | \$ 6,908,074     | \$ 17,304,167    | \$ 13,662,452    |
| Interest on federal funds sold  | 80,839             | 50,740           | 133,164          | 86,273           |
| Interest on securities:   |                    |                  |                  |                  |
| Taxable   | 1,277,567          | 1,312,857        | 2,565,640        | 2,687,887        |
| Tax-exempt  | 366,956            | 425,946          | 755,240          | 869,482          |
| Dividends and interest on all other securities  | 91,649             | 49,787           | 178,998          | 104,905          |
| Total interest and dividend income  | 10,822,143         | 8,747,404        | 20,937,209       | 17,410,999       |
| <b>Interest Expense:</b>  |                    |                  |                  |                  |
| Interest on savings and interest-bearing demand deposits  | 571,012            | 342,557          | 1,064,605        | 664,624          |
| Interest on time deposits   | 2,526,873          | 1,597,555        | 4,805,638        | 3,082,898        |
| Interest on federal funds purchased, securities sold under agreement to repurchase and other borrowings | 464,393            | 278,405          | 872,214          | 502,133          |
| Interest on Federal Home Loan Bank advances   | 1,153,712          | 549,982          | 2,138,046        | 1,134,103        |
| Total interest expense  | 4,715,990          | 2,768,499        | 8,880,503        | 5,383,758        |
| Net interest income   | 6,106,153          | 5,978,905        | 12,056,706       | 12,027,241       |
| Provision for loan losses   | 300,000            | 225,000          | 600,000          | 450,000          |
| Net interest income, after provision for loan losses  | 5,806,153          | 5,753,905        | 11,456,706       | 11,577,241       |
| <b>Noninterest Income:</b>  |                    |                  |                  |                  |
| Income from fiduciary activities  | 661,486            | 696,730          | 1,338,900        | 1,413,464        |
| Service charges on deposit accounts   | 1,391,562          | 1,185,227        | 2,725,497        | 2,257,805        |
| Other service charges, commissions and fees   | 718,288            | 401,050          | 1,253,637        | 899,202          |
| Income from bank owned life insurance   | 133,575            | 124,933          | 266,728          | 247,477          |
| Net gain on available-for-sale securities   | 550                | 3,775            | 1,896            | 8,918            |
| Other operating income  | 119,456            | 139,845          | 225,612          | 230,481          |
| Total noninterest income  | 3,024,917          | 2,551,560        | 5,812,270        | 5,057,347        |
| <b>Noninterest Expense:</b>   |                    |                  |                  |                  |
| Salaries and employee benefits  | 3,825,051          | 3,563,821        | 7,536,647        | 6,975,042        |
| Occupancy and equipment   | 885,790            | 744,172          | 1,777,310        | 1,501,085        |
| Supplies  | 255,398            | 234,117          | 255,398          | 234,117          |
| Postage and courier   | 128,953            | 115,994          | 268,426          | 234,250          |
| Service fees  | 200,459            | 147,457          | 369,186          | 276,782          |
| Data processing   | 186,249            | 146,661          | 355,272          | 293,809          |
| Advertising   | 189,364            | 187,501          | 331,207          | 251,765          |
| Customer development  | 126,924            | 133,898          | 294,329          | 265,602          |
| Employee professional development   | 160,248            | 164,330          | 291,284          | 279,634          |
| Other   | 387,006            | 343,433          | 1,006,355        | 967,663          |
| Total noninterest expenses  | 6,345,442          | 5,781,384        | 12,485,414       | 11,279,749       |

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|                            |              |              |              |              |
|----------------------------|--------------|--------------|--------------|--------------|
| Income before income taxes | 2,485,628    | 2,524,081    | 4,783,562    | 5,354,839    |
| Income tax expense         | 679,807      | 669,925      | 1,287,372    | 1,444,025    |
| Net income                 | \$ 1,805,821 | \$ 1,854,156 | \$ 3,496,190 | \$ 3,910,814 |

**Basic Earnings per Share**

|                                      |           |           |           |           |
|--------------------------------------|-----------|-----------|-----------|-----------|
| Average shares outstanding           | 3,988,674 | 4,016,144 | 3,991,815 | 4,015,763 |
| Net income per share of common stock | \$ 0.45   | \$ 0.46   | \$ 0.88   | \$ 0.97   |

**Diluted Earnings per Share**

|                                      |           |           |           |           |
|--------------------------------------|-----------|-----------|-----------|-----------|
| Average shares outstanding           | 4,049,006 | 4,095,746 | 4,052,729 | 4,098,913 |
| Net income per share of common stock | \$ 0.45   | \$ 0.45   | \$ 0.86   | \$ 0.95   |

See Notes to Consolidated Financial Statements.

**Table of Contents****Old Point Financial Corporation and Subsidiaries**

## Consolidated Statements of Changes in Stockholders' Equity

| (Unaudited)  | Shares of<br>Common<br>Stock | Common<br>Stock   | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income (Loss) | Total             |
|--|------------------------------|-------------------|----------------------------------|----------------------|--|-------------------|
| <b>FOR SIX MONTHS ENDED JUNE 30, 2006</b>                                      |                              |                   |                                  |                      |  |                   |
| Balance at beginning of period   | 4,013,553                    | \$ 20,067,765     | \$ 14,319,580                    | \$ 39,074,325        | \$ (2,405,624)   | \$ 71,056,046     |
| Comprehensive income:  |                              |                   |                                  |                      |  |                   |
| Net income   |                              |                   |                                  | 3,496,190            |  | 3,496,190         |
| Unrealized holding losses arising during the period<br>(net of tax, \$436,492) |                              |                   |                                  |                      | (847,309)  | (847,309)         |
| Reclassification adjustment, (net of tax, \$645)                               |                              |                   |                                  |                      | (1,251)  | (1,251)           |
| <b>Total comprehensive income</b>  |                              |                   |                                  | <b>3,496,190</b>     | <b>(848,560)</b>                                       | <b>2,647,630</b>  |
| Sale of common stock   | 10,070                       | 50,350            | 280,835                          | (180,768)            |  | 150,417           |
| Repurchase and retirement of common stock                                      | (32,318)                     | (161,590)         |                                  | (769,203)            |  | (930,793)         |
| Nonqualified stock options   |                              |                   | 19,457                           |                      |  | 19,457            |
| Cash dividends (\$.34 per share)   |                              |                   |                                  | (1,355,569)          |  | (1,355,569)       |
| <br>Balance at end of period   | <br>3,991,305                | <br>\$ 19,956,525 | <br>\$ 14,619,872                | <br>\$ 40,264,975    | <br>\$ (3,254,184)                                     | <br>\$ 71,587,188 |
| <b>FOR SIX MONTHS ENDED JUNE 30, 2005</b>                                      |                              |                   |                                  |                      |  |                   |
| Balance at beginning of period   | 4,013,644                    | \$ 20,068,220     | \$ 14,074,162                    | \$ 34,803,848        | \$ 193,092   | \$ 69,139,322     |
| Comprehensive income:  |                              |                   |                                  |                      |  |                   |
| Net income   |                              |                   |                                  | 3,910,814            |  | 3,910,814         |
| Unrealized holding losses arising during the period<br>(net of tax, \$474,939) |                              |                   |                                  |                      | (921,941)  | (921,941)         |
| Reclassification adjustment, (net of tax, \$3,032)                             |                              |                   |                                  |                      | (5,886)  | (5,886)           |
| <b>Total comprehensive income</b>  |                              |                   |                                  | <b>3,910,814</b>     | <b>(927,827)</b>                                       | <b>2,982,987</b>  |
| Sale of common stock   | 2,500                        | 12,500            | 69,210                           | (27,583)             |  | 54,127            |
| Nonqualified stock options   |                              |                   | 9,378                            |                      |  | 9,378             |
| Cash dividends (\$.32 per share)   |                              |                   |                                  | (1,285,174)          |  | (1,285,174)       |
| <br>Balance at end of period   | <br>4,016,144                | <br>\$ 20,080,720 | <br>\$ 14,152,750                | <br>\$ 37,401,905    | <br>\$ (734,735)                                       | <br>\$ 70,900,640 |

