

SUMMIT FINANCIAL GROUP INC
Form 10-Q
August 08, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10 – Q

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

For the quarterly period ended June 30, 2014

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 0-16587

Summit Financial Group, Inc.
(Exact name of registrant as specified in its charter)

West Virginia	55-0672148
(State or other jurisdiction	(IRS Employer
of	
incorporation or	Identification No.)
organization)	

300 North Main Street	
Moorefield, West Virginia	26836
(Address of principal	(Zip
executive offices)	Code)

(304) 530-1000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Sections 13 or 15(d) of the Securities and 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

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any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit 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.

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company

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.

Common Stock, \$2.50 par value
7,457,222 shares outstanding as of August 1, 2014

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Summit Financial Group, Inc. and Subsidiaries
Consolidated Balance Sheets (unaudited)

	June 30, 2014	December 31, 2013	June 30, 2013
Dollars in thousands	(unaudited)	(*)	(unaudited)
ASSETS			
Cash and due from banks	\$ 3,749	\$ 3,442	\$ 4,336
Interest bearing deposits with other banks	9,970	8,340	7,971
Cash and cash equivalents	13,719	11,782	12,307
Securities available for sale	287,883	288,780	291,180
Other investments	7,436	7,815	7,411
Loans held for sale, net	413	321	1,080
Loans, net	992,816	937,070	925,979
Property held for sale	48,783	53,392	47,258
Premises and equipment, net	20,301	20,623	20,936
Accrued interest receivable	5,683	5,669	5,718
Intangible assets	7,798	7,949	8,124
Cash surrender value of life insurance policies	36,151	35,611	30,027
Other assets	14,975	17,215	19,950
Total assets	\$ 1,435,958	\$ 1,386,227	\$ 1,369,970
LIABILITIES AND SHAREHOLDERS' EQUITY			
Liabilities			
Deposits			
Non interest bearing	\$ 106,134	\$ 92,837	\$ 92,147
Interest bearing	951,661	910,975	946,016
Total deposits	1,057,795	1,003,812	1,038,163
Short-term borrowings	91,729	62,769	16,762
Long-term borrowings	121,942	163,516	163,565
Subordinated debentures	16,800	16,800	16,800

Subordinated debentures owed to unconsolidated subsidiary trusts	19,589	19,589	19,589
Other liabilities	10,638	8,669	7,880
Total liabilities	1,318,493	1,275,155	1,262,759

Commitments and Contingencies

Shareholders' Equity

Preferred stock and related surplus - authorized 250,000 shares;

Series 2009, 8% Non-cumulative convertible preferred stock, par value \$1.00; issued 3,710 shares	3,519	3,519	3,519
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Series 2011, 8% Non-cumulative convertible preferred stock, par value \$1.00; issued 2014 - 11,914, December 2013 - 11,938 shares, June 2013 - 11,978 shares	5,764	5,776	5,796
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Common stock and related surplus - authorized 20,000,000 shares;

\$2.50 par value; issued and outstanding 2014 - 7,457,222 shares, December 2013 - 7,451,022 shares, and June 2013 - 7,440,222 shares	24,691	24,664	24,593
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Retained earnings	81,569	77,134	72,462
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Accumulated other comprehensive income	1,922	(21)	841
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Total shareholders' equity	117,465	111,072	107,211
Total liabilities and shareholders' equity	\$ 1,435,958	\$ 1,386,227	\$ 1,369,970

(*) - December 31, 2013 financial information has been extracted from audited consolidated financial statements
See Notes to Consolidated Financial Statements

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Summit Financial Group, Inc. and Subsidiaries
Consolidated Statements of Income (unaudited)

	Three Months Ended		Six Months Ended	
	June 30,	June 30,	June 30,	June 30,
Dollars in thousands, except per share amounts	2014	2013	2014	2013
Interest income				
Interest and fees on loans				
Taxable	\$ 12,428	\$ 12,734	\$ 24,572	\$ 25,568
Tax-exempt	87	65	159	135
Interest and dividends on securities				
Taxable	1,199	926	2,481	1,956
Tax-exempt	628	581	1,198	1,215
Interest on interest bearing deposits with other banks	2	2	4	3
Total interest income	14,344	14,308	28,414	28,877
Interest expense				
Interest on deposits	2,335	2,820	4,576	5,588
Interest on short-term borrowings	59	9	112	26
Interest on long-term borrowings and subordinated debentures	1,630	1,975	3,368	4,001
Total interest expense	4,024	4,804	8,056	9,615
Net interest income	10,320	9,504	20,358	19,262
Provision for loan losses	1,000	1,000	2,000	2,500
Net interest income after provision for loan losses	9,320	8,504	18,358	16,762
Other income				
Insurance commissions	1,091	1,132	2,273	2,316
Service fees related to deposit accounts	1,101	1,085	2,144	2,096
Realized securities (losses)	(43)	(57)	(64)	(16)
Other	557	570	1,137	1,134
Total other-than-temporary impairment loss on securities	(1)	(27)	(1)	(117)
Portion of loss recognized in other comprehensive income	-	-	-	37
Net impairment loss recognized in earnings	(1)	(27)	(1)	(80)
Total other income	2,705	2,703	5,489	5,450

Other expense				
Salaries, commissions, and employee benefits	4,045	3,987	8,026	8,105
Net occupancy expense	505	476	1,046	932
Equipment expense	513	559	1,079	1,146
Professional fees	282	360	598	622
Amortization of intangibles	63	88	150	176
FDIC premiums	495	515	997	1,055
Foreclosed properties expense	229	295	482	575
Loss on sale of foreclosed properties	54	523	129	563
Write-down of foreclosed properties	962	1,494	1,891	2,423
Other	1,382	1,241	2,630	2,503
Total other expense	8,530	9,538	17,028	18,100
Income before income taxes	3,495	1,669	6,819	4,112
Income tax expense	1,063	452	1,997	1,102
Net Income	2,432	1,217	4,822	3,010
Dividends on preferred shares	193	194	387	388
Net Income applicable to common shares	\$ 2,239	\$ 1,023	\$ 4,435	\$ 2,622
Basic earnings per common share	\$ 0.30	\$ 0.14	\$ 0.59	\$ 0.35
Diluted earnings per common share	\$ 0.25	\$ 0.13	\$ 0.50	\$ 0.31

