

F&M BANK CORP
Form 10-Q
November 16, 2009

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549
FORM 10-Q**

**Quarterly report Under Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended September 30, 2009.**

**Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
Commission File Number: 000-13273
F & M BANK CORP.**

Virginia

54-1280811

(State or Other Jurisdiction of
Incorporation or Organization)

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

P. O. Box 1111
Timberville, Virginia 22853
(Address of Principal Executive Offices) (Zip Code)
(540) 896-8941
(Registrant's Telephone Number, Including Area Code)

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

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

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

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

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

Class
Common Stock, par value \$5

Outstanding at November 1, 2009
2,294,433 shares

F & M BANK CORP.
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Part I Financial Information
Item 1 Financial Statements

F & M BANK CORP.
CONSOLIDATED STATEMENTS OF INCOME
(In Thousands of Dollars Except per Share Amounts)
(Unaudited)

	Three Months Ended	
	September 30,	
	2009	2008
<i>Interest Income</i>		
Interest and fees on loans held for investment	\$ 6,302	\$ 6,125
Interest and fees on loans held for sale	259	65
Interest on federal funds sold	3	17
Interest on interest bearing deposits	7	24
Dividends on equity securities	61	140
Interest on debt securities	129	246
 Total Interest Income	 6,761	 6,617
<i>Interest Expense</i>		
Interest on demand deposits	355	187
Interest on savings accounts	47	77
Interest on time deposits over \$100,000	477	281
Interest on time deposits	1,024	1,370
 Total interest on deposits	 1,903	 1,915
Interest on short-term debt	9	216
Interest on long-term debt	563	534
 Total Interest Expense	 2,475	 2,665
 Net Interest Income	 4,286	 3,952
 <i>Provision for Loan Losses</i>	 2,790	 120
 Net Interest Income after Provision for Loan Losses	 1,496	 3,832
<i>Noninterest Income</i>		
Service charges	342	367
Insurance and other commissions	104	54
Other	167	272
Income on bank owned life insurance	92	94
Security gains	0	208
Other than temporarily impaired losses	(786)	(520)

Total Noninterest Income	(81)	475
<i>Noninterest Expense</i>		
Salaries	1,349	1,279
Employee benefits	440	396
Occupancy expense	144	145
Equipment expense	165	147
Intangible amortization	69	69
Other	1,082	757
Total Noninterest Expense	3,249	2,793
Income before Income Taxes	(1,834)	1,514
Income Tax expense (benefit)	(978)	428
Minority interest in consolidated subsidiary (earnings) losses	(20)	
Net Income (Loss)	\$ (876)	\$ 1,086
Per Share Data		
Net Income (Loss)	\$ (.38)	\$.47
Cash Dividends	\$.23	\$.23
Weighted Average Shares Outstanding	2,294,275	2,314,827

The accompanying notes are an integral part of these statements.

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F & M BANK CORP.
CONSOLIDATED STATEMENTS OF INCOME
(In Thousands of Dollars Except per Share Amounts)
(Unaudited)

	Nine Months Ended	
	September 30,	
	2009	2008
<i>Interest Income</i>		
Interest and fees on loans held for investment	\$ 18,905	\$ 17,315
Interest and fees on loans held for sale	810	185
Interest on federal funds sold	5	46
Interest on interest bearing deposits	17	99
Dividends on equity securities	165	400
Interest on debt securities	579	734
Total Interest Income	20,481	18,779
<i>Interest Expense</i>		
Interest on demand deposits	870	567
Interest on savings accounts	155	222
Interest on time deposits over \$100,000	1,580	1,345
Interest on time deposits	3,336	3,797
Total interest on deposits	5,941	5,931
Interest on short-term debt	65	402
Interest on long-term debt	1,718	1,389
Total Interest Expense	7,724	7,722
Net Interest Income	12,757	11,057
<i>Provision for Loan Losses</i>	3,310	385
Net Interest Income after Provision for Loan Losses	9,447	10,672
<i>Noninterest Income</i>		
Service charges	943	1,007
Insurance and other commissions	385	223
Other	722	923
Income on bank owned life insurance	272	242
Security gains (losses)	(5)	177
Other than temporarily impaired losses	(1,612)	(520)
Total Noninterest Income	705	2,052

Noninterest Expense

Salaries	3,836	3,773
Employee benefits	1,321	1,122
Occupancy expense	427	422
Equipment expense	433	413
Intangible amortization	207	207
Other	2,907	2,270
Total Noninterest Expense	9,131	8,207

Income before Income Taxes

Income before Income Taxes	1,021	4,517
Income Tax expense (benefit)	(144)	1,283
Minority interest in consolidated subsidiary (earnings) losses	(66)	

Net Income

Net Income	\$ 1,099	\$ 3,234
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Per Share Data

Net Income	\$.48	\$ 1.39
Cash Dividends	\$.69	\$.67
Weighted Average Shares Outstanding	2,290,859	2,327,735

The accompanying notes are an integral part of these statements.

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F & M BANK CORP.
CONSOLIDATED BALANCE SHEETS
(In Thousands of Dollars)

	September 30, 2009 (Unaudited)	December 31, 2008 (Audited)
Assets		
Cash and due from banks	\$ 5,775	\$ 5,687
Federal funds sold	2,411	8,979
Cash and cash equivalents	8,186	14,666
Interest bearing deposits in banks	63	1,162
Securities:		
Held to maturity fair value of \$110,000 in 2009 and 2008 (note 2)	110	110
Available for sale (note 2)	16,935	22,237
Other investments	9,031	8,439
Loans held for sale	22,215	3,780
Loans held for investment (note 3)	426,763	399,233
Less allowance for loan losses (note 4)	(4,700)	(2,189)
Net loans held for investment	422,063	397,044
Bank premises and equipment	7,182	7,457
Interest receivable	1,863	2,056
Core deposit intangible	391	598
Goodwill	2,670	2,670
Bank owned life insurance	6,520	6,304
Other assets	5,896	5,535
Total assets	\$ 503,125	\$ 472,058
Liabilities		
Deposits:		
Noninterest bearing	\$ 51,250	\$ 49,786
Interest bearing:		
Demand	64,394	39,773
Money market accounts	22,822	22,779
Savings	33,884	29,367
Time deposits over \$100,000	77,762	63,855
All other time deposits	138,814	136,665
Total deposits	388,926	342,225
Short-term debt	4,022	20,510

Accrued liabilities	7,332	7,687
Subordinated Debt	875	
Long-term debt	64,152	65,331
Total liabilities	465,307	435,753
Minority interest in consolidated subsidiary	113	47
Stockholders Equity		
Common stock, \$5 par value, 6,000,000 shares authorized, 2,294,340 and 2,289,497 shares issued and outstanding in 2009 and 2008, respectively	11,472	11,447
Retained earnings	27,468	27,687
Accumulated other comprehensive loss	(1,235)	(2,876)
Total stockholders equity	37,705	36,258
Total liabilities and stockholders equity	\$ 503,125	\$ 472,058

The accompanying notes are an integral part of these statements.