See Notes to Consolidated Financial Statements.



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## Consolidated Statements of Cash Flows

|   | Six Months Ended June 30,<br>2006<br>(unaudited) 2005 |               |
|---|---|---------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                                       |   |               |
| Net income  | \$ 3,496,190  | \$ 3,910,814  |
| Adjustments to reconcile net income to net cash provided by operating activities: |   |               |
| Depreciation and amortization   | 777,825   | 663,002       |
| Provision for loan losses   | 600,000   | 450,000       |
| Net gain on sale of available-for-sale securities                                 | (1,896)   | (8,918)       |
| Net amortization (accretion) of securities  | (24,079)  | 10,203        |
| Loss (gain) on disposal of equipment  | (180)   | 1,969         |
| Increase in bank-owned life insurance   | (866,728)   | (923,085)     |
| Increase in other assets  | (104,754)   | (206,275)     |
| Increase in other liabilities   | 866,450   | 658,923       |
| Net cash provided by operating activities   | 4,742,828   | 4,556,633     |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                                       |   |               |
| Purchases of available-for-sale securities  | (4,028,813)   | (2,421,647)   |
| Purchases of held-to-maturity securities  | (300,000)   | (400,000)     |
| Proceeds from maturities and calls of securities                                  | 8,472,000   | 9,013,450     |
| Proceeds from sales of available-for-sale securities                              | 1,275,000   | 3,454,300     |
| Loans made to customers   | (168,455,656)   | (111,062,057) |
| Principal payments received on loans  | 113,199,064   | 106,623,923   |
| Purchases of premises and equipment   | (978,280)   | (1,746,967)   |
| Net cash provided by (used in) investing activities                               | (50,816,685)  | 3,461,002     |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                                       |   |               |
| Increase (decrease) in non-interest bearing deposits                              | (734,344)   | 3,021,117     |
| Increase (decrease) in savings deposits   | 4,311,926   | (8,679,395)   |
| Proceeds from the sale of time deposits   | 86,971,384  | 76,910,120    |
| Payments for maturing time deposits   | (70,483,834)  | (74,087,423)  |
| Increase in federal funds purchased and repurchase agreements                     | 1,018,878   | 1,341,707     |
| Increase in Federal Home Loan Bank advances                                       | 35,000,000  | 15,000,000    |
| Decrease in interest-bearing demand notes and other borrowed money                | (454,231)   | (1,898,985)   |
| Proceeds from issuance of common stock  | 150,417   | 54,127        |
| Repurchase and retirement of common stock   | (930,793)   |               |
| Effect of nonqualified stock options  | 19,457  | 9,378         |
| Cash dividends paid on common stock   | (1,355,569)   | (1,285,174)   |
| Net cash provided by financing activities   | 53,513,291  | 10,385,472    |
| Net increase in cash and cash equivalents   | 7,439,434   | 18,403,107    |
| Cash and cash equivalents at beginning of period                                  | 15,606,024  | 13,572,813    |
| Cash and cash equivalents at end of period  | \$ 23,045,458   | \$ 31,975,920 |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>                          |   |               |
| Cash payments for:  |   |               |
| Interest  | \$ 8,571,212  | \$ 5,290,524  |

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|  |             |             |
|--|-------------|-------------|
| Income tax   | 1,175,000   | 1,450,000   |
| <b>SUPPLEMENTAL SCHEDULE OF NONCASH TRANSACTIONS</b> |             |             |
| Unrealized loss on investment securities             | (1,285,697) | (1,405,798) |

See Notes to Consolidated Financial Statements.

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**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)****Note 1. General**

The accompanying unaudited consolidated financial statements of Old Point Financial Corporation (the Company) and its subsidiaries have been prepared in accordance with U. S. generally accepted accounting principles for interim financial information. All significant intercompany balances and transactions have been eliminated. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments and reclassifications consisting of a normal and recurring nature considered necessary to present fairly the financial positions at June 30, 2006 and December 31, 2005, the results of operations for the three months and six months ended June 30, 2006 and 2005, and statements of changes in stockholders' equity and cash flows for the six months ended June 30, 2006 and 2005. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year.

These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's 2005 annual report on Form 10-K. Certain previously reported amounts have been reclassified to conform to current period presentation.

The Company maintains a website on the Internet at [www.oldpoint.com](http://www.oldpoint.com). The Company makes available free of charge, on or through its website, its proxy statements, annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports as soon as reasonably practicable after such material is electronically filed with the Securities and Exchange Commission (SEC). The information available at the Company's Internet address is not part of this Form 10-Q or any other report filed by the Company with the SEC. The public may read and copy any documents the Company files at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The Company's SEC filings can also be obtained on the SEC's website on the Internet at [www.sec.gov](http://www.sec.gov).

**Note 2. Securities**

Amortized costs and fair values of securities held-to-maturity at June 30, 2006 and December 31, 2005 are as follows:

|   | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|---|-------------------|------------------------------|-------------------------------|---------------|
|   | (in thousands)    |                              |                               |               |
| <b>June 30, 2006</b>                            |                   |                              |                               |               |
| Obligations of U. S. Government agencies        | \$ 2,500          | \$                           | \$ (52)                       | \$ 2,448      |
| Obligations of state and political subdivisions | 823               | 37                           |                               | 860           |
|   | \$ 3,323          | \$ 37                        | \$ (52)                       | \$ 3,308      |
| <b>December 31, 2005</b>                        |                   |                              |                               |               |
| Obligations of U. S. Government agencies        | \$ 2,300          | \$                           | \$ (41)                       | \$ 2,259      |
| Obligations of state and political subdivisions | 823               | 59                           |                               | 882           |
|   | \$ 3,123          | \$ 59                        | \$ (41)                       | \$ 3,141      |