See Notes to Consolidated Financial Statements

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Summit Financial Group, Inc. and Subsidiaries
Consolidated Statement of Comprehensive Income (unaudited)

	For the Three Months Ended June 30,		
Dollars in thousands	2014		2013
Net income	\$	2,432	\$ 1,217
Other comprehensive income (loss):			
Net unrealized (loss) on cashflow hedge of (\$1,173), net of deferred taxes of (\$434)		(739)	-
Net unrealized gain (loss) on available for sale debt securities of:			
2014 - \$2,282 net of deferred taxes of \$844 and reclassification adjustment for net realized (losses) included in net income of (\$42); 2013 - (\$6,174), net of deferred taxes of (\$2,346) and reclassification adjustment for net realized (losses) included in net income of (\$57)		1,438	(3,828)
Total comprehensive income (loss)	\$	3,131	\$ (2,611)

	For the Six Months Ended June 30,		
Dollars in thousands	2014		2013
Net income	\$	4,822	\$ 3,010
Other comprehensive income (loss):			
Net unrealized (loss) on cashflow hedge of (\$2,384), net of deferred taxes of (\$882)		(1,502)	-
Non-credit related other-than-temporary impairment on available for sale debt securities - 2014-\$0, net of deferred taxes of \$0; 2013 - \$37, net of deferred		-	(23)

taxes of \$14		
Net unrealized gain		
(loss) on available for		
sale debt securities of:		
2014 - \$5,468 net of deferred taxes of		
\$2,023 d reclassification adjustment		
for net realized (losses) included in net		
income of (\$64); 2013 - (\$6,460), net of		
deferred taxes of (\$2,455) and		
reclassification adjustment for net realized		
(losses) included in		
net income of (\$16)	3,445	(4,005)
Total comprehensive		
income (loss)	\$ 6,765	\$ (1,018)

See Notes to Consolidated Financial Statements

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Summit Financial Group, Inc. and Subsidiaries
Consolidated Statements of Shareholders' Equity (unaudited)

	Series 2009 Preferred Stock and Related Surplus	Series 2011 Preferred Stock and Related Surplus	Common Stock and Related Surplus	Retained Earnings	Accumulated Other Compre- hensive Income	Total Share- holders' Equity
Dollars in thousands, except per share amounts						
Balance, December 31, 2013	\$ 3,519	\$ 5,776	\$ 24,664	\$ 77,134	\$ (21)	\$ 111,072
Six Months Ended June 30, 2014						
Comprehensive income:						
Net income	-	-	-	4,822	-	4,822
Other comprehensive income (loss)					1,943	1,943
Total comprehensive income (loss)						6,765
Exercise of stock options	-	-	15	-	-	15
Stock compensation expense	-	-	-	-	-	-
Series 2009 Preferred Stock cash dividends declared (\$40.00 per share)	-	-	-	(149)	-	(149)
Series 2011 Preferred Stock cash dividends declared (\$20.00 per share)	-	-	-	(238)	-	(238)
Conversion of Series 2011 Preferred Stock to Common Stock	-	(12)	12			
Balance, June 30, 2014	\$ 3,519	\$ 5,764	\$ 24,691	\$ 81,569	\$ 1,922	\$ 117,465
Balance, December 31, 2012						
	\$ 3,519	\$ 5,807	\$ 24,520	\$ 69,840	\$ 4,869	\$ 108,555
Six Months Ended June 30, 2013						
Comprehensive income:						

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Net income	-	-	-	3,010	-	3,010
Other comprehensive income (loss)					(4,028)	(4,028)
Total comprehensive income (loss)						(1,018)
Exercise of stock options	-	-	61	-	-	61
Stock compensation expense	-	-	1	-	-	1
Series 2009 Preferred Stock cash dividends declared (\$40.00 per share)	-	-	-	(148)	-	(148)
Series 2011 Preferred Stock cash dividends declared (\$20.00 per share)	-	-	-	(240)	-	(240)
Conversion of Series 2011 Preferred Stock to Common Stock	-	(11)	11			
Balance, June 30, 2013	\$ 3,519	\$ 5,796	\$ 24,593	\$ 72,462	\$ 841	\$ 107,211

See Notes to Consolidated Financial Statements

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Summit Financial Group, Inc. and Subsidiaries
Consolidated Statements of Cash Flows (unaudited)

Dollars in thousands	Six Months Ended	
	June 30, 2014	June 30, 2013
Cash Flows from		
Operating Activities		
Net income	\$ 4,822	\$ 3,010
Adjustments to		
reconcile net earnings to		
net cash		
provided by		
operating activities:		
Depreciation	547	587
Provision for loan		
losses	2,000	2,500
Stock compensation		
expense	-	1
Deferred income tax		
expense	494	360
Loans originated for		
sale	(960)	(4,624)
Proceeds from loans		
sold	868	3,770
Securities losses	64	16
Other-than-temporary		
impairment of securities	1	80
Loss on disposal of		
assets	129	552
Write down of		
foreclosed properties	1,891	2,423
Amortization of		
securities premiums		
(accretion of discounts),		
net	2,517	3,002
Amortization of		
goodwill and purchase		
accounting		
adjustments, net	155	181
(Increase) in accrued		
interest receivable	(15)	(97)
(Increase) in cash		
surrender value of bank		
owned life insurance	(539)	(474)
(Increase) decrease in		
other assets	(492)	1,009
Increase (decrease) in		
other liabilities	388	(929)
Net cash provided by		
operating activities	11,870	11,367