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F & M BANK CORP.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands of Dollars)
(Unaudited)

	Nine Months Ended	
	September 30,	
	2009	2008
<i>Cash Flows from Operating Activities</i>		
Net income	\$ 1,099	\$ 3,234
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	488	468
Amortization (accretion) of security premiums (discounts)	26	(29)
Net (increase) decrease in loans held for sale	(18,434)	
Provision for loan losses	3,310	385
Intangible amortization	207	207
(Increase) decrease in interest receivable	193	47
(Increase) decrease in other assets	426	640
Increase in accrued expenses	(1,096)	(606)
(Gain) loss on security transactions	1,617	343
Amortization of limited partnership investments	277	335
Income from life insurance investment	(216)	(223)
Net Adjustments	(13,202)	1,567
Net Cash Provided (Used) by Operating Activities	(12,103)	4,801
<i>Cash Flows from Investing Activities</i>		
Purchase of investments available for sale	(6,948)	(19,449)
Proceeds from sales of investments available for sale	12,097	20,393
Proceeds from maturity of investments available for sale	16	1,010
Net increase in loans held for investment	(28,843)	(64,879)
Purchase of property and equipment	(212)	(734)
Net (increase) decrease in interest bearing bank deposits	1,099	397
Net Cash Used in Investing Activities	(22,801)	(63,262)
<i>Cash Flows from Financing Activities</i>		
Net change in demand and savings deposits	30,645	9,003
Net change in time deposits	16,056	15,780
Net change in short-term debt	(16,489)	10,935
Cash dividends paid	(1,587)	(1,561)
Repurchase of common stock	(54)	(1,536)
Change in federal funds purchased		(2,932)
Proceeds of long-term debt	13,275	42,000
Proceeds from issuance of common stock	157	118

Repayment of long-term debt	(13,579)	(7,929)
Net Cash Provided (Used) by Financing Activities	28,424	63,878
<i>Net Decrease (Increase) in Cash and Cash Equivalents</i>	(6,480)	5,417
<i>Cash and Cash Equivalents, Beginning of Period</i>	14,666	8,706
<i>Cash and Cash Equivalents, End of Period</i>	\$ 8,186	\$ 14,123

Supplemental Disclosure

Cash paid for:

Interest expense	\$ 7,904	\$ 7,952
Income taxes	620	700

The accompanying notes are an integral part of these statements.

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F & M BANK CORP.
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY
(In Thousands of Dollars)
(Unaudited)

	Nine Months Ended September 30,	
	2009	2008
<i>Balance, beginning of period, as previously stated</i>	\$ 36,258	\$ 39,165
Cumulative effect of initial adoption of ASC Topic 715 (formerly FAS 106)		(428)
<i>Balance, beginning of period, restated</i>	\$ 36,258	\$ 38,737
Comprehensive Income		
Net income	1,099	3,234
Net change in unrealized appreciation on securities available for sale, net of taxes (Note 1)	1,642	(710)
Total comprehensive income	2,741	2,524
Repurchase of common stock	(54)	(1,536)
Common stock sold	157	118
Dividends declared	(1,397)	(1,569)
<i>Balance, end of period</i>	\$ 37,705	\$ 38,274

The accompanying notes are an integral part of these statements.

Table of Contents**F & M BANK CORP.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****NOTE 1 ACCOUNTING PRINCIPLES:**

The consolidated financial statements include the accounts of F & M Bank Corp. and its subsidiaries (the Company). Significant intercompany accounts and transactions have been eliminated in consolidation.

The consolidated financial statements conform to accounting principles generally accepted in the United States and to general industry practices. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly the financial position as of September 30, 2009 and the results of operations for the nine month periods ended September 30, 2009 and September 30, 2008. The notes included herein should be read in conjunction with the notes to financial statements included in the 2008 annual report to stockholders of the F & M Bank Corp.

The Company does not expect the anticipated adoption of any newly issued accounting standards to have a material impact on future operations or financial position.

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities and gains or losses on certain derivative contracts, are reported as a separate component of the equity section of the balance sheet. Such items, along with operating net income, are components of comprehensive income.

The components of other comprehensive income and related tax effects are as follows:

	September 30, 2009	December 31, 2008
Changes in:		
Net Income	\$ 1,099,027	\$ 3,204,015
Adjustment for initial adoption of ASC 715		
Funded Status Adjustment		(1,835,082)
Tax effect		623,928
Pension plan adjustment, net of tax		(1,211,154)
Unrealized holding gains (losses) on available-for-sale securities:	758,466	(2,742,769)
Other than temporary impairment losses	1,612,355	1,758,730
Reclassification adjustment for (gains) losses realized in income	4,899	(78,173)
Net unrealized gains (losses)	2,375,720	(1,062,212)
Tax effect	734,179	361,152
Unrealized holding gain (losses), net of tax	1,641,541	(701,060)
Net change in other comprehensive income	\$ 2,740,568	\$ 1,291,801

Subsequent Events

In preparing these financial statements, the Company has evaluated events and transactions for potential recognition or disclosure through November 13, 2009, the date the financial statements were issued.

Table of Contents**F & M BANK CORP.****NOTES TO CONSOLIDATED FINANCIAL STATEMENT****NOTE 2 INVESTMENT SECURITIES:**

The amounts at which investment securities are carried in the consolidated balance sheets and their approximate market values at September 30, 2009 and December 31, 2008 are as follows (in thousands):

	2009		2008	
	Cost	Market Value	Cost	Market Value
Securities Held to Maturity				
U. S. Treasury and agency obligations	\$ 110	\$ 110	\$ 110	\$ 110
Total	\$ 110	\$ 110	\$ 110	\$ 110

	2009		2008	
	Cost	Market Value	Cost	Market Value
Securities Available for Sale				
Government sponsored enterprises	\$ 5,977	\$ 6,018	\$ 10,013	\$ 10,194
Equity securities	3,886	3,724	5,430	3,064
Mortgage-backed securities	6,418	6,715	8,391	8,573
Corporate Bonds	281	478	281	281
Municipals			125	125
Total	\$ 16,562	\$ 16,935	\$ 24,240	\$ 22,237

The amortized cost and fair value of securities at September 30, 2009, by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Securities Held to Maturity		Securities Available for Sale	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	\$ 110	\$ 110	\$ 2,319	\$ 2,315
Due after one year through five years			3,978	4,020
Due after five years			6,379	6,876
Marketable equities	110	110	12,676	13,211
Total	\$ 110	\$ 110	\$ 16,562	\$ 16,935

There were no sales of debt securities during the first three quarters of 2009 or in all of 2008. Following is a table reflecting gains and losses on sales of equity securities:

	2009	2008
Gains	\$	\$ 244
Losses	(5)	(166)
Net Gains (Losses)	\$ (5)	\$ 78

Table of Contents**F & M BANK CORP.****NOTES TO CONSOLIDATED FINANCIAL STATEMENT****NOTE 2 INVESTMENT SECURITIES (CONTINUED):**

The primary purpose of the investment portfolio is to generate income and meet liquidity needs of the Company through readily saleable financial instruments. The portfolio includes fixed rate bonds, whose prices move inversely with rates, variable rate bonds and equity securities. At the end of any accounting period, the investment portfolio has unrealized gains and losses. The Company monitors the portfolio, which is subject to liquidity needs, market rate changes and credit risk changes, to see if adjustments are needed. The primary concern in a loss situation is the credit quality of the business behind the instrument. Bonds deteriorate in value due to credit quality of the individual issuer and changes in market conditions. These losses relate to market conditions and the timing of purchases.

A summary of these losses as of September 30, 2009 (in thousands) is as follows:

	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Government sponsored enterprises	\$	\$	\$	\$	\$	\$
Mortgage backed obligations			317	(3)	317	(3)
Marketable equities	28	(12)	1,334	(331)	1,362	(343)
Total	\$ 28	\$ (12)	\$ 1,651	\$ (334)	\$ 1,679	\$ (346)

The losses above are not considered to be other than temporarily impaired at the end of the period. See page 14 for further discussion.