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Amortized costs and fair values of securities available-for-sale at June 30, 2006 and December 31, 2005 are as follows:

|   | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value     |
|---|-------------------|------------------------------|-------------------------------|-------------------|
|   | (in thousands)    |                              |                               |                   |
| <b>June 30, 2006</b>                            |                   |                              |                               |                   |
| United States Treasury securities               | \$ 981            | \$                           | \$ (1)                        | \$ 980            |
| Obligations of U. S. Government agencies        | 150,971           |                              | (5,255)                       | 145,716           |
| Obligations of state and political subdivisions | 31,255            | 381                          | (27)                          | 31,609            |
| Money market investments                        | 783               |                              |                               | 783               |
| Federal Home Loan Bank stock - restricted       | 6,644             |                              |                               | 6,644             |
| Federal Reserve Bank stock - restricted         | 169               |                              |                               | 169               |
| Other marketable equity securities              | 193               |                              | (29)                          | 164               |
| <b>Total</b>                                    | <b>\$ 190,996</b> | <b>\$ 381</b>                | <b>\$ (5,312)</b>             | <b>\$ 186,065</b> |
| <b>December 31, 2005</b>                        |                   |                              |                               |                   |
| United States Treasury securities               | \$ 984            | \$ 1                         | \$                            | \$ 985            |
| Obligations of U. S. Government agencies        | 154,761           | 1                            | (4,370)                       | 150,392           |
| Obligations of state and political subdivisions | 34,832            | 763                          | (12)                          | 35,583            |
| Money market investments                        | 686               |                              |                               | 686               |
| Federal Home Loan Bank stock - restricted       | 4,963             |                              |                               | 4,963             |
| Federal Reserve Bank stock - restricted         | 169               |                              |                               | 169               |
| Other marketable equity securities              | 193               |                              | (28)                          | 165               |
| <b>Total</b>                                    | <b>\$ 196,588</b> | <b>\$ 765</b>                | <b>\$ (4,410)</b>             | <b>\$ 192,943</b> |

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Information pertaining to securities with gross unrealized losses at June 30, 2006 and December 31, 2005, aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

|   | Quarter Ended June 30, 2006   |               |                               |               |                               |               |
|---|-------------------------------|---------------|-------------------------------|---------------|-------------------------------|---------------|
|   | Less Than Twelve Months       |               | More Than Twelve Months       |               | Total                         |               |
|   | Gross<br>Unrealized<br>Losses | Fair<br>Value | Gross<br>Unrealized<br>Losses | Fair<br>Value | Gross<br>Unrealized<br>Losses | Fair<br>Value |
| <b>Securities Available-for-Sale</b>            |                               |               |                               |               |                               |               |
| Debt securities:                                |                               |               |                               |               |                               |               |
| United States Treasury securities               | \$ 1                          | \$ 980        | \$                            | \$            | \$ 1                          | \$ 980        |
| Obligations of U. S. Government Agencies        |                               |               | 5,255                         | 145,716       | 5,255                         | 145,716       |
| Obligations of state and political subdivisions | 12                            | 1,003         | 15                            | 250           | 27                            | 1,253         |
| Total debt securities                           | 13                            | 1,983         | 5,270                         | 145,966       | 5,283                         | 147,949       |
| Other marketable equity securities              |                               |               | 29                            | 21            | 29                            | 21            |
| Total securities available-for-sale             | \$ 13                         | \$ 1,983      | \$ 5,299                      | \$ 145,987    | \$ 5,312                      | \$ 147,970    |
| <b>Securities Held-to-Maturity</b>              |                               |               |                               |               |                               |               |
| Obligations of U. S. Government Agencies        | \$ 6                          | \$ 594        | \$ 46                         | \$ 1,854      | \$ 52                         | \$ 2,448      |
| Total securities held-to-maturity               | \$ 6                          | \$ 594        | \$ 46                         | \$ 1,854      | \$ 52                         | \$ 2,448      |
| Total   | \$ 19                         | \$ 2,577      | \$ 5,345                      | \$ 147,841    | \$ 5,364                      | \$ 150,418    |

  

|   | Year Ended December 31, 2005  |               |                               |               |                               |               |
|---|-------------------------------|---------------|-------------------------------|---------------|-------------------------------|---------------|
|   | Less Than Twelve Months       |               | More Than Twelve Months       |               | Total                         |               |
|   | Gross<br>Unrealized<br>Losses | Fair<br>Value | Gross<br>Unrealized<br>Losses | Fair<br>Value | Gross<br>Unrealized<br>Losses | Fair<br>Value |
| <b>Securities Available-for-Sale</b>            |                               |               |                               |               |                               |               |
| Debt securities:                                |                               |               |                               |               |                               |               |
| Obligations of U. S. Government Agencies        | \$ 96                         | \$ 5,903      | \$ 4,274                      | \$ 142,689    | \$ 4,370                      | \$ 148,592    |
| Obligations of state and political subdivisions | 12                            | 253           |                               |               | 12                            | 253           |
| Total debt securities                           | 108                           | 6,156         | 4,274                         | 142,689       | 4,382                         | 148,845       |
| Other marketable equity securities              |                               |               | 28                            | 22            | 28                            | 22            |
| Total securities available-for-sale             | \$ 108                        | \$ 6,156      | \$ 4,302                      | \$ 142,711    | \$ 4,410                      | \$ 148,867    |
| <b>Securities Held-to-Maturity</b>              |                               |               |                               |               |                               |               |
| Obligations of U. S. Government Agencies        | \$ 14                         | \$ 1,086      | \$ 27                         | \$ 1,173      | \$ 41                         | \$ 2,259      |
| Total securities held-to-maturity               | \$ 14                         | \$ 1,086      | \$ 27                         | \$ 1,173      | \$ 41                         | \$ 2,259      |
| Total   | \$ 122                        | \$ 7,242      | \$ 4,329                      | \$ 143,884    | \$ 4,451                      | \$ 151,126    |

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The Company has the ability and intent to hold these securities until maturity. The securities are impaired primarily due to rising interest rates. None of the securities are impaired due to credit issues. Therefore, securities with a loss are considered temporarily impaired.