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Cash Flows from Investing Activities		
Proceeds from maturities and calls of securities available for sale	3,001	1,058
Proceeds from sales of securities available for sale	36,230	29,389
Principal payments received on securities available for sale	16,664	32,768
Purchases of securities available for sale	(52,110)	(79,177)
Purchases of other investments	(1,968)	-
Proceeds from maturities and calls of other investments	-	(643)
Redemption of Federal Home Loan Bank Stock	2,347	4,618
Net principal payments received on loans	(59,716)	5,878
Purchases of premises and equipment	(224)	(393)
Proceeds from disposal of premises and equipment	-	11
Proceeds from sales of other repossessed assets & property held for sale	4,846	8,862
Net cash provided by (used in) investing activities	(50,930)	2,371
Cash Flows from Financing Activities		
Net increase in demand deposit, NOW and savings accounts	64,451	6,123
Net increase (decrease) in time deposits	(10,468)	4,915
Net increase in short-term borrowings	28,960	12,804
Proceeds from long-term borrowings	-	3,454
Repayment of long-term borrowings	(41,574)	(43,202)
Exercise of stock options	15	61
Dividends paid on preferred stock	(387)	(388)
Net cash provided by (used in) financing activities	40,997	(16,233)

Increase (decrease) in cash and cash equivalents	1,937	(2,495)
Cash and cash equivalents:		
Beginning	11,782	14,802
Ending	\$ 13,719	\$ 12,307

(Continued)

See Notes to Consolidated
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Summit Financial Group, Inc. and Subsidiaries
 Consolidated Statements of Cash Flows (unaudited)

Dollars in thousands	Six Months Ended	
	June 30, 2014	June 30, 2013
Supplemental Disclosures of Cash Flow Information		
Cash payments for:		
Interest	\$ 8,294	\$ 9,881
Income taxes	\$ 1,459	\$ 1,081
Supplemental Schedule of Noncash Investing and Financing Activities		
Other assets acquired in settlement of loans	\$ 1,970	\$ 2,811

See Notes to
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Summit Financial Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)

NOTE 1. BASIS OF PRESENTATION

We, Summit Financial Group, Inc. and subsidiaries, prepare our consolidated financial statements in accordance with accounting principles generally accepted in the United States of America for interim financial information and with instructions to Form 10-Q and Regulation S-X. Accordingly, they do not include all the information and footnotes required by accounting principles generally accepted in the United States of America for annual year end financial statements. In our opinion, all adjustments considered necessary for a fair presentation have been included and are of a normal recurring nature.

The presentation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from these estimates.

The results of operations for the quarter ended June 30, 2014 are not necessarily indicative of the results to be expected for the full year. The consolidated financial statements and notes included herein should be read in conjunction with our 2013 audited financial statements and Annual Report on Form 10-K. Certain accounts in the consolidated financial statements for December 31, 2013 and June 30, 2013, as previously presented, have been reclassified to conform to current year classifications.

NOTE 2. SIGNIFICANT NEW AUTHORITATIVE ACCOUNTING GUIDANCE

ASU 2013-11, Income Taxes (Topic 740) - Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists requires that an unrecognized tax benefit, or a portion of an unrecognized tax benefit, be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward. However, if a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. The amendments were effective for years, and interim periods within those years, beginning after December 15, 2013. The amendments did not have a material impact on our consolidated financial statements.

ASU 2014-01, Investments (Topic 323) - Accounting for Investments in Affordable Housing Projects revises the necessary criteria that need to be met in order for an entity to account for investments in affordable housing projects net of the provision for income taxes. It also changes the method of recognition from an effective amortization approach to a proportional amortization approach. Additional disclosures were also set forth in this update. The amendments are effective for annual periods, and interim reporting periods within those annual periods, beginning after December 15, 2014. The amendments are required to be applied retrospectively to all periods presented. Early adoption is permitted. Management is currently evaluating the impact of the guidance on our consolidated financial statements.

ASU 2014-04, Receivables (Topic 310) - Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure clarifies that an in substance repossession or foreclosure occurs upon either the creditor obtaining legal title to the residential real estate property or the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or

through a similar legal agreement. The amendments are effective for annual periods, and interim reporting periods within those annual periods, beginning after December 15, 2014. The amendments may be adopted using either a modified retrospective transition method or a prospective transition method. Early adoption is permitted. Management does not believe the amendments will have a material impact on our consolidated financial statements.

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Summit Financial Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)

NOTE 3. FAIR VALUE MEASUREMENTS

ASC Topic 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. ASC Topic 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value.

Level 1: Quoted prices (unadjusted) or identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, and other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Accordingly, securities available-for-sale are recorded at fair value on a recurring basis. Additionally, from time to time, we may be required to record other assets at fair value on a nonrecurring basis, such as loans held for sale, and impaired loans held for investment. These nonrecurring fair value adjustments typically involve application of lower of cost or market accounting or write-downs of individual assets.

Following is a description of valuation methodologies used for assets and liabilities recorded at fair value.

Available-for-Sale Securities: Investment securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include mortgage-backed securities issued by government sponsored entities, municipal bonds and corporate debt securities.

Derivative Financial Instruments: Derivative financial instruments are recorded at fair value on a recurring basis. Fair value measurement is based on pricing models run by a third-party, utilizing observable market-based inputs. All future floating cash flows are projected and both floating and fixed cash flows are discounted to the valuation date. As a result, we classify interest rate swaps as Level 2.

Loans Held for Sale: Loans held for sale are carried at the lower of cost or market value. The fair value of loans held for sale is based on what secondary markets are currently offering for portfolios with similar characteristics. As such, we classify loans subject to nonrecurring fair value adjustments as Level 2.