NOTE 3 LOANS HELD FOR INVESTMENT:

Loans outstanding at September 30, 2009 and December 31, 2008 are summarized as follows:

	2009	2008
Real Estate		
Construction	\$ 86,123	\$ 71,259
Residential	183,795	169,122
Commercial and agricultural	135,743	134,008
Installment loans to individuals	18,866	22,792
Credit cards	2,116	1,940
Other	120	112
Total	\$ 426,763	\$ 399,233

Table of Contents**F & M BANK CORP.****NOTES TO CONSOLIDATED FINANCIAL STATEMENT****NOTE 4 ALLOWANCE FOR LOAN LOSSES:**

A summary of transactions in the allowance for loan losses follows:

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2009	2008	2009	2008
Balance, beginning of period	\$ 2,189	\$ 1,703	\$ 2,556	\$ 1,707
Provisions charged to operating expenses	3,310	385	2,790	120
Net (charge-offs) recoveries:				
Loan recoveries	51	59	22	18
Loan charge-offs	(850)	(327)	(668)	(25)
Total Net Charge-Offs *	(799)	(268)	(646)	(7)
Balance, End of Period	\$ 4,700	\$ 1,820	\$ 4,700	\$ 1,820
* Components of Net Charge-Offs				
Real Estate	(699)	1	(612)	
Commercial	(44)	(260)		
Installment	(56)	(9)	(34)	(7)
Total	\$ (799)	\$ (268)	\$ (646)	\$ (7)

NOTE 5 EMPLOYEE BENEFIT PLAN

The Bank has a qualified noncontributory defined benefit pension plan that covers substantially all of its employees. The benefits are primarily based on years of service and earnings. The following is a summary of net periodic pension costs for the nine-month periods ended September 30, 2009 and 2008.

	2009	2008
Service cost	\$ 269,100	\$ 241,785
Interest cost	204,999	192,162
Expected return on plan assets	(235,284)	(282,534)
Amortization of net obligation at transition		
Amortization of prior service cost	(3,975)	(3,975)
Amortization of net (gain) or loss	93,153	8,841
Net periodic benefit cost	\$ 327,993	\$ 156,279

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F & M BANK CORP.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 FAIR VALUE

FASB Accounting Standards Codification ASC 820 (Topic 820) Fair Value Measures and Disclosures (formerly SFAS No. 157), defines fair value, establishes a framework for measuring fair value, establishes a three-level valuation hierarchy for disclosure of fair value measurement and enhances disclosure requirements for fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

Level 1 Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 Inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement. The following sections provide a description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy:

Securities: Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities would include highly liquid government bonds, mortgage products and exchange traded equities. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics, or discounted cash flow. Level 2 securities would include U.S. agency securities, mortgage-backed agency securities, obligations of states and political subdivisions and certain corporate, asset backed and other securities. In certain cases where there is limited activity or less transparency around inputs to the valuation, securities are classified within Level 3 of the valuation hierarchy. Currently, all of the Company's securities are considered to be Level 2 securities.

Impaired Loans: ASC 820 applies to loans measured for impairment using the practical expedients permitted by ASC 310 Receivables including impaired loans measured at an observable market price (if available), or at the fair value of the loan's collateral (if the loan is collateral dependent). Fair value of the loan's collateral, when the loan is dependent on collateral, is determined by appraisals or independent valuation which is then adjusted for the cost related to liquidation of the collateral.

Other Real Estate Owned: Certain assets such as other real estate owned (OREO) are measured at fair value less cost to sell. We believe that the fair value component in its valuation follows the provisions of ASC 820.

Assets and Liabilities Recorded at Fair Value on a Recurring Basis

The table below presents the recorded amount of assets and liabilities measured at fair value on a recurring basis.

September 30, 2009	Total	Level 1	Level 2	Level 3
Investment securities available-for-sale	\$ 16,935	\$ 4,202	\$ 12,733	
Loans held for sale	22,215		22,215	
Impaired loans	6,966	5,322	1,644	
Other real estate owned	524		524	
Total assets at fair value	46,640	9,524	37,116	

Total liabilities at fair value

There were no assets or liabilities recorded at fair value on a non-recurring basis.

Table of Contents**F & M BANK CORP.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****NOTE 7 DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS:**

ASC 825 Financial Instruments (formerly SFAS 107) defines the fair value of a financial instrument as the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced liquidation or sale. As the majority of the Bank's financial instruments lack an available trading market, significant estimates, assumptions and present value calculations are required to determine estimated fair value. Estimated fair value and the carrying value of financial instruments at September 30, 2009 and December 31, 2008 are as follows (in thousands):

	September 30, 2009		December 31, 2008	
	Estimated Fair Value	Carrying Value	Estimated Fair Value	Carrying Value
<i>Financial Assets</i>				
Cash	\$ 5,775	\$ 5,775	\$ 5,687	\$ 5,687
Interest bearing deposits	63	63	1,164	1,162
Federal funds sold	2,411	2,411	8,979	8,979
Securities available for sale	16,935	16,935	22,237	22,237
Securities held to maturity	110	110	110	110
Other investments	9,031	9,031	8,439	8,439
Loans	449,442	422,063	418,630	399,233
Loan held for sale	22,215	22,215	3,780	3,780
Bank owned life insurance	6,520	6,520	6,304	6,304
Accrued interest receivable	1,863	1,863	2,056	2,056
<i>Financial Liabilities</i>				
Demand Deposits:				
Non-interest bearing	51,250	51,250	49,786	49,786
Interest bearing	87,216	87,216	62,552	62,552
Savings deposits	33,884	33,884	29,367	29,367
Time deposits	218,631	216,576	202,082	200,521
Accrued liabilities	7,332	7,332	7,687	7,687
Short-term debt	4,022	4,022	20,569	20,510
Long-term debt	65,176	65,027	68,846	65,331

The carrying value of cash and cash equivalents, other investments, deposits with no stated maturities, short-term borrowings, and accrued interest approximate fair value. The fair value of securities was calculated using the most recent transaction price or a pricing model, which takes into consideration maturity, yields and quality. The remaining financial instruments were valued based on the present value of estimated future cash flows, discounted at various rates in effect for similar instruments entered into as of the end of each respective period shown above.

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

F & M Bank Corp. (Company), incorporated in Virginia in 1983, is a one-bank holding company pursuant to section 3(a)(1) of the Bank Holding Company Act of 1956, which provides financial services through its wholly-owned subsidiary Farmers & Merchants Bank (Bank). TEB Life Insurance Company (TEB) and Farmers & Merchants Financial Services (FMFS) are wholly-owned subsidiaries of the Bank. Ownership of TEB was transferred from the Company to the Bank during the first quarter of 2009. The Bank also holds a majority ownership in VBS Mortgage LLC (VBS).

The Bank is a full service commercial bank offering a wide range of banking and financial services through its nine branch offices. TEB reinsures credit life and accident and health insurance sold by the Bank in connection with its lending activities. FMFS provides title insurance, brokerage services and property/casualty insurance to customers of the Bank. VBS provides a variety of mortgage products including FHA, VA and VHDA loans. VBS was founded in Harrisonburg, VA in 1999. VBS has two offices, located in Harrisonburg and Broadway Virginia.

The Company's primary trade area services customers in Rockingham County, Shenandoah County, Page County and the northern part of Augusta County.