**Note 3. Loans**

Loans at June 30, 2006 and December 31, 2005 are summarized as follows:

|                                  | June 30,<br>2006 | December 31,<br>2005 |
|----------------------------------|------------------|----------------------|
|                                  | (in thousands)   |                      |
| Commercial and other loans       | \$ 67,548        | \$ 63,224            |
| Real estate loans:               |                  |                      |
| Construction                     | 51,530           | 36,517               |
| Farmland                         | 229              | 168                  |
| Equity lines of credit           | 25,283           | 21,765               |
| 1-4 family residential           | 114,327          | 101,328              |
| Multifamily residential          | 10,559           | 8,526                |
| Nonfarm nonresidential           | 210,775          | 193,744              |
| Installment loans to individuals | 65,549           | 66,903               |
| Tax-exempt loans                 | 3,329            | 2,376                |
| <b>Total loans</b>               | <b>549,129</b>   | <b>494,551</b>       |
| Less: Allowance for loan losses  | (4,549)          | (4,448)              |
| Net deferred loan costs          | 325              | 146                  |
| <br>                             |                  |                      |
| Loans, net                       | \$ 544,905       | \$ 490,249           |

**Note 4. Allowance for Loan Losses**

The following summarizes activity in the allowance for loan losses at June 30, 2006 and December 31, 2005:

|                            | June 30,<br>2006 | December 31,<br>2005 |
|----------------------------|------------------|----------------------|
|                            | (in thousands)   |                      |
| Balance, beginning of year | \$ 4,448         | \$ 4,303             |
| Recoveries                 | 151              | 370                  |
| Provision for loan losses  | 600              | 1,050                |
| Loans charged off          | (650)            | (1,275)              |
| <br>                       |                  |                      |
| Balance, end of period     | \$ 4,549         | \$ 4,448             |

**Note 5. Stock-Based Compensation**

The Company adopted Statement of Financial Accounting Standards (SFAS) No. 123R, Share-Based Payment (SFAS No. 123R) effective January 1, 2006 using the modified prospective method and as such results for prior periods have not been restated. Share-based compensation arrangements include stock options, restricted stock plans, performance-based awards, stock appreciation rights and employee stock purchase plans. SFAS No. 123R requires all share-based payments to employees to be valued using a fair value method on the date of grant and to be expensed based on that fair value over the applicable vesting period. The initial implementation had no effect on the Company's financial statements as all outstanding options were fully vested at December 31, 2005 and the Company has not issued new options in 2006.



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Had compensation costs for the stock option plans in 2005 been determined based upon the fair value at the date of grant consistent with SFAS No. 123, pro forma net income and earnings per share for the six months ended June 30, 2005 would have been as follows:

Pro forma disclosure under SFAS No. 123

|                                      | <b>Six Months Ended<br/>June 30, 2005</b> |
|--------------------------------------|---|
| <b>Net income:</b>                   |   |
| As reported                          | \$ 3,910,814                              |
| Fair value-based expense, net of tax | (284,560)                                 |
| <br>Pro forma                        | <br>\$ 3,626,254                          |
| <b>Basic earnings per share:</b>     |   |
| As reported                          | \$ 0.97                                   |
| Pro forma                            | \$ 0.90                                   |
| <b>Diluted earnings per share:</b>   |   |
| As reported                          | \$ 0.95                                   |
| Pro forma                            | \$ 0.89                                   |

Stock option plan activity for the six months ended June 30, 2006 is summarized below:

|                                  | <b>Shares</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>Weighted<br/>Average<br/>Remaining<br/>Contractual<br/>Life<br/>(in years)</b> | <b>Value of<br/>Unexercised<br/>In-The-<br/>Money<br/>Options</b> |
|----------------------------------|---------------|--|---|---|
| Options outstanding, January 1   | 265,387       | \$ 22.09   |   |   |
| Granted                          |               |  |   |   |
| Exercised                        | (11,840)      | 16.69  |   |   |
| Canceled or expired              | (3,000)       | 28.85  |   |   |
| <br>Options outstanding, June 30 | <br>250,547   | <br>22.25  | <br>4.75  | <br>\$ 1,814,523  |
| Options exercisable, June 30     | 250,547       | \$ 22.25   | 4.75  | \$ 1,814,523  |

The total value of the in-the-money options exercised during the six months ended June 30, 2006 was \$340 thousand.

As of June 30, 2006, there was no unrecognized compensation expense because all outstanding options were vested.

SFAS 123R requires the benefits of tax deductions in excess of grant-date fair value be reported as a financing cash flow. The Company had \$19.5 thousand in tax deductions from the exercise of stock options in the second quarter of 2006.



**Table of Contents****Note 6. Pension Plan**

The Company provides pension benefits for eligible employees through a defined benefit pension plan. Substantially all employees participate in the retirement plan on a non-contributing basis and are fully vested after 25 years of service. The components of net periodic pension cost are as follows:

| Quarter ended June 30,             | 2006                    | 2005       |
|------------------------------------|-------------------------|------------|
|                                    | <b>Pension Benefits</b> |            |
| Service cost                       | \$ 126,049              | \$ 106,345 |
| Interest cost                      | 83,788                  | 80,017     |
| Expected return on plan assets     | (96,067)                | (80,259)   |
| Amortization of prior service cost | 320                     | 320        |
| Amortization of net loss           | 44,789                  | 38,001     |
| Net periodic benefit cost          | \$ 158,879              | \$ 144,424 |
|                                    |                         |            |
| Six months ended June 30,          | 2006                    | 2005       |
|                                    | <b>Pension Benefits</b> |            |
| Service cost                       | \$ 252,098              | \$ 212,690 |
| Interest cost                      | 167,576                 | 160,034    |
| Expected return on plan assets     | (192,134)               | (160,518)  |
| Amortization of prior service cost | 640                     | 640        |
| Amortization of net loss           | 89,578                  | 76,002     |
| Net periodic benefit cost          | \$ 317,758              | \$ 288,848 |

The Company previously disclosed in its financial statements for the year ended December 31, 2005 that it expected to contribute \$750 thousand to its pension plan in 2006. As of June 30, 2006, no contributions have been made. The Company continues to anticipate contributing \$750 thousand in 2006.

On July 11, 2006 the Board of Directors of the Company voted to freeze the pension plan effective September 30, 2006. The Company is currently working on a notification that must be sent to employees by August 15, 2006.

**Note 7. Earnings per Share**

Basic earnings per share is computed by dividing net income by the weighted average number of shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common shares outstanding during the period, including the effect of dilutive potential common shares outstanding attributable to stock options.

**Note 8. Recent Accounting Pronouncements**

In March 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 156, Accounting for Servicing of Financial Assets an amendment of FASB Statement 140 (Statement 156). Statement 156 amends Statement 140 with respect to separately recognized servicing assets and liabilities. Statement 156 requires an entity to recognize a servicing asset or liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract and requires all servicing assets and liabilities to be initially measured at fair value, if practicable. Statement 156 also permits entities to subsequently measure servicing assets and liabilities using an amortization method or fair value measurement method. Under the amortization method, servicing assets and liabilities are amortized in proportion to and over the estimated period of servicing. Under the fair value measurement method, servicing assets are measured at fair value at each reporting date and changes in fair value are reported in net income for the period the change occurs.

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Adoption of Statement 156 is required as of the beginning of fiscal years beginning subsequent to September 15, 2006. Earlier adoption is permitted as of the beginning of an entity's fiscal year, provided the entity has not yet issued financial statements, including interim financial statements.

The Company does not expect the adoption of Statement 156 at the beginning of 2007 to have a material impact.

## **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

The following discussion is intended to assist readers in understanding and evaluating the financial condition, changes in financial condition and the results of operations of the Company. The Company consists of the parent company and its wholly-owned subsidiaries, The Old Point National Bank of Phoebus (the Bank) and Old Point Trust & Financial Services, N. A. (Trust), collectively referred to as the Company. This discussion should be read in conjunction with the consolidated financial statements and other financial information contained elsewhere in this report.