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Summit Financial Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)

Loans: We do not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and an allowance for loan loss is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the original contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment in accordance with ASC Topic 310, Accounting by Creditors for Impairment of a Loan. The fair value of impaired loans is estimated using one of several methods, including collateral value, liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. Prior to January 1, 2014, substantially all impaired loans were valued based upon the fair value of their collateral. Beginning January 1, 2014, only impaired loans internally graded as substandard, doubtful, or loss are evaluated using the fair value of collateral method. In accordance with ASC Topic 310, impaired loans where an allowance is established based on the fair value of collateral requires classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, we record the impaired loan as nonrecurring Level 2. When a current appraised value is not available and there is no observable market price, we record the impaired loan as nonrecurring Level 3. This change in accounting estimate did not have a material impact on our financial condition or results of operations.

When impaired loans are deemed required to be included in the fair value hierarchy, management immediately begins the process of evaluating the estimated fair value of the underlying collateral to determine if a related specific allowance for loan losses or charge-off is necessary. Current appraisals are ordered once a loan is deemed impaired if the existing appraisal is more than twelve months old, or more frequently if there is known deterioration in value. For recently identified impaired loans, a current appraisal may not be available at the financial statement date. Until the current appraisal is obtained, the original appraised value is discounted, as appropriate, to compensate for the estimated depreciation in the value of the loan's underlying collateral since the date of the original appraisal. Such discounts are generally estimated based upon management's knowledge of sales of similar collateral within the applicable market area and its knowledge of other real estate market-related data as well as general economic trends. When a new appraisal is received (which generally are received within 3 months of a loan being identified as impaired), management then re-evaluates the fair value of the collateral and adjusts any specific allocated allowance for loan losses, as appropriate. In addition, management also assigns a discount of 7–10% for the estimated costs to sell the collateral.

Other Real Estate Owned ("OREO"): OREO consists of real estate acquired in foreclosure or other settlement of loans. Such assets are carried on the balance sheet at the lower of the investment in the real estate or its fair value less estimated selling costs. The fair value of OREO is determined on a nonrecurring basis generally utilizing current appraisals performed by an independent, licensed appraiser applying an income or market value approach using observable market data (Level 2). Updated appraisals of OREO are generally obtained if the existing appraisal is more than 18 months old or more frequently if there is a known deterioration in value. However, if a current appraisal is not available, the original appraised value is discounted, as appropriate, to compensate for the estimated depreciation in the value of the real estate since the date of its original appraisal. Such discounts are generally estimated based upon management's knowledge of sales of similar property within the applicable market area and its knowledge of other real estate market-related data as well as general economic trends (Level 3). Upon foreclosure, any fair value adjustment is charged against the allowance for loan losses. Subsequent fair value adjustments are recorded in the period incurred and included in other noninterest expense in the consolidated statements of income.

Assets and Liabilities Recorded at Fair Value on a Recurring Basis

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

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Summit Financial Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)

Dollars in thousands	Balance at June 30, 2014	Fair Value Measurements Using:		
		Level 1	Level 2	Level 3
Available for sale securities				
U.S. Government sponsored agencies	\$ 25,830	\$ -	\$ 25,830	\$ -
Mortgage backed securities:				
Government sponsored agencies	157,555	-	157,555	-
Nongovernment sponsored entities	9,931	-	9,931	-
State and political subdivisions	10,035	-	10,035	-
Corporate debt securities	-	-	-	-
Other equity securities	77	-	77	-
Tax-exempt state and political subdivisions	84,455	-	84,455	-
Total available for sale securities	\$ 287,883	\$ -	\$ 287,883	\$ -
Derivative financial instrument				
Interest rate swaps	\$ -	\$ -	\$ -	

Dollars in thousands	Balance at December 31, 2013	Fair Value Measurements Using:		
		Level 1	Level 2	Level 3
Available for sale securities				
U.S. Government sponsored agencies	\$ 29,657	\$ -	\$ 29,657	\$ -
Mortgage backed securities:				
Government sponsored agencies	155,716	-	155,716	-
Nongovernment sponsored entities	11,819	-	11,819	-
	15,870	-	15,870	-

State and political subdivisions				
Corporate debt securities	3,966	-	3,966	-
Other equity securities				
	77	-	77	-
Tax-exempt state and political subdivisions				
	71,675	-	71,675	-
Total available for sale securities				
	\$ 288,780	\$ -	\$ 288,780	\$ -
Derivative financial instrument				
Interest rate swaps				
	\$ 803	\$ -	\$ 803	

There were no assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the period ended June 30, 2014.

Assets and Liabilities Recorded at Fair Value on a Nonrecurring Basis

We may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis in accordance with U.S. generally accepted accounting principles. These include assets that are measured at the lower of cost or market that were recognized at fair value below cost at the end of the period. Assets measured at fair value on a nonrecurring basis are included in the table below.

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Summit Financial Group, Inc. and Subsidiaries
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Dollars in thousands	Total at June 30, 2014	Fair Value Measurements Using:		
		Level 1	Level 2	Level 3
Residential mortgage loans held for sale				
	\$ 413	\$ -	\$ 413	\$ -
Collateral-dependent impaired loans				
Commercial	\$ -	\$ -	\$ -	\$ -
Commercial real estate	2,119	-	2,119	-
Construction and development	13,079	-	9,918	3,161
Residential real estate	8,540	-	8,526	14
Consumer	4	-	-	4
Total collateral-dependent impaired loans	\$ 23,742	\$ -	\$ 20,563	\$ 3,179
OREO				
Commercial	\$ 110	\$ -	\$ 110	\$ -
Commercial real estate	5,762	-	5,762	-
Construction and development	30,920	-	28,810	2,110
Residential real estate	11,991	-	11,581	410
Total OREO	\$ 48,783	\$ -	\$ 46,263	\$ 2,520

Dollars in thousands	Total at December 31, 2013	Fair Value Measurements Using:		
		Level 1	Level 2	Level 3
Residential mortgage loans held for sale				
	\$ 321	\$ -	\$ 321	\$ -
Collateral-dependent impaired loans				
Commercial	\$ 1,616		\$ 920	\$ 696
Commercial real estate	17,902	-	4,879	13,023
	22,083	-	17,590	4,493

Construction and development				
Residential real estate	14,747	-	8,336	6,411
Consumer	34	-	3	31
Total collateral-dependent impaired loans	\$ 56,382	\$ -	\$ 31,728	\$ 24,654
OREO				
Commercial	\$ -	\$ -	\$ -	\$ -
Commercial real estate	9,903	-	9,903	-
Construction and development	31,610	-	29,993	1,617
Residential real estate	11,879	-	11,847	32
Total OREO	\$ 53,392	\$ -	\$ 51,743	\$ 1,649

ASC Topic 825, Financial Instruments, requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis. The following summarizes the methods and significant assumptions we used in estimating our fair value disclosures for financial instruments.