Management's discussion and analysis is presented to assist the reader in understanding and evaluating the financial condition and results of operations of the Company. The analysis focuses on the consolidated financial statements, footnotes, and other financial data presented. The discussion highlights material changes from prior reporting periods and any identifiable trends which may affect the Company. Amounts have been rounded for presentation purposes. This discussion and analysis should be read in conjunction with the Consolidated Financial Statements and the Notes to the Consolidated Financial Statements presented in Item 1, Part 1 or this Form 10Q.

Forward-Looking Statements

Certain statements in this report may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are statements that include projections, predictions, expectations or beliefs about future events or results or otherwise are not statements of historical fact. Such statements are often characterized by the use of qualified words (and their derivatives) such as expect, believe, estimate, plan, project, or other statements concerning opinions or judgment of the Company and its management about future events.

Although the Company believes that its expectations with respect to certain forward-looking statements are based upon reasonable assumptions within the bounds of its existing knowledge of its business and operations, there can be no assurance that actual results, performance or achievements of the Company will not differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements. Actual future results and trends may differ materially from historical results or those anticipated depending on a variety of factors, including, but not limited to, the effects of and changes in: general economic conditions, the interest rate environment, legislative and regulatory requirements, competitive pressures, new products and delivery systems, inflation, changes in the stock and bond markets, technology, and consumer spending and savings habits.

We do not update any forward-looking statements that may be made from time to time by or on behalf of the Company.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)**
Critical Accounting Policies**General**

The Company's financial statements are prepared in accordance with accounting principles generally accepted in the United States (GAAP). The financial information contained within the statements is, to a significant extent, financial information that is based on measures of the financial effects of transactions and events that have already occurred. A variety of factors could affect the ultimate value that is obtained either when earning income, recognizing an expense, recovering an asset or relieving a liability. The Company uses historical loss factors as one factor in determining the inherent loss that may be present in its loan portfolio. Actual losses could differ significantly from the historical factors that are used. The fair value of the investment portfolio is based on period end valuations but changes daily with the market. In addition, GAAP itself may change from one previously acceptable method to another method. Although the economics of these transactions would be the same, the timing of events that would impact these transactions could change.

Allowance for Loan Losses

The allowance for loan losses is an estimate of the losses that may be sustained in the loan portfolio. The allowance is based on ASC 450 (formerly SFAS No. 5), Contingencies which requires that losses be accrued when occurrence is probable and can be reasonably estimated and ASC 310 (formerly SFAS 114), Receivables which requires that losses be accrued based on the differences between the value of collateral, present value of future cash flows or values that are observable in the secondary market and the loan balance.

Goodwill and Intangibles

ASC 805 Business Combinations and ASC 350 Intangibles requires that the purchase method of accounting be used for all business combinations initiated after September 30, 2001. Additionally, it further clarifies the criteria for the initial recognition and measurement of intangible assets separate from goodwill. ASC 350 prescribes the accounting for goodwill and intangible assets subsequent to initial recognition. The provisions of ASC 350 discontinue the amortization of goodwill and intangible assets with indefinite lives. Instead, these assets will be subject to at least an annual impairment review and more frequently if certain impairment indicators are in evidence. ASC 350 also requires that reporting units be identified for the purpose of assessing potential future impairments of goodwill.

Core deposit intangibles are amortized on a straight-line basis over ten years. The Company adopted ASC 350 on January 1, 2002 and determined that the core deposit intangible will continue to be amortized over the estimated useful life.

Securities Impairment

The Company follows the guidance in ASC 320-10 and SAB Topic 5M, *Other Than Temporary Impairment* in evaluating if these impairments are temporary or other than temporary in nature. This determination is made on an investment by investment basis and includes all available evidence at the time of the determination including the following:

The length of time of impairment;

The extent of the impairment relative to the cost of the investment;

Recent volatility in the market value of the investment;

The financial condition and near-term prospects of the issuer, including any specific events which may impair the earnings potential of the issuer; or

The intent and ability of the Company to hold its investment for a period of time sufficient to allow for any anticipated recovery in market value.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)
Securities Impairment, continued**

The following description provides our revised policies/procedures for the evaluation for Other Than Temporary Impairment (OTTI) for the quarter ended September 30, 2009 and for subsequent periods:

We will begin our evaluation using a default position that OTTI has occurred and then use all available evidence to determine whether prospects for the individual security are sufficient to support temporary impairment at the date of the SEC filing. This evaluation will be conducted at each filing date.

For purposes of determining OTTI, the security value recovery period will be projected for a maximum of a two year holding period. This will be the maximum; a shorter period may be used when there are particular conditions related to the individual security which make recovery unlikely.

The primary focus in determining whether a security is OTTI, and projecting potential recovery, will be the prospects for the individual security, rather than broad market indices. All available evidentiary material will be considered, including the Company's public filings with the SEC, press releases, analyst reports, etc.

Secondary consideration will be given to historic returns, but only to the extent that this evidence is instructive in determining whether the individual security has shown a history of outperforming (or underperforming) the market (or industry) in prior economic cycles. This factor would only be considered when the declines in value were not limited to the individual security, but were prevalent over the broader market. This measure will be considered to aid in determining whether OTTI should be recognized earlier, rather than later (ie. a security which underperforms relative to the industry or market will result in early recognition of OTTI). In no event will OTTI recognition be delayed beyond the two year projection period.

OTTI may be recognized as early as Q1, regardless of holding period projections, when there are specific factors relative to the security which make recovery unlikely. These factors could include evidence contained in the aforementioned SEC filings, press releases, analyst reports, but may also be based on the severity of the impairment.

Situations where a security has declined in value more rapidly than the industry (or market), absent strong evidence supporting prospects for recover, will result in OTTI being recognized in Q1 or Q2 rather than continuing to evaluate the security over several quarters, based on holding period projections.

Results of Operations**Net Income**

Net loss for the third quarter of 2009 was \$876,000 or \$.38 per share, compared to net income of \$1,086,000 or \$.47 per share in the second quarter of 2008. Noninterest income, exclusive of securities transactions, decreased 10.42% and noninterest expense increased 16.33% during the same period.

Earnings from Bank Operations are reflected in table below, these represent the core earnings from banking operations for the first nine months of 2009 and 2008, respectively. These amounts are exclusive of gains or losses on the Parent's equity portfolio and historic rehabilitation credits related to the investment in low income housing projects.

	2009	2008
Net Income from Bank Operations	\$ 1,799	\$ 3,134
Income or loss from Parent Company Activities	(700)	100
Net Income for the year	1,099	3,234

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)**
Net Interest Income

The 2009 year to date tax equivalent net interest margin increased \$1,652,000 or 14.70% compared to the same period in 2008. The yield on earning assets decreased .65%, while the cost of funds decreased .66% compared to the same period in 2008. In response to the economic slowdown, the Federal Reserve's Federal Open Market Committee (FOMC) began lowering short-term interest rate in September 2007. In December 2008, the FOMC lowered the Federal Funds Rate to an historic low of 0 to 25 BP. The Prime Rate, which typically tracks at 3.00% above the Federal Funds Rate, currently stands at 3.25%.

The Interest Sensitivity Analysis on page 24 indicates the Company is in a slightly asset sensitive position in the one year time horizon (1.46%), the recent decrease in rates and asset growth resulted in a .19% decrease in the net interest margin compared to the same period in 2008. This has resulted due to the fact that a large portion of rate sensitive liabilities (primarily interest bearing demand deposits and savings) have reached a virtual rate floor (due to the current level of market rates), while rate sensitive assets continue to reprice at lower rates.