### **Caution About Forward Looking Statements**

In addition to historical information, this report may contain forward-looking statements. For this purpose, any statement that is not a statement of historical fact may be deemed to be a forward-looking statement. These forward-looking statements may include statements regarding profitability, liquidity, allowance for loan losses, interest rate sensitivity, market risk, growth strategy and financial and other goals. Forward-looking statements often use words such as believes, expects, plans, may, will, should, projects, contemplates, and forecasts, intends or other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts. Forward-looking statements are subject to numerous assumptions, risks and uncertainties, and actual results could differ materially from historical results or those anticipated by such statements.

Factors that could have a material adverse effect on the operations and future prospects of the Company include, but are not limited to, changes in: interest rates, general economic conditions, monetary and fiscal policies of the U. S. Government, including policies of the Office of the Comptroller of the Currency, U. S. Treasury and the Federal Reserve Board, the quality or composition of the loan or investment portfolios, demand for loan products, deposit flows, competition, and accounting principles, policies and guidelines. These risks and uncertainties should be considered in evaluating the forward-looking statements contained herein, and readers are cautioned not to place undue reliance on such statements. Any forward-looking statement speaks only as of the date on which it is made, and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which it is made. In addition, past results of operations are not necessarily indicative of future results.

### **General**

The Company is the parent company of the Bank and Trust. The Bank is a locally owned and managed community bank serving the Hampton Roads localities of Hampton, Newport News, Norfolk, Virginia Beach, Chesapeake, Williamsburg/James City County, York County and Isle of Wight County. The Bank currently has 19 branch offices. Trust is a wealth management services provider.

### **Critical Accounting Policies and Estimates**

As of June 30, 2006, there have been no significant changes with regard to the critical accounting policies and estimates disclosed in the Company's annual report on Form 10-K for the year ended December 31, 2005. That disclosure included a discussion of the accounting policy that requires management's most difficult, subjective or complex judgments: the allowance for loan losses.

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### **Earnings Summary**

Net income for the second quarter of 2006 was \$1.8 million as compared with \$1.9 million earned in the comparable quarter in 2005, a decrease of 2.61%. The lower income is attributed to continued pressure on the net interest yield, increase in the loan loss provision and further branch expansion. Basic and diluted earnings per share for the second quarter of 2006 were \$0.45. Basic earnings per share for the second quarter of 2005 were \$0.46, or \$0.45 on a fully diluted basis. Annualized return on average assets (ROA) for the second quarter of 2006 was 0.93% and 1.08% for the comparable period in 2005. Return on equity (ROE) was 10.09% for the second quarter of 2006 compared with 10.53% for the same period in 2005.

For the six months ended June 30, 2006 and 2005, ROA was 0.91% and 1.14%, respectively. ROE was 9.81% in 2006 and 11.20% in 2005.

### **Net Interest Income**

The principal source of earnings for the Company is net interest income. Net interest income is the difference between interest and fees generated by earning assets and interest expense paid to fund them. Changes in the volume and mix of interest-earning assets and interest-bearing liabilities, as well as their respective yields and rates, have a significant impact on the level of net interest income. The net interest yield is calculated by dividing tax equivalent net interest income by average earning assets.

Net interest income, on a fully tax equivalent basis, was \$6.3 million in the second quarter of 2006, an increase of \$104 thousand, or 1.67% from the second quarter of 2005. The net interest yield was 3.45% in the second quarter of 2006 as compared to 3.87% in 2005.

For the six months ended June 30, 2006 net interest income on a fully tax equivalent basis decreased \$22 thousand, or 0.18%, over the comparable period in 2005. Comparing the first six months of 2006 to 2005, average loans increased \$84.9 million, or 19.58%, while investment securities decreased \$7.8 million, or 3.82%. Average earning assets increased 11.86% and the net interest yield decreased from 3.89% in 2005 to 3.47% in 2006. Although the net interest yield decreased by 42 basis points, the significant increase in loan volume lessened the negative effect on net interest income.

Tax equivalent interest income increased \$2.1 million, or 22.84%, in the second quarter of 2006 compared to the second quarter of 2005. Average earning assets grew \$89.2 million, or 13.88%. Total average loans increased \$96.0 million, or 22.10%, while average investment securities decreased \$6.4 million, or 3.17%. The yield on earning assets increased for the second quarter of 2006 compared to the second quarter of 2005 by 44 basis points. Most of the increase was due to increasing yields in the loan portfolio.

Interest expense increased \$1.9 million, or 70.3%, in the second quarter of 2006 from the second quarter of 2005 while interest-bearing liabilities increased \$93.6 million or 18.30% in the second quarter of 2006 over the same period in 2005. The cost of funding those liabilities increased 95 basis points from 2005. For the six months ended June 30, 2006 interest expense increased \$3.5 million, or 64.93%, over the same period in 2005.

The following table shows an analysis of average earning assets, interest-bearing liabilities and rates and yields. Nonaccrual loans are included in loans outstanding.

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## AVERAGE BALANCE SHEETS , NET INTEREST INCOME\* AND RATES\*

|   | For the quarter ended June 30, |  |                  |                            |  |                  |
|---|--------------------------------|--|------------------|----------------------------|--|------------------|
|   | 2006<br>Average<br>Balance     | 2006<br>Interest<br>Income/<br>Expense | Yield/<br>Rate** | 2006<br>Average<br>Balance | 2005<br>Interest<br>Income/<br>Expense | Yield/<br>Rate** |
| Loans   | \$ 530,477                     | \$ 9,025                               | 6.81%            | \$ 434,467                 | \$ 6,924                               | 6.37%            |
| Investment securities:  |                                |  |                  |                            |  |                  |
| Taxable   | 162,946                        | 1,370                                  | 3.36%            | 164,430                    | 1,363                                  | 3.32%            |
| Tax-exempt  | 31,592                         | 556                                    | 7.04%            | 36,485                     | 644                                    | 7.06%            |
| Total investment securities   | 194,538                        | 1,926                                  | 3.96%            | 200,915                    | 2,007                                  | 4.00%            |
| Federal funds sold  | 6,713                          | 81                                     | 4.83%            | 7,138                      | 50                                     | 2.80%            |
| Total earning assets  | 731,728                        | \$ 11,032                              | 6.03%            | 642,520                    | \$ 8,981                               | 5.59%            |
| Reserve for loan losses   | (4,502)                        |  |                  | (4,112)                    |  |                  |
| Other nonearning assets   | 49,684                         |  |                  | 48,702                     |  |                  |
| Total assets  | \$ 776,910                     |  |                  | \$ 687,110                 |  |                  |
| Time and savings deposits:  |                                |  |                  |                            |  |                  |
| Interest-bearing transaction accounts                               | \$ 9,229                       | \$ 6                                   | 0.26%            | \$ 7,360                   | \$ 5                                   | 0.27%            |
| Money market deposit accounts                                       | 153,455                        | 513                                    | 1.34%            | 144,998                    | 283                                    | 0.78%            |
| Savings accounts  | 41,425                         | 52                                     | 0.50%            | 42,494                     | 55                                     | 0.52%            |
| Time deposits, \$100,000 or more                                    | 85,795                         | 899                                    | 4.19%            | 71,218                     | 541                                    | 3.04%            |
| Other time deposits   | 167,024                        | 1,628                                  | 3.90%            | 142,078                    | 1,057                                  | 2.98%            |
| Total time and savings deposits                                     | 456,928                        | 3,098                                  | 2.71%            | 408,148                    | 1,941                                  | 1.90%            |
| Federal funds purchased, repurchase agreements and other borrowings | 50,904                         | 464                                    | 3.65%            | 52,193                     | 278                                    | 2.13%            |
| Federal Home Loan Bank advances                                     | 97,333                         | 1,154                                  | 4.74%            | 51,223                     | 550                                    | 4.29%            |
| Total interest-bearing liabilities                                  | 605,165                        | 4,716                                  | 3.12%            | 511,564                    | 2,769                                  | 2.17%            |
| Demand deposits   | 98,259                         |  |                  | 103,648                    |  |                  |
| Other liabilities   | 1,936                          |  |                  | 1,466                      |  |                  |
| Stockholders equity   | 71,550                         |  |                  | 70,432                     |  |                  |
| Total liabilities and stockholders equity                           | \$ 776,910                     |  |                  | \$ 687,110                 |  |                  |
| Net interest income/yield   |                                | \$ 6,316                               | 3.45%            |                            | \$ 6,212                               | 3.87%            |