Cash and cash equivalents: The carrying values of cash and cash equivalents approximate their estimated fair value.

Interest bearing deposits with other banks: The carrying values of interest bearing deposits with other banks approximate their estimated fair values.

Federal funds sold: The carrying values of Federal funds sold approximate their estimated fair values.

Securities: Estimated fair values of securities are based on quoted market prices, where available. If quoted market prices are not available, estimated fair values are based on quoted market prices of comparable securities.

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Summit Financial Group, Inc. and Subsidiaries
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Loans held for sale: The carrying values of loans held for sale approximate their estimated fair values.

Loans: The estimated fair values for loans are computed based on scheduled future cash flows of principal and interest, discounted at interest rates currently offered for loans with similar terms to borrowers of similar credit quality. No prepayments of principal are assumed.

Accrued interest receivable and payable: The carrying values of accrued interest receivable and payable approximate their estimated fair values.

Deposits: The estimated fair values of demand deposits (i.e. non-interest bearing checking, NOW, money market and savings accounts) and other variable rate deposits approximate their carrying values. Fair values of fixed maturity deposits are estimated using a discounted cash flow methodology at rates currently offered for deposits with similar remaining maturities. Any intangible value of long-term relationships with depositors is not considered in estimating the fair values disclosed.

Short-term borrowings: The carrying values of short-term borrowings approximate their estimated fair values.

Long-term borrowings: The fair values of long-term borrowings are estimated by discounting scheduled future payments of principal and interest at current rates available on borrowings with similar terms.

Subordinated debentures: The carrying values of subordinated debentures approximate their estimated fair values.

Subordinated debentures owed to unconsolidated subsidiary trusts: The carrying values of subordinated debentures owed to unconsolidated subsidiary trusts approximate their estimated fair values.

Derivative financial instruments: The fair value of the interest rate swaps is valued using independent pricing models.

Off-balance sheet instruments: The fair values of commitments to extend credit and standby letters of credit are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present credit standing of the counter parties. The amounts of fees currently charged on commitments and standby letters of credit are deemed insignificant, and therefore, the estimated fair values and carrying values are not shown below.

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Summit Financial Group, Inc. and Subsidiaries
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The carrying values and estimated fair values of our financial instruments are summarized below:

Dollars in thousands	June 30, 2014		December 31, 2013	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Financial assets				
Cash and due from banks	\$ 13,719	\$ 13,719	\$ 11,782	\$ 11,782
Securities available for sale	287,883	287,883	288,780	288,780
Other investments	7,436	7,436	7,815	7,815
Loans held for sale, net	413	413	321	321
Loans, net	992,816	1,016,258	937,070	952,592
Accrued interest receivable	5,683	5,683	5,669	5,669
Derivative financial instruments	-	-	803	803
	\$ 1,307,950	\$ 1,331,392	\$ 1,252,240	\$ 1,267,762
Financial liabilities				
Deposits	\$ 1,057,795	\$ 1,082,200	\$ 1,003,812	\$ 1,029,606
Short-term borrowings	91,729	91,729	62,769	62,769
Long-term borrowings	121,942	130,627	163,516	173,863
Subordinated debentures	16,800	16,800	16,800	16,800
Subordinated debentures owed to unconsolidated subsidiary trusts	19,589	19,589	19,589	19,589
Accrued interest payable	1,195	1,195	1,433	1,433
Derivative financial instruments	1,582	1,582	-	-
	\$ 1,310,632	\$ 1,343,722	\$ 1,267,919	\$ 1,304,060

NOTE 4. EARNINGS PER SHARE

The computations of basic and diluted earnings per share follow:

Dollars in thousands, except per share amounts	For the Three Months Ended June 30,					
	2014	Common			2013	Common
	Income	Shares	Per Share	Income	Shares	Per Share
	(Numerator)	(Denominator)	(Share)	(Numerator)	(Denominator)	(Share)
Net income	\$ 2,432			\$ 1,217		
Less preferred stock dividends	(193)			(194)		
Basic EPS	\$ 2,239	7,457,222	\$ 0.30	\$ 1,023	7,438,401	\$ 0.14
Effect of dilutive securities:						
Stock options		9,607			7,568	
Series 2011 convertible preferred stock	119	1,489,250		120	1,499,071	
Series 2009 convertible preferred stock	74	674,545		74	674,545	
Diluted EPS	\$ 2,432	9,630,624	\$ 0.25	\$ 1,217	9,619,585	\$ 0.13

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Dollars in thousands, except per share amounts	For the Six Months Ended June 30,					
	2014	Common			2013	Common
	Income	Shares	Per Share	Income	Shares	Per Share
	(Numerator)	(Denominator)	(Numerator)	(Denominator)	(Denominator)	(Share)
Net income	\$ 4,822			\$ 3,010		
Less preferred stock dividends	(387)			(388)		
Basic EPS	\$ 4,435	7,455,307	\$ 0.59	\$ 2,622	7,435,344	\$ 0.35
Effect of dilutive securities:						
Stock options		9,675			7,496	
Series 2011 convertible preferred stock	238	1,490,228		240	1,499,533	
Series 2009 convertible preferred stock	149	674,545		148	674,545	
Diluted EPS	\$ 4,822	9,629,755	\$ 0.50	\$ 3,010	9,616,918	\$ 0.31

Stock option grants and the convertible preferred shares are disregarded in this computation if they are determined to be anti-dilutive. Our anti-dilutive stock options at June 30, 2014 and 2013 totaled 143,000 shares and 170,500 shares, respectively.