A schedule of the net interest margin for 2009 and 2008 can be found in Table I on page 23.

Provision for Loan Losses

The provision for loan losses for the quarter ended September 30, 2009 was \$2.79 million, an increase of \$2.48 million from the most recent quarter and an increase of \$2.79 million from the same quarter a year ago. Approximately \$1.0 million of the current quarter provision for loan losses related to an increase in the specific reserve on one participation loan to a troubled bank that is at high risk of failure. The increase in the provision for loan losses and the current levels of the allowance for loan losses reflect specific reserves related to nonperforming loans, changes in risk rating on loans, net charge-off activity, loan growth, delinquency trends and other credit risk factors that the Company considers in assessing the adequacy of the allowance for loan losses. The allowance for loan losses as a percentage of the loan portfolio was 1.10% at September 30, 2009, .61% at June 30, 2009, .54% and .47% for the periods ending December 31, 2008 and September 30, 2008, respectively.

Noninterest Income

Noninterest income, exclusive of securities transactions, decreased \$73,000 or 3.05% through September 30, 2009. Items contributing to the decrease include a \$64,000 decrease in service charges, and a \$124,000 decrease in secondary market fees which were offset by a \$162,000 increase in Insurance and other commissions. Revenue from FMFS, TEB Life Insurance Company and VBS Mortgage contributed \$103,000 of the increase in Insurance and other commissions.

Noninterest Expense

Noninterest expense increased \$924,000 (11.26%) in 2009. The increase is the result of a \$262,000 increase in salaries and benefits expense (5.4%). The increase in salaries and benefits is due primarily to increase in pension expense. Exclusive of personnel expenses, other noninterest expenses increased at an annualized rate of 20% in 2009 compared to 2008. Areas that increased include a \$105,000 increase in data processing expense and a \$473,000 increase in FDIC assessment fees.

Data processing expense increased due primarily to the support of our rewards checking products, which have generated approximately \$31 million in new deposits in the last year. The FDIC assessment increased due to an increase in our insured deposits and the accrual for the FDIC special assessment. Operating costs continue to compare very favorably to the peer group. As stated in the most recently available Bank Holding Company Performance Report, the Company's and peer group noninterest expenses averaged 2.36% and 3.51% of average assets, respectively. The Company's operating costs have always compared favorably to the peer group due to an excellent asset to employee ratio and below average facilities costs.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Financial Condition

Federal Funds Sold and Interest Bearing Bank Deposits

The Company's subsidiary bank invests a portion of its excess liquidity in either federal funds sold or interest bearing bank deposits. Federal funds sold offer daily liquidity and pay market rates of interest that at quarter end was benchmarked at .25% by the Federal Reserve. Actual rates received vary slightly based upon money supply and demand among banks. Interest bearing bank deposits are held either in money market accounts or as short-term certificates of deposits. Combined balances in federal funds sold and interest bearing bank deposits have decreased due to growth in the loan portfolio.

Securities

The Company's securities portfolio serves several purposes. Portions of the portfolio are held to assist the Company with liquidity, asset liability management, as security for certain public funds and repurchase agreements and for long-term growth potential.

The securities portfolio consists of investment securities (commonly referred to as securities held to maturity) and securities available for sale. Securities are classified as investment securities when management has the intent and ability to hold the securities to maturity. Investment securities are carried at amortized cost. Securities available for sale include securities that may be sold in response to general market fluctuations, liquidity needs and other similar factors. Securities available for sale are recorded at market value. Unrealized holding gains and losses on available for sale securities are excluded from earnings and reported (net of deferred income taxes) as a separate component of shareholders' equity.

As of September 30, 2009, the market value of securities available for sale exceeded their cost by \$373,000. This includes decreases in the equity securities portfolio held by the Company and an increase in value of government obligations held by the Bank and the equities securities portfolio held by TEB Life Insurance Company. Management has traditionally held debt securities (regardless of classification) until maturity and thus it does not expect the fluctuations in value of these securities to have a direct impact on earnings.

Investments in debt securities have decreased approximately \$6.1 million of 2009. The portfolio is made up of primarily agency and mortgage-backed securities with an average portfolio life of approximately two years. This short average life results in less portfolio volatility and positions the Bank to redeploy assets in response to rising rates. Given the historically low interest rates proceeds from bond maturities and mortgage-backed securities pay downs have been used to support the growth in the loan portfolio. Scheduled maturities for the remainder of 2009 total \$4,124,000 and these bonds have an average yield of approximately 2.74%. Based on current market rates, as these bonds mature, the funds will be reinvested at rates that are significantly lower.

A review of these investments as of September 30, 2009, revealed several securities that were impaired as of quarter end. The write down for the third quarter totaled \$786,000 or \$519,000 net of deferred tax. This results in a year to date write down on equity securities for book purposes of \$1,612,000 or 1,064,000 net of deferred tax. Management continues to re-evaluate the portfolio for impairment on a quarterly basis. The Company also sustained losses of \$5,000 year to date from the sale of securities.

Subsequent to the aforementioned impairment write downs, the Company's equity securities portfolio was \$35,000 above cost at September 30, 2009. The increase in the value of the equities portfolio is spread over a number of asset sectors including holdings in the financial sector. This increase is reflective of, and consistent with, the recent recovery in stock market prices. To minimize risk the Company holds a diversified portfolio of equity investments in a number of large, regional financial institutions and a variety of other predominantly blue-chip securities. Management continues to believe that these investments offer adequate current returns (dividends) and have the potential for future increases in value.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)**
Loan Portfolio

The Company operates in a predominately rural area that includes the counties of Rockingham, Page and Shenandoah in the western portion of Virginia. The local economy benefits from a variety of businesses including agri-business, manufacturing, service businesses and several universities and colleges. The Bank is an active residential mortgage and residential construction lender and generally makes commercial loans to small and mid size businesses and farms within its primary service area.

The allowance for loan losses (see subsequent section) provides for the risk that borrowers will be unable to repay their obligations and is reviewed quarterly for adequacy. The risk associated with real estate and installment notes to individuals is based upon employment, the local and national economies and consumer confidence. All of these affect the ability of borrowers to repay indebtedness. The risk associated with commercial lending is substantially based on the strength of the local and national economies.

While lending is geographically diversified within the service area, the Company does have loan concentrations, defined as loans that are 25% or more of Tier II capital (Tier I Capital plus Allowance for Loan and Lease Losses and Subordinated Debt), in agricultural (primarily poultry farming), construction (real estate development and spec housing), hotels, bank holding companies, assisted living facilities and multi-family residential properties. Management and the Board of Directors review these concentrations quarterly. During the first nine months of 2009 the total loan portfolio increased \$27,530,000.