|                             | For the six months ended June 30, |  |                  |                            |  |                  |
|-----------------------------|-----------------------------------|--|------------------|----------------------------|--|------------------|
|                             | 2006<br>Average<br>Balance        | 2006<br>Interest<br>Income/<br>Expense | Yield/<br>Rate** | 2006<br>Average<br>Balance | 2005<br>Interest<br>Income/<br>Expense | Yield/<br>Rate** |
| Loans                       | \$ 518,293                        | \$ 17,343                              | 6.69%            | \$ 433,438                 | \$ 13,695                              | 6.32%            |
| Investment securities:      |                                   |  |                  |                            |  |                  |
| Taxable                     | 163,625                           | 2,745                                  | 3.36%            | 166,790                    | 2,793                                  | 3.35%            |
| Tax-exempt                  | 32,464                            | 1,144                                  | 7.05%            | 37,086                     | 1,317                                  | 7.10%            |
| Total investment securities | 196,089                           | 3,889                                  | 3.97%            | 203,876                    | 4,110                                  | 4.03%            |

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|   |            |           |       |            |           |       |
|---|------------|-----------|-------|------------|-----------|-------|
| Federal funds sold  | 5,703      | 133       | 4.66% | 6,439      | 86        | 2.67% |
| Total earning assets  | 720,085    | \$ 21,365 | 5.93% | 643,753    | \$ 17,891 | 5.56% |
| Reserve for loan losses   | (4,518)    |           |       | (4,144)    |           |       |
| Other nonearning assets   | 49,634     |           |       | 48,926     |           |       |
| Total assets  | \$ 765,201 |           |       | \$ 688,535 |           |       |
| Time and savings deposits:  |            |           |       |            |           |       |
| Interest-bearing transaction accounts                               | \$ 8,892   | \$ 11     | 0.25% | \$ 7,108   | \$ 10     | 0.28% |
| Money market deposit accounts                                       | 152,805    | 950       | 1.24% | 146,287    | 548       | 0.75% |
| Savings accounts  | 41,601     | 103       | 0.50% | 42,792     | 107       | 0.50% |
| Time deposits, \$100,000 or more                                    | 83,786     | 1,676     | 4.00% | 71,422     | 1,030     | 2.88% |
| Other time deposits   | 165,508    | 3,130     | 3.78% | 142,682    | 2,053     | 2.88% |
| Total time and savings deposits                                     | 452,592    | 5,870     | 2.59% | 410,291    | 3,748     | 1.83% |
| Federal funds purchased, repurchase agreements and other borrowings | 50,551     | 872       | 3.45% | 50,974     | 502       | 1.97% |
| Federal Home Loan Bank advances                                     | 91,256     | 2,138     | 4.69% | 52,708     | 1,134     | 4.30% |
| Total interest-bearing liabilities                                  | 594,399    | 8,880     | 2.99% | 513,973    | 5,384     | 2.10% |
| Demand deposits   | 97,390     |           |       | 102,641    |           |       |
| Other liabilities   | 2,142      |           |       | 2,068      |           |       |
| Stockholders' equity  | 71,270     |           |       | 69,853     |           |       |
| Total liabilities and stockholders' equity                          | \$ 765,201 |           |       | \$ 688,535 |           |       |
| Net interest income/yield   |            | \$ 12,485 | 3.47% |            | \$ 12,507 | 3.89% |

\* Computed on a fully taxable equivalent basis using a 34% rate

\*\* Annualized

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### **Provision for Loan Losses**

The provision for loan losses is a charge against earnings necessary to maintain the allowance for loan losses at a level consistent with management's evaluation of the portfolio.

The provision for loan losses was \$600 thousand for the first six months of 2006, up from \$450 thousand in the comparable period in 2005. The increase in the provision was due to strong loan growth and not higher charge offs. Loans charged off (net of recoveries) in the first six months of 2006 were \$499 thousand compared with loans charged off (net of recoveries) of \$574 thousand in the first six months of 2005. On an annualized basis net loan charge offs were 0.18% of total net loans for the first six months of 2006 compared with 0.27% for the same period in 2005.

On June 30, 2006, nonperforming assets totaled \$422 thousand compared with \$585 thousand on June 30, 2005. The June 2006 total consisted of \$257 thousand in nonaccrual loans and \$165 thousand in a former branch site listed for sale. The June 2005 total consisted of \$420 thousand in nonaccrual loans and \$165 thousand in a former branch site listed for sale. Loans still accruing interest but past due 90 days or more decreased to \$356 thousand as of June 30, 2006 compared with \$871 thousand as of June 30, 2005.

The allowance for loan losses on June 30, 2006 was \$4.6 million, compared with \$4.2 million on June 30, 2005. It represented a multiple of 10.78 times nonperforming assets and 17.70 times nonperforming loans. Nonperforming loans includes nonaccrual and restructured loans. The allowance for loan losses was 0.83% and 0.96% of total loans on June 30, 2006 and 2005, respectively.

### **Noninterest Income**

For the second quarter of 2006, noninterest income increased \$473 thousand, or 18.55%, over the same period in 2005. The unwinding of a Federal Home Loan Bank (FHLB) advance contributed to \$237 thousand of this increase. For the six months ended June 30, 2006, noninterest income increased \$755 thousand or 14.93% over the same period in 2005. The growth in noninterest income is attributed to the FHLB advance transaction and increases in service charges on deposit accounts and other service charges, commissions and fees. The increase in service charges on deposit accounts is attributed to the increase of over 6,900 consumer checking accounts as of June 30, 2006. The increase in accounts is related to the bank wide new consumer checking account initiative that began in April 2005. The service charge commissions and fees related income is higher due to an increased volume of debit card transactions. The increased volume of debit card transactions is also related to the bank wide new consumer checking account initiative.