NOTE 5. SECURITIES

The amortized cost, unrealized gains, unrealized losses and estimated fair values of securities at June 30, 2014, December 31, 2013, and June 30, 2013 are summarized as follows:

Dollars in thousands	Amortized Cost	June 30, 2014		Estimated Fair Value
		Unrealized Gains	Unrealized Losses	
Available for Sale				
Taxable debt securities				

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U. S. Government agencies and corporations	\$ 24,998	\$ 885	\$ 53	\$ 25,830
Residential mortgage-backed securities:				
Government-sponsored agencies	155,631	2,921	997	157,555
Nongovernment-sponsored entities	9,555	385	9	9,931
State and political subdivisions				
General obligations	4,532	9	144	4,397
Water and sewer revenues	2,382	7	44	2,345
Other revenues	3,319	7	33	3,293
Corporate debt securities	-	-	-	-
Total taxable debt securities	200,417	4,214	1,280	203,351
Tax-exempt debt securities				
State and political subdivisions				
General obligations	46,859	1,552	204	48,207
Water and sewer revenues	11,868	176	58	11,986
Lease revenues	7,990	54	68	7,976
Lottery/casino revenues	3,832	145	41	3,936
Other revenues	12,205	198	53	12,350
Total tax-exempt debt securities	82,754	2,125	424	84,455
Equity securities	77	-	-	77
Total available for sale securities	\$ 283,248	\$ 6,339	\$ 1,704	\$ 287,883

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Summit Financial Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)

Dollars in thousands	Amortized Cost	December 31, 2013		Estimated Fair Value
		Unrealized Gains	Losses	
Available for Sale				
Taxable debt securities				
U. S. Government agencies				
and corporations	\$ 29,100	\$ 675	\$ 118	\$ 29,657
Residential mortgage-backed securities:				
Government-sponsored agencies				
	155,270	2,019	1,573	155,716
Nongovernment-sponsored entities				
	11,519	321	21	11,819
State and political subdivisions				
General obligations	9,317	-	475	8,842
Water and sewer revenues				
	3,229	-	114	3,115
Other revenues	4,051	4	142	3,913
Corporate debt securities	3,973	24	31	3,966
Total taxable debt securities	216,459	3,043	2,474	217,028
Tax-exempt debt securities				
State and political subdivisions				
General obligations	41,156	675	1,154	40,677
Water and sewer revenues				
	8,996	15	306	8,705
Lease revenues	7,956	-	391	7,565
Lottery/casino revenues	4,443	63	169	4,337
Other revenues	10,527	55	191	10,391
Total tax-exempt debt securities	73,078	808	2,211	71,675
Equity securities	77	-	-	77
Total available for sale securities	\$ 289,614	\$ 3,851	\$ 4,685	\$ 288,780

Dollars in thousands	Amortized Cost	June 30, 2013		Estimated Fair Value
		Unrealized Gains	Losses	
Available for Sale				
Taxable debt securities:				
U. S. Government agencies				
and corporations	\$ 35,605	\$ 1,186	\$ 27	\$ 36,764
Residential mortgage-backed securities:				
	147,738	2,313	1,510	148,541

Government-sponsored agencies				
Nongovernment-sponsored agencies	12,373	326	42	12,657
State and political subdivisions	13,838	2	493	13,347
Corporate debt securities	3,966	27	34	3,959
Total taxable debt securities	213,520	3,854	2,106	215,268
Tax-exempt debt securities:				
State and political subdivisions	76,225	1,647	2,037	75,835
Residential mortgage-backed securities:				
Government-sponsored agencies	-	-	-	-
Total tax-exempt debt securities	76,225	1,647	2,037	75,835
Equity securities	77	-	-	77
Total available for sale securities	\$ 289,822	\$ 5,501	\$ 4,143	\$ 291,180

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Summit Financial Group, Inc. and Subsidiaries
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The below information is relative to the five states where issuers with the highest volume of state and political subdivision securities held in our portfolio are located. We own no such securities of any single issuer which we deem to be a concentration.

Dollars in thousands	Amortized Cost	June 30, 2014 Unrealized		Estimated Fair Value
		Gains	Losses	
California	\$ 17,649	\$ 470	\$ 41	\$ 18,078
West				
Virginia	12,313	242	54	12,501
Illinois	8,941	142	77	9,006
Texas	7,380	368	74	7,674
Pennsylvania	7,298	64	49	7,313

Management performs pre-purchase and ongoing analysis to confirm that all investment securities meet applicable credit quality standards. Prior to July 1, 2013, we principally used credit ratings from Nationally Recognized Statistical Rating Organizations (“NRSROs”) to support analyses of our portfolio of securities issued by state and political subdivisions, as we generally do not purchase securities that are rated below the six highest NRSRO rating categories. Beginning July 1, 2013, in addition to considering a security’s NRSRO rating, we now also assess or confirm through an internal review of an issuer’s financial information and other applicable information that: 1) the issuer’s risk of default is low; 2) the characteristics of the issuer’s demographics and economic environment are satisfactory; and 3) the issuer’s budgetary position and stability of tax or other revenue sources are sound.