Nonperforming loans include nonaccrual loans, loans 90 days or more past due and restructured loans. Nonaccrual loans are loans on which interest accruals have been suspended or discontinued permanently. Restructured loans are loans which have had the original interest rate or repayment terms changed due to financial hardship. Nonperforming loans totaled \$8,017,000 at September 30, 2009 compared to \$3,689,000 at September 30, 2008. Approximately 77% of these past due loans are secured by real estate. Although management expects that there will be some loan losses, the bank is generally well secured and continues to actively work with its customers to effect payment. As of September 30, 2009, the Company holds \$524,000 of real estate which was acquired through foreclosure. The following is a summary of information pertaining to risk elements and impaired loans:

	September 30, 2009	June 30, 2009	March 31, 2009	December 31, 2008	September 30, 2008
Nonaccrual Loans:					
Real Estate	3,638	1,918	1,518	1,374	1,225
Commercial	1,364	31			
Other					
Loans past due 90 days or more:					
Real Estate	2,550	4,432	2,798	3,205	2,276
Commercial	312	432	497	26	
Other	153	38	148	161	188
Total Nonperforming loans	8,017	6,461	4,961	4,766	3,689
Nonperforming loans as a percentage of loans held for investment	1.88%	1.55%	1.21%	1.19%	.97%
Net Charge Offs to Total Loans	.19%	.04%	.004%	.08%	.07%
	58.63%	39.56%	48.00%	45.93%	49.33%

Allowance for loan and lease losses
to nonperforming loans

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Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)**
Allowance for Loan Losses

Management evaluates the allowance for loan losses on a quarterly basis in light of national and local economic trends, changes in the nature and volume of the loan portfolio and the trend of past due and criticized loans. Specific factors evaluated include internally generated loan review reports, past due reports, historical loan loss experience and changes in the financial strength of individual borrowers that have been included on the Banks watch list or schedule of classified loans.

In evaluating the portfolio, loans are segregated into loans with identified potential losses and pools of loans by type (commercial, residential, consumer, credit cards). Loans with identified potential losses include examiner and bank classified loans. Classified relationships in excess of \$100,000 are reviewed individually for impairment under FAS 114. A variety of factors are taken into account when reviewing these credits including borrower cash flow, payment history, fair value of collateral, company management, the industry in which the borrower is involved and economic factors. Loan relationships that are determined to have no impairment are placed back into the appropriate loan pool and reviewed under FAS 5.

Loan pools are further segmented into watch list, past due over 90 days and all other loans by type. Watch list loans include loans that are 60 days past due, and may include restructured loans, borrowers that are highly leveraged, loans that have been upgraded from classified or loans that contain policy exceptions (term, collateral coverage, etc.). Loss estimates on these loans reflect the increased risk associated with these assets due to any of the above factors. The past due pools contain loans that are currently 90 days or more past due. Loss rates assigned reflect the fact that these loans bear a significantly higher risk of charge-off. Loss rates vary by loan type to reflect the likelihood that collateral values will offset a portion of the anticipated losses.

The remainder of the portfolio falls into pools by type of homogenous loans that do not exhibit any of the above described weaknesses. Loss rates are assigned based on historical loss rates over the prior five years. A multiplier has been applied to these loss rates to reflect the time for loans to season within the portfolio and the inherent imprecision of these estimates.

All potential losses are evaluated within a range of low to high. A general reserve has been established to reflect other unidentified losses within the portfolio. This helps to offset the increased risk of loss associated with fluctuations in past due trends, changes in the local and national economies, and other unusual events. The Board approves the loan loss provision for the following quarter based on this evaluation and an effort is made to keep the actual allowance at or above the midpoint of the range established by the evaluation process.

The allowance for loan losses of \$4,700,000 at September 30, 2009 is equal to 1.10% of loans held for investment. This compares to an allowance of \$1,820,000 at September 30, 2008. Management has funded the allowance a total of \$3,310,000 through September 30, 2009. Net charge-offs year to date total \$799,000.

The overall level of the allowance is somewhat below its peer group average. Management feels this is appropriate based on its loan loss history and the composition of its loan portfolio. Based on historical losses, delinquency rates, collateral values of delinquent loans and a thorough review of the loan portfolio, management is of the opinion that the allowance for loan losses fairly states the estimated losses in the current portfolio.

Deposits and Other Borrowings

The Company's main source of funding is comprised of deposits received from individuals, governmental entities and businesses located within the Company's service area. Deposit accounts include demand deposits, savings, money market and certificates of deposit. Total deposits have increased \$46,701,000 since December 31, 2008. Time deposits increased \$16,056,000 during this period while demand deposits and savings deposits increased \$30,645,000. Certificates of deposit increased as a result of the Bank's membership in the CDARS program. CDARS (Certificate of Deposit Account Registry Service) is a program that allows the bank to accept customer deposits in excess of FDIC limits and through reciprocal agreements with other network participating banks offer FDIC insurance up to as much as \$50 million in deposits. The CDARS program also allows the Bank to purchase funds through its One-Way Buy program. At September 30, 2009 the Bank had obtained a total of \$32,844,000 in CDARS funding. Demand deposits and savings deposits increased as a result of the rewards checking product which has generated approximately \$31 million in new deposits in the last year.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)****Short-term debt**

Short-term debt consists of federal funds purchased, commercial repurchase agreements (repos.) and daily rate credit from the Federal Home Loan Bank (FHLB). With the commercial repos customers deposit operating funds into their checking account and by mutual agreement with the bank their excess funds are swept daily into the repurchase accounts. These accounts are not considered deposits and are not insured by the FDIC. The Bank pledges securities held in its investment portfolio as collateral for these short-term loans. Federal funds purchased are overnight borrowings obtained from the Bank's primary correspondent bank to manage short-term liquidity needs. Daily rate credit from the FHLB has been used to finance loans held for sale and also to finance the increase in short-term residential and commercial construction loans.

Long-term debt

Borrowings from the Federal Home Loan Bank of Atlanta (FHLB) continue to be an important source of funding real estate loan growth. The Company's subsidiary bank borrows funds on a fixed rate basis. These borrowings are used to fund loan growth. By borrowing from the FHLB at various fixed rate terms, the program allows the Bank to match the maturity of its rate real estate portfolio with the maturity of its debt. This reduces the Company's exposure to interest rate changes. Scheduled repayments totaled \$13,579,000 through September 30, 2009. Additional borrowings of \$13,275,000 were obtained to support loan growth and to extend maturities at more favorable longer term rates.

In March 2008, the Company entered into an agreement with a correspondent bank (Silverton Bank) to provide a \$5 million line of credit to be used for general corporate purposes, including capital contributions to the Bank and for the current stock repurchase program. The loan is unsecured and bears a rate of prime minus 1.25%. At September 30, 2009, \$5 million was owed on this line of credit. Subsequent to quarter end the Company entered into an agreement with Page Valley Bank (and several sub-participants) to refinance the Silverton line of credit as a five year, fixed rate, amortizing loan at 6%. This transaction took place on November 2, 2009.

In September 2008 the Company entered into an agreement with Page Valley Bank to provide a \$1 million term loan to be used for a capital contribution to the Bank. The loan is unsecured and bears a rate of prime. Repayment terms include quarterly payments of \$250,000 plus interest beginning in December 2008, at September 30, 2009 the balance on this loan was \$250,000 (paid in full subsequent to quarter end on October 2, 2009).

In August 2009, the Company began to issue Subordinated debt agreements with local investors with terms of 7 to 10 years. Interest rates are fixed on the notes for the full term but vary by maturity. Rates range from 7.0% on the 7 year note to 8.05% on the ten year note. As of September 30, 2009 the balance outstanding was \$875,000.

Capital

The Company seeks to maintain a strong capital base to expand facilities, promote public confidence, support current operations and grow at a manageable level. As of September 30, 2009, the Company's total risk based capital and total capital to total assets ratios were 10.45% and 7.10%, respectively. Both ratios are in excess of regulatory minimums and exceed the ratios of the Company's peers.