### **Noninterest Expenses**

For the second quarter of 2006, noninterest expenses increased \$564 thousand, or 9.76%, over the second quarter of 2005. For the six months ended June 30, 2006 noninterest expenses increased \$1.2 million or 10.69% over the same period in 2005. For the six months ended June 30, 2006 salaries and employee benefits increased by \$562 thousand, or 8.05% over the same period in 2005 as a result of normal yearly salary increases and an increase of 11 in the Company's full time equivalent (FTE) positions. The staffing increases were due to the opening of two new branches in October 2005 and February 2006.

The increases in the various categories of noninterest expense were directly related to the Company's branch expansion and increase of consumer checking accounts.

The Company anticipates a continued trend of increases in noninterest expense in future periods. Salaries and employee benefits, as well as occupancy expenses, will continue to increase as the Company expands its branch system in the future. The Company also expects increases to back office staffing expense in order to support its growing branch system. In an effort to keep noninterest expense under control, the Board of Directors voted to freeze the Company's pension plan effective September 30, 2006.

### **Balance Sheet Review**

At June 30, 2006, the Company had total assets of \$797.0 million, an increase of 7.71% from \$740.0 million at December 31, 2005. Net loans as of June 30, 2006 were \$544.9 million, an increase of 11.15% from \$490.2 million at December 31, 2005. The Company realized significant growth in the real estate category of loans. Note 3 of the consolidated financial statements details the loan volume by category as of June 30, 2006 and December 31, 2005.



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Average assets as of June 30, 2006 were \$765.2 million compared to \$688.5 million as of June 30, 2005. The growth in assets in 2006 was due to the growth in average loans, which increased 19.58% as compared to the same period in 2005.

Total investment securities at June 30, 2006 were \$189.4 million, a decrease of 3.41% from \$196.1 million on December 31, 2005. The Company's goal is to provide maximum return on the investment portfolio within the framework of its asset/liability objectives. The objectives include managing interest sensitivity, liquidity and pledging requirements. Current growth as noted in the above paragraph has occurred in the loan portfolio. The reduction in investment securities helped fund this loan growth.

At June 30, 2006, total deposits increased to \$556.8 million, up 3.74% from \$536.7 million on December 31, 2005. Deposit growth, especially demand deposit growth is not as strong as Management would like. Management has developed an incentive plan for the second half of 2006 to reverse the slowing pace of noninterest-bearing and savings deposits.

FHLB advances increased to \$115.0 million, an increase of 43.75% from \$80.0 million on December 31, 2005. FHLB advances were used to fund the majority of our loan growth.

**Capital Resources**

Under the banking regulations, Total Capital is composed of core capital (Tier 1) and supplemental capital (Tier 2). Tier 1 capital consists of common stockholders' equity and retained earnings less goodwill. Tier 2 capital consists of certain qualifying debt and a qualifying portion of the allowance for loan losses. The following is a summary of the Company's capital ratios at June 30, 2006. As shown below, these ratios were all well above the regulatory minimum levels.

|                 | <b>2006<br/>Regulatory<br/>Minimums</b> | <b>June 30, 2006</b> |
|-----------------|---|----------------------|
| Tier 1          | 4.00%                                   | 12.86%               |
| Total Capital   | 8.00%                                   | 13.64%               |
| Tier 1 Leverage | 3.00%                                   | 9.63%                |

Quarter-end book value was \$17.94 in 2006 and \$17.65 in 2005. Cash dividends were \$1.4 million or \$0.34 per share in the six months ended June 30, 2006, and \$1.3 million or \$0.32 per share in the six months ended June 30, 2005. The common stock of the Company has not been extensively traded.

**Liquidity**

Liquidity is the ability of the Company to meet present and future financial obligations through either the sale or maturity of existing assets or the acquisition of additional funds through liability management. Liquid assets include cash, interest-bearing deposits with banks, federal funds sold, investments in securities and loans maturing within one year.

In addition, secondary sources are available through the use of borrowed funds if the need should arise. The Company's sources of funds include a large stable deposit base and secured advances from FHLB. As of the end of the second quarter 2006, the Company had \$122.4 million in FHLB borrowing availability. The Company has available short-term unsecured borrowed funds in the form of federal funds with correspondent banks. As of the end of the second quarter 2006, the Company had \$40.0 million available in federal funds to handle any short-term borrowing needs.



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Management is not aware of any market or institutional trends, events or uncertainties that are expected to have a material effect on the liquidity, capital resources or operations of the Company. Nor is management aware of any current recommendations by regulatory authorities that would have a material effect on liquidity, capital resources or operations. The Company's internal sources of such liquidity are deposits, loan and investment repayments and securities available for sale. The Company's primary external source of liquidity is advances from the FHLB of Atlanta.

As a result of the Company's management of liquid assets, availability of borrowed funds and the ability to generate liquidity through liability funding, management believes that the Company maintains overall liquidity sufficient to satisfy its depositors' requirements and to meet its customers' future borrowing needs.

## **Contractual Obligations**

In the normal course of business there are various outstanding contractual obligations of the Company that will require future cash outflows. In addition, there are commitments and contingent liabilities, such as commitments to extend credit that may or may not require cash outflows.

The Company has signed two contracts to purchase property for future branch sites. One contract is for a purchase price of \$1.4 million, which amount will be paid in full at closing in August 2006. The second contract is for \$4.0 million, which will be paid in full at the time of closing, which is currently scheduled for September 2006. As of June 30, 2006, there have been no other material changes outside the ordinary course of business in the Company's contractual obligations disclosed in the Company's annual report on Form 10-K for the year ended December 31, 2005.

## **Off-Balance Sheet Arrangements**

As of June 30, 2006, there were no material changes in the Company's off-balance sheet arrangements disclosed in the Company's annual report on Form 10-K for the year ended December 31, 2005.

## **Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

An important element of earnings performance and the maintenance of sufficient liquidity is proper management of the interest sensitivity gap and liquidity gap. The interest sensitivity gap is the difference between interest sensitive assets and interest sensitive liabilities in a specific time interval. This gap can be managed by repricing assets or liabilities, which are variable rate instruments, by replacing an asset or liability at maturity or by adjusting the interest rate during the life of the asset or liability. Matching the amounts of assets and liabilities maturing in the same time interval helps to hedge interest rate risk and to minimize the impact of rising or falling interest rates on net interest income.

The Company determines the overall magnitude of interest sensitivity risk and then formulates policies governing asset generating and pricing, funding sources and pricing, and off-balance sheet commitments. These decisions are based on management's expectations regarding future interest rate movements, the state of the national and regional economy, and other financial and business risk factors. The Company uses computer simulations to measure the effect of various interest rate scenarios on net interest income. This modeling reflects interest rate changes and the related impact on net interest income and net income over specified time horizons.