The maturities, amortized cost and estimated fair values of securities at June 30, 2014, are summarized as follows:

Dollars in thousands	Available for Sale	
	Amortized Cost	Estimated Fair Value
Due in one year or less	\$ 59,685	\$ 60,630
Due from one to five years	100,747	102,143
Due from five to ten years	25,962	26,503
Due after ten years	96,777	98,530
Equity securities	77	77
	\$ 283,248	\$ 287,883

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The proceeds from sales, calls and maturities of available for sale securities, including principal payments received on mortgage-backed obligations, and the related gross gains and losses realized, for the six months ended June 30, 2014 are as follows:

Dollars in thousands	Proceeds from			Gross realized	
	Sales	Calls and Maturities	Principal Payments	Gains	Losses
Securities available for sale	\$ 36,230	\$ 3,001	\$ 16,664	\$ 550	\$ 614

During the three and six months ended June 30, 2014 and 2013, we recorded other-than-temporary impairment losses on residential mortgage-backed nongovernment sponsored entity securities as follows:

Dollars in thousands	Three Months Ended		Six Months Ended	
	2014	June 30, 2013	2014	June 30, 2013
Total other-than-temporary impairment losses	\$ (1)	\$ (27)	\$ (1)	\$ (117)
Portion of loss recognized in other comprehensive income	-	-	-	37
Net impairment losses recognized in earnings	\$ (1)	\$ (27)	\$ (1)	\$ (80)

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Summit Financial Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)

Activity related to the credit component recognized on debt securities available for sale for which a portion of other-than-temporary impairment was recognized in other comprehensive income for the three and six months ended June 30, 2014 is as follows:

	Three Months Ended June 30, 2014	Six Months Ended June 30, 2014
In thousands	Total	Total
Beginning Balance	\$ (3,021)	\$ (3,021)
Additions for the credit component on debt securities in which other-than-temporary impairment was not previously recognized	(1)	(1)
Securities sold during the period	2,814	2,814
Ending Balance	\$ (208)	\$ (208)

We held 86 available for sale securities having an unrealized loss at June 30, 2014. We do not intend to sell these securities, and it is more likely than not that we will not be required to sell these securities before recovery of their amortized cost bases. We believe that this decline in value is primarily attributable to the lack of market liquidity and to changes in market interest rates and not due to credit quality. Accordingly, no additional other-than-temporary impairment charge to earnings is warranted at this time.

Provided below is a summary of securities available for sale which were in an unrealized loss position at June 30, 2014 and December 31, 2013, including debt securities for which a portion of other-than-temporary impairment has been recognized in other comprehensive income.

	June 30, 2014					
	Less than 12 months		12 months or more		Total	
Dollars in thousands	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Temporarily impaired securities						
Taxable debt securities						
U. S. Government agencies and corporations	\$ 2,448	\$ (6)	\$ 3,396	\$ (47)	\$ 5,844	\$ (53)
Residential mortgage-backed securities:	35,211	(550)	23,421	(447)	58,632	(997)

Government-sponsored agencies							
Nongovernment-sponsored entities	2,598	(9)	86	-	2,684	(9)	
State and political subdivisions:							
General obligations	-	-	4,103	(144)	4,103	(144)	
Water and sewer revenues	-	-	1,836	(44)	1,836	(44)	
Other revenues	1,104	(16)	926	(17)	2,030	(33)	
Corporate debt securities	-	-	-	-	-	-	
Tax-exempt debt securities							
State and political subdivisions:							
General obligations	4,816	(44)	7,572	(160)	12,388	(204)	
Water and sewer revenues	1,070	(21)	2,608	(37)	3,678	(58)	
Lease revenues	-	-	2,529	(68)	2,529	(68)	
Lottery/casino revenues	-	-	1,106	(41)	1,106	(41)	
Other revenues	2,771	(18)	826	(35)	3,597	(53)	
Total temporarily impaired securities	50,018	(664)	48,409	(1,040)	98,427	(1,704)	
Other-than-temporarily impaired securities							
Taxable debt securities							
Residential mortgage-backed securities:							
Nongovernment-sponsored entities	-	-	-	-	-	-	
Total other-than-temporarily impaired securities	-	-	-	-	-	-	
Total	\$ 50,018	\$ (664)	\$ 48,409	\$ (1,040)	\$ 98,427	\$ (1,704)	

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Summit Financial Group, Inc. and Subsidiaries
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Dollars in thousands	December 31, 2013					
	Less than 12 months		12 months or more		Total	
	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Temporarily impaired securities						
Taxable debt securities						
U. S. Government agencies						
and corporations	\$ 10,868	\$ (118)	\$ -	\$ -	\$ 10,868	\$ (118)
Residential						
mortgage-backed securities:						
Government-sponsored						
agencies	55,035	(1,385)	13,249	(188)	68,284	(1,573)
Nongovernment-sponsored						
entities	2,407	(12)	565	(7)	2,972	(19)
State and political						
subdivisions:						
General obligations	4,505	(264)	2,337	(211)	6,842	(475)
Water and sewer revenues	1,309	(31)	1,554	(83)	2,863	(114)
Other revenues	3,142	(142)	-	-	3,142	(142)
Corporate debt securities	2,968	(31)	-	-	2,968	(31)
Tax-exempt debt securities						
State and political						
subdivisions:						
General obligations	19,603	(997)	2,102	(157)	21,705	(1,154)
Water and sewer revenues	5,643	(224)	983	(82)	6,626	(306)
Lease revenues	6,112	(349)	958	(42)	7,070	(391)
Lottery/casino revenues	2,720	(132)	554	(37)	3,274	(169)
Other revenues	8,815	(191)	-	-	8,815	(191)
Total temporarily impaired						
securities	123,127	(3,876)	22,302	(807)	145,429	(4,683)
Other-than-temporarily impaired securities						
Taxable debt securities						
Residential						
mortgage-backed securities:						
Nongovernment-sponsored						
entities	-	-	1	(2)	1	(2)
Total other-than-temporarily						
impaired securities	-	-	1	(2)	1	(2)
Total	\$ 123,127	\$ (3,876)	\$ 22,303	\$ (809)	\$ 145,430	\$ (4,685)

NOTE 6. LOANS

Loans are generally stated at the amount of unpaid principal, reduced by unearned discount and allowance for loan losses. Interest on loans is accrued daily on the outstanding balances. Loan origination fees and certain direct loan origination costs are deferred and amortized as adjustments of the related loan yield over its contractual life. We categorize residential real estate loans in excess of \$600,000 as jumbo loans.