Liquidity

Liquidity is the ability 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 and loans maturing within one year. The Company's ability to obtain deposits and purchase funds at favorable rates determines its liquidity exposure. As a result of the Company's management of liquid assets and the ability to generate liquidity through liability funding, management believes that the Company maintains overall liquidity sufficient to satisfy its depositors' requirements and meet its customers' credit needs.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)**

Additional sources of liquidity available to the Company include, but are not limited to, loan repayments, the ability to obtain deposits through the adjustment of interest rates, the purchase of federal funds and funds raised through the CDARS One-Way Buy Program. To further meet its liquidity needs, the Company also maintains lines of credit with correspondent financial institutions. The Company's subsidiary bank also has a line of credit with the Federal Home Loan Bank of Atlanta that allows for secured borrowings.

Interest Rate Sensitivity

In conjunction with maintaining a satisfactory level of liquidity, management must also control the degree of interest rate risk assumed on the balance sheet. Managing this risk involves regular monitoring of interest sensitive assets relative to interest sensitive liabilities over specific time intervals. The Company monitors its interest rate sensitivity periodically and makes adjustments as needed. There are no off balance sheet items that will impair future liquidity.

As of September 30, 2009, the Company had a cumulative Gap Rate Sensitivity Ratio of 1.46 % for the one year repricing period. This generally indicates that earnings would decrease in an increasing interest rate environment as liabilities reprice more quickly than assets. However, in actual practice, this may not be the case as loans tied to the prime rate of interest will reprice immediately with an increase in short term market rates, while deposit rates will remain stable until competitive market conditions dictate the necessity for an increase in rates. Management constantly monitors the Company's interest rate risk and has decided the current position is acceptable for a well-capitalized community bank.

A summary of asset and liability repricing opportunities is shown in Table II, on page 24.

Stock Repurchase

On September 18, 2008, the Company's Board of Directors approved an increase in the number of shares of common stock that the Company can repurchase under the share repurchase program from 150,000 to 200,000 shares. Shares repurchased through September 30, 2009 total 164,132; of this amount, 2,122 shares were repurchased in 2009, at an average cost of \$25.58 per share.

Effect of Newly Issued Accounting Standards

In June 2009, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 168, *The FASB Accounting Standards Codification* and the Hierarchy of Generally Accepted Accounting Principles a replacement of FASB Statement No. 162, (SFAS 168). SFAS 168 establishes the *FASB Accounting Standards Codification*™ (Codification) as the source of authoritative generally accepted accounting principles (GAAP) for nongovernmental entities. The Codification does not change GAAP. Instead, it takes the thousands of individual pronouncements that currently comprise GAAP and reorganizes them into approximately 90 accounting Topics, and displays all Topics using a consistent structure. Contents in each Topic are further organized first by Subtopic, then Section and finally Paragraph. The Paragraph level is the only level that contains substantive content. Citing particular content in the Codification involves specifying the unique numeric path to the content through the Topic, Subtopic, Section and Paragraph structure. FASB suggests that all citations begin with FASB ASC, where ASC stands for *Accounting Standards Codification*.

In conjunction with the issuance of SFAS 168, the FASB also issued its first Accounting Standards Update No. 2009-1, Topic 105 Generally Accepted Accounting Principles (ASU 2009-1) which includes SFAS 168 in its entirety as a transition to the ASC. ASU 2009-1 is effective for interim and annual periods ending after September 15, 2009 and will not have an impact on the Company's financial position or results of operations but will change the referencing system for accounting standards. Certain of the following pronouncements were issued prior to the issuance of the ASC and adoption of the ASUs. For such pronouncements, citations to the applicable Codification by Topic, Subtopic and Section are provided where applicable in addition to the original standard type and number.

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)**

The FASB issued ASU 2009-05, Fair Value Measurements and Disclosures (Topic 820) Measuring Liabilities at Fair Value in August, 2009 to provide guidance when estimating the fair value of a liability. When a quoted price in an active market for the identical liability is not available, fair value should be measured using (a) the quoted price of an identical liability when traded as an asset; (b) quoted prices for similar liabilities or similar liabilities when traded as assets; or (c) another valuation technique consistent with the principles of Topic 820 such as an income approach or a market approach. If a restriction exists that prevents the transfer of the liability, a separate adjustment related to the restriction is not required when estimating fair value. The ASU was effective October 1, 2009 for the Company and will have no impact on financial position or operations.

The FASB issued SFAS 166 (not yet reflected in FASB ASC), Accounting for Transfers of Financial Assets an amendment of FASB Statement No. 140, (SFAS 166) in June 2009. SFAS 166 limits the circumstances in which a financial asset should be derecognized when the transferor has not transferred the entire financial asset by taking into consideration the transferor's continuing involvement. The standard requires that a transferor recognize and initially measure at fair value all assets obtained (including a transferor's beneficial interest) and liabilities incurred as a result of a transfer of financial assets accounted for as a sale. The concept of a qualifying special-purpose entity is removed from SFAS 140 along with the exception from applying FIN 46(R). The standard is effective for the first annual reporting period that begins after November 15, 2009, for interim periods within the first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application is prohibited. The Company does not expect the standard to have any impact on the Company's financial statements.

SFAS 167 (not yet reflected in FASB ASC), Amendments to FASB Interpretation No. 46(R), (SFAS 167) was also issued in June 2009. The standard amends FIN 46(R) to require a company to analyze whether its interest in a variable interest entity (VIE) gives it a controlling financial interest. A company must assess whether it has an implicit financial responsibility to ensure that the VIE operates as designed when determining whether it has the power to direct the activities of the VIE that significantly impact its economic performance. Ongoing reassessments of whether a company is the primary beneficiary is also required by the standard. SFAS 167 amends the criteria to qualify as a primary beneficiary as well as how to determine the existence of a VIE. The standard also eliminates certain exceptions that were available under FIN 46(R). SFAS 167 is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application is prohibited. Comparative disclosures will be required for periods after the effective date. The Company does not expect the standard to have any impact on the Company's financial position.

ASU 2009-12, Fair Value Measurements and Disclosures (Topic 820) Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent), issued in September, 2009, allows a company to measure the fair value of an investment that has no readily determinable fair market value on the basis of the investee's net asset value per share as provided by the investee. This allowance assumes that the investee has calculated net asset value in accordance with the GAAP measurement principles of Topic 946 as of the reporting entity's measurement date. Examples of such investments include investments in hedge funds, private equity funds, real estate funds and venture capital funds. The update also provides guidance on how the investment should be classified within the fair value hierarchy based on the value for which the investment can be redeemed. The amendment is effective for interim and annual periods ending after December 15, 2009 with early adoption permitted. The Company does not have investments in such entities and, therefore, there will be no impact to our financial statements.

Existence of Securities and Exchange Commission Web Site

The Securities and Exchange Commission maintains a Web site that contains reports, proxy and information statements and other information regarding registrants that file electronically with the Commission, including F & M Bank Corp. and the address is (<http://www.sec.gov>).