Based on scheduled maturities only, the Company was liability sensitive as of June 30, 2006. It should be noted, however, that non-maturing deposit liabilities totaling \$200.1 million, which consist of interest checking, money market, and savings accounts, are less interest sensitive than other market driven deposits. In a rising rate environment these deposit rates have historically lagged behind the changes in earning asset rates, thus mitigating the impact from the liability sensitivity position. The asset/liability model allows the Company to reflect the fact that non-maturing deposits are less rate sensitive than other deposits by using a decay rate. The decay rate is a type of artificial maturity that simulates maturities for non-maturing deposits over the number of months that more closely reflects historic data. Using the decay rate, the model reveals that the Company is fairly balanced between assets and liabilities.

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When the Company is asset sensitive, net interest income should improve if interest rates rise since assets will reprice faster than liabilities. Conversely, if interest rates fall, net interest income should decline, depending on the optionality (prepayment speeds) of the assets. When the Company is liability sensitive, net interest income should fall if rates rise and rise if rates fall.

The most likely scenario represents the rate environment as management forecasts it to occur. From this base, rate shocks in 100 basis point increments are applied to see the impact on the Company's earnings. The rate shock model reveals that a 100 basis point decrease in rates would cause an approximately 2.21% decrease in net income. The rate shock model reveals that a 100 basis point rise in rates would cause an approximately 0.13% decrease in net income and that a 200 basis point rise in rates would cause an approximately 0.14% increase in net income at June 30, 2006.

### **Item 4. Controls and Procedures.**

The Company maintains a system of disclosure controls and procedures that is designed to ensure that material information is accumulated and communicated to management, including the Company's Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions to be made regarding required disclosure. As required, management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were operating effectively to ensure that information required to be disclosed by the Company in reports that it files or submits under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the SEC.

The Company's management is also responsible for establishing and maintaining adequate internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. No changes in the Company's internal control over financial reporting occurred during the fiscal quarter ended June 30, 2006 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

The Company's management, including the Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal controls will prevent all error and fraud. A control system, no matter how well conceived and operated, provides reasonable, not absolute, assurance that the objectives of the control system are met. The design of a control system reflects resource constraints and the benefits of controls must be considered relative to their costs. Because there are inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been or will be detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns occur because of simple error or mistake. Controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls is based in part upon certain assumptions about the likelihood of future events. There can be no assurance that any design will succeed in achieving its stated goals under all future conditions; over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with the policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

**Table of Contents****PART II - OTHER INFORMATION****Item 1. Legal Proceedings.**

There are no pending or threatened legal proceedings to which the Company, or any of its subsidiaries, is a party or to which the property of either the Company or its subsidiaries is subject that, in the opinion of management, may materially impact the financial condition of the Company.

**Item 1A. Risk Factors.**

As of June 30, 2006, there have been no material changes in the risk factors faced by the Company from those disclosed in the Company's annual report on Form 10-K for the year ended December 31, 2005.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

The following table presents the monthly share repurchases during the period ended June 30, 2006:

| Period               | Total<br>Number<br>of Shares<br>Purchased | Average<br>Price Paid<br>Per Share | Total Number<br>of Shares<br>Purchased<br>as Part of the<br>Repurchase<br>Program (1) | Maximum<br>Number of<br>Shares that<br>May Yet Be<br>Purchased<br>Under the<br>Repurchase<br>Program (1) |
|----------------------|---|------------------------------------|---|--|
| 4/1/2006 - 4/30/2006 | 600                                       | 29.30                              | 600   | 168,960  |
| 5/1/2006 - 5/31/2006 |   |                                    |   | 168,960  |
| 6/1/2006 - 6/30/2006 | 600                                       | 29.40                              | 600   | 168,360  |
| Total                | 1,200                                     |                                    | 1,200   |  |

- (1) In replacement of a similar authorization in 2005, on January 10, 2006, the Company authorized a program to repurchase during the current calendar year up to an aggregate of five percent (5%) of the shares of the Company's common stock outstanding as of January 1 of the current calendar year. There is currently no stated expiration date for this program. The Company repurchased 1,200 shares of the Company's common stock during the quarter ended June 30, 2006.

**Item 3. Defaults Upon Senior Securities.**

None.

**Item 4. Submission of Matters to a Vote of Security Holders.**

The Company held its Annual Meeting of Stockholders on April 25, 2006. A quorum of stockholders was present, consisting of a total of 2,937,008.8166 shares, represented in person or by proxy. At the Annual Meeting the stockholders elected the 15 directors listed below to serve as directors of the Company for one-year terms, having received the following votes:

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|                         | <b>For</b>   | <b>Withheld</b> |
|-------------------------|--------------|-----------------|
| James Reade Chisman     | 2,796,879.49 | 140,129.33      |
| Dr. Richard F. Clark    | 2,838,276.49 | 98,732.33       |
| Russell S. Evans, Jr.   | 2,844,226.49 | 92,782.33       |
| Dr. Arthur D. Greene    | 2,844,226.49 | 92,782.33       |
| Gerald E. Hansen        | 2,844,357.49 | 92,651.33       |
| Stephen D. Harris       | 2,844,107.49 | 92,901.33       |
| John Cabot Ishon        | 2,839,851.94 | 97,156.87       |
| Eugene M. Jordan        | 2,839,585.49 | 97,423.33       |
| John B. Morgan, II      | 2,844,107.49 | 92,901.33       |
| Louis G. Morris         | 2,841,085.49 | 95,923.33       |
| Robert L. Riddle        | 2,842,307.49 | 94,701.33       |
| Dr. H. Robert Schappert | 2,840,773.33 | 96,235.48       |
| Robert F. Shuford       | 2,833,875.49 | 103,133.33      |
| Ellen Clark Thacker     | 2,836,757.49 | 100,251.33      |
| Melvin R. Zimm          | 2,841,807.49 | 95,201.33       |

No other matters were voted on during the 2006 Annual Meeting.

**Item 5. Other Information.**

(b) The Company has made no changes to the procedures by which security holders may recommend nominees to its board of directors.

**Item 6. Exhibits.**

Exhibits

| <b>Exhibit No.</b> | <b>Description</b>   |
|--------------------|--|
| 3.1                | Articles of Incorporation of Old Point Financial Corporation, as amended April 25, 1995 (incorporated by reference to Exhibit 3 to Form 10-K filed March 26, 1999) |
| 3.2                | Bylaws of Old Point Financial Corporation, as amended August 11, 1992 (incorporated by reference to Exhibit 3 to Form 10-K filed March 26, 1999)                   |
| 31.1               | Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002   |
| 31.2               | Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002   |
| 32.1               | Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002                                     |

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**OLD POINT FINANCIAL CORPORATION**

August 4, 2006

/s/ Robert F. Shuford  
Robert F. Shuford  
President and Chief Executive Officer

(principal executive officer)

August 4, 2006

/s/ Laurie D. Grabow  
Laurie D. Grabow  
Senior Vice President and CFO

(principal financial and accounting officer)