Table of Contents**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)****TABLE 1**

F & M BANK CORP.
NET INTEREST MARGIN ANALYSIS
(ON A FULLY TAXABLE EQUIVALENT BASIS)
(Dollar Amounts in Thousands)

	Nine Months Ended September 30, 2009			Nine Months Ended September 30, 2008			Three Months Ended September 30, 2009			Three Months Ended September 30, 2008		
	Average Balance	Income/ Expense	Rates	Average Balance	Income/ Expense	Rates	Average Balance	Income/ Expense	Rates	Average Balance	Income/ Expense	Rates
Rate related income												
Loans held for investment ¹	\$ 412,984	\$ 19,001	6.13%	\$ 343,996	\$ 17,412	6.75%	\$ 422,056	\$ 6,331	6.00%	\$ 370,276	\$ 6,159	6.65%
Loans held for sale	27,860	810	3.88%	5,958	185	4.14%	27,576	259	3.76%	6,196	65	4.20%
Federal funds sold	3,515	5	.19%	3,012	46	2.04%	5,874	3	.20%	4,001	17	1.70%
Bank deposits	1,148	16	1.86%	2,712	99	4.87%	1,077			2,058	24	4.66%
Investments Taxable ³	16,268	585	4.79%	19,873	846	5.68%	13,190	140	4.25%	19,365	289	5.97%
Partially taxable ^{2,3}	3,773	197	6.96%	10,091	369	4.88%	3,834	77	8.03%	8,834	125	5.66%
Tax exempt ^{2,3}	51	3	7.84%	184	6	4.35%				125	1	3.20%
Total earning assets	465,599	20,617	5.90%	385,826	18,963	6.55%	473,607	6,810	5.75%	410,855	6,680	6.50%
Interest Expense												
Demand deposits	73,166	869	1.58%	58,053	567	1.30%	81,956	354	1.73%	58,629	187	1.28%
Savings	32,363	155	.64%	30,057	222	.98%	33,996	47	.55%	31,921	77	.96%
Time deposits	216,545	4,917	3.03%	163,867	5,142	4.18%	221,804	1,501	2.71%	165,370	1,651	3.99%
Short-term debt	16,882	65	.51%	24,007	402	2.23%	7,175	9	.50%	38,992	216	2.22%
Long-term debt	67,466	1,718	3.40%	46,962	1,389	3.94%	65,637	563	3.43%	54,007	533	3.95%
	406,422	7,724	2.53%	322,946	7,722	3.19%	410,568	2,474	2.41%	348,919	2,664	3.05%

Total interest bearing liabilities				
Net interest income ¹	12,893	\$ 11,241	\$ 4,336	\$ 4,016
Net yield on interest earning assets ¹	3.69%	3.88%	3.66%	3.91%
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Table of Contents**TABLE II**

F & M BANK CORP.
INTEREST SENSITIVITY ANALYSIS
September 30, 2009
(In Thousands of Dollars)

The following table presents the Company's interest sensitivity.

	0 - 3 Months	4 - 12 Months	1 - 5 Years	Over 5 Years	Not Classified	Total
Uses of Funds						
Loans						
Commercial	\$ 112,235	\$ 18,175	\$ 77,734	\$ 5,180	\$	\$ 213,324
Installment	10,653	863	9,428	3,262		24,206
Real estate for investments	39,758	12,394	117,943	17,022		187,117
Real estate for sale	22,215					22,215
Credit cards	2,116					2,116
Federal funds sold	2,411					2,411
Interest bearing bank deposits	70					70
Investment securities	60	2,366	4,020	6,397	4,202	17,045
Total	189,518	33,798	209,125	31,861	4,202	468,504
Sources of Funds						
Interest bearing demand deposits						
Savings deposits		24,289	50,047	12,879		87,215
Certificates of deposit \$100,000 and over	23,234	34,806	19,723			77,763
Other certificates of deposit	20,173	70,847	47,794			138,814
Short-term borrowings	4,022					4,022
Long-term borrowings	22,771	9,575	31,806	875		65,027
Total	\$ 70,200	\$ 146,294	\$ 169,700	\$ 20,531	\$	\$ 406,725
Discrete Gap	119,318	(112,496)	39,425	11,330	4,202	61,779
Cumulative Gap	119,318	6,822	46,247	57,577	61,779	
Ratio of Cumulative Gap to Total Earning Assets						
	25.47%	1.46%	9.87%	12.29%	13.19%	

Table II reflects the earlier of the maturity or repricing dates for various assets and liabilities as of September 30, 2009. In preparing the above table, no assumptions were made with respect to loan prepayments. Loan principal

payments are included in the earliest period in which the loan matures or can reprice. Principal payments on installment loans scheduled prior to maturity are included in the period of maturity or repricing. Proceeds from the redemption of investments and deposits are included in the period of maturity. Estimated maturities of deposits, which have no stated maturity dates, were derived from guidance contained in FDICIA 305.

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Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not Applicable

Item 4T. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As a result of the enactment of the Sarbanes-Oxley Act of 2002, issuers such as F & M Bank Corp. that file periodic reports under the Securities Exchange Act of 1934 (the Act) are required to include in those reports certain information concerning the issuer's controls and procedures for complying with the disclosure requirements of the federal securities laws. These disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports it files or submits under the Act, is communicated to the issuer's management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

We have established our disclosure controls and procedures to ensure that material information related to the Company is made known to our principal executive officers and principal financial officer on a regular basis, in particular during the periods in which our quarterly and annual reports are being prepared. These disclosure controls and procedures consist principally of communications between and among the Chief Executive Officer and the Chief Financial Officer, and the other executive officers of the Company and its subsidiaries to identify any new transactions, events, trends, contingencies or other matters that may be material to the Company's operations. As required, we will evaluate the effectiveness of these disclosure controls and procedures on a quarterly basis, and most recently did so as of the end of the period covered by this report.

The Company's Chief Executive Officer and Chief Financial Officer, based on their evaluation as of the end of the period covered by this quarterly report of the Company's disclosure controls and procedures (as defined in Rule 13(a)-14(e) of the Securities Exchange Act of 1934), have concluded that the Company's disclosure controls and procedures are adequate and effective for purposes of Rule 13(a)-14(e) and timely, alerting them to financial information relating to the Company required to be included in the Company's filings with the Securities and Exchange Commission under the Securities Exchange Act of 1934.

Changes in Internal Controls

Due to the nature of the Company's business as stewards of assets of customers; internal controls are of the utmost importance. The Company has established procedures during the normal course of business to reasonably ensure that fraudulent activity of either a material amount to these results or in any amount is not occurring. In addition to these controls and review by executive officers, the Company retains the services of an internal auditor to complete regular audits, which examine the processes and procedures of the Company and the Bank to ensure that these processes are reasonably effective to prevent internal or external fraud and that the processes comply with relevant regulatory guidelines of all relevant banking authorities. The findings of the internal auditor are presented to management of the Bank and to the Audit Committee of the Company.

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Part II Other Information

Item 1. Legal Proceedings Not Applicable

Item 1a. Risk Factors There have been no material changes from the risk factors previously disclosed in Item 1a of the Corporation's Form 10k filed on March 23, 2009.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds Not Applicable

Item 3. Defaults Upon Senior Securities Not Applicable

Item 4. Submission of Matters to a Vote of Security Holders Not Applicable

Item 5. Other Information Not Applicable

Item 6. Exhibits

(a) **Exhibits**

- 3 i Restated Articles of Incorporation of F & M Bank Corp. are incorporated by reference to Exhibits to F & M Bank Corp.'s 2001 Form 10K filed August 17, 2007.
- 3 ii Amended and Restated Bylaws of F & M Bank Corp. are incorporated by reference to Exhibits to F & M Bank Corp.'s Form 10K filed March 1, 2002.
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) (filed herewith).
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) (filed herewith).
- 32 Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).

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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.

F & M BANK CORP.

/s/ DEAN W. WITHERS

Dean W. Withers

President and Chief Executive Officer

/s/ NEIL W. HAYSLETT

Neil W. Hayslett

Executive Vice President and Chief
Financial Officer

November 13, 2009

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