Generally, loans are placed on nonaccrual status when principal or interest is greater than 90 days past due based upon the loan's contractual terms. Interest is accrued daily on impaired loans unless the loan is placed on nonaccrual status. Impaired loans are placed on nonaccrual status when the payments of principal and interest are in default for a period of 90 days, unless the loan is both well-secured and in the process of collection. Interest on nonaccrual loans is recognized primarily using the cost-recovery method. Loans may be returned to accrual status when repayment is reasonably assured and there has been demonstrated performance under the terms of the loan or, if applicable, the terms of the restructured loans.

Commercial-related loans or portions thereof (which are risk-rated) are charged off to the allowance for loan losses when the loss has been confirmed. This determination is made on a case by case basis considering many factors, including the prioritization of our claim in bankruptcy, expectations of the workout/restructuring of the loan and valuation of the borrower's equity. We deem a loss confirmed when a loan or a portion of a loan is classified "loss" in accordance with bank regulatory classification guidelines, which state, "Assets classified loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted".

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Consumer-related loans are generally charged off to the allowance for loan losses upon reaching specified stages of delinquency, in accordance with the Federal Financial Institutions Examination Council policy. For example, credit card loans are charged off by the end of the month in which the account becomes 180 days past due or within 60 days from receiving notification about a specified event (e.g., bankruptcy of the borrower), which ever is earlier. Residential mortgage loans are generally charged off to net realizable value no later than when the account becomes 180 days past due. Other consumer loans, if collateralized, are generally charged off to net realizable value at 120 days past due.

Loans are summarized as follows:

Dollars in thousands	June 30, 2014	December 31, 2013	June 30, 2013
Commercial	\$ 90,096	\$ 88,352	\$ 78,963
Commercial real estate			
Owner-occupied	154,260	149,618	149,660
Non-owner occupied	314,439	280,790	277,773
Construction and development			
Land and land development	64,246	71,453	73,427
Construction	20,902	15,155	7,634
Residential real estate			
Non-jumbo	219,569	212,946	216,759
Jumbo	52,487	53,406	58,567
Home equity	61,248	54,844	53,774
Consumer	19,777	19,889	20,147
Other	6,798	3,276	3,397
Total loans, net of unearned fees	1,003,822	949,729	940,101
Less allowance for loan losses	11,006	12,659	14,122
Loans, net	\$ 992,816	\$ 937,070	\$ 925,979

The following table presents the contractual aging of the recorded investment in past due loans by class as of June 30, 2014 and 2013 and December 31, 2013.

Dollars in thousands	At June 30, 2014					> 90 days and Accruing
	30-59 days	Past Due		Total	Current	
		60-89 days	> 90 days			
Commercial	\$ 33	\$ 363	\$ 396	\$ 792	\$ 89,304	\$ -

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Commercial real estate							
Owner-occupied	642	348	759	1,749	152,511	-	
Non-owner occupied	237	-	234	471	313,968	-	
Construction and development							
Land and land development	142	14	4,860	5,016	59,230	-	
Construction	-	-	-	-	20,902	-	
Residential mortgage							
Non-jumbo	3,198	1,760	2,060	7,018	212,551	-	
Jumbo	707	723	-	1,430	51,057	-	
Home equity	196	36	143	375	60,873	-	
Consumer	452	183	72	707	19,070	-	
Other	-	-	-	-	6,798	-	
Total	\$ 5,607	\$ 3,427	\$ 8,524	\$ 17,558	\$ 986,264	\$ -	

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At December 31, 2013						
Dollars in thousands	30-59 days	Past Due		Total	Current	> 90 days and Accruing
		60-89 days	> 90 days			
Commercial	\$ 74	\$ 34	\$ 1,190	\$ 1,298	\$ 87,054	\$ -
Commercial real estate						
Owner-occupied	328	459	487	1,274	148,344	-
Non-owner occupied	912	115	128	1,155	279,635	-
Construction and development						
Land and land development	1,627	-	8,638	10,265	61,188	-
Construction	-	-	-	-	15,155	-
Residential mortgage						
Non-jumbo	2,708	1,673	1,321	5,702	207,244	-
Jumbo	-	-	-	-	53,406	-
Home equity	588	87	-	675	54,169	-
Consumer	224	82	106	412	19,477	-
Other	-	-	-	-	3,276	-
Total	\$ 6,461	\$ 2,450	\$ 11,870	\$ 20,781	\$ 928,948	\$ -

At June 30, 2013						
Dollars in thousands	30-59 days	Past Due		Total	Current	> 90 days and Accruing
		60-89 days	> 90 days			
Commercial	\$ 144	\$ 55	\$ 1,669	\$ 1,868	\$ 77,095	\$ -
Commercial real estate						
Owner-occupied	85	-	314	399	149,261	-
Non-owner occupied	543	-	899	1,442	276,331	-
Construction and development						
Land and land development	698	-	9,929	10,627	62,800	-
Construction	-	-	60	60	7,574	-
Residential mortgage						

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Non-jumbo	4,086	1,171	2,494	7,751	209,008	-
Jumbo	709	-	9,000	9,709	48,858	-
Home equity	101	26	25	152	53,622	-
Consumer	239	64	63	366	19,781	-
Other	53	-	-	53	3,344	-
Total	\$ 6,658	\$ 1,316	\$ 24,453	\$ 32,427	\$ 907,674	\$ -

Nonaccrual loans: The following table presents the nonaccrual loans included in the net balance of loans at June 30, 2014, December 31, 2013 and June 30, 2013.

Dollars in thousands	6/30/2014	12/31/2013	6/30/2013
Commercial	\$ 416	\$ 1,224	\$ 3,996
Commercial real estate			
Owner-occupied	953	1,953	796
Non-owner occupied	583	365	899
Construction and development			
Land & land development	8,849	12,830	11,445
Construction	-	-	60
Residential mortgage			
Non-jumbo	2,950	2,446	4,333
Jumbo	-	-	9,000
Home equity	339	-	271
Consumer	129	128	92
Total	\$ 14,219	\$ 18,946	\$ 30,892

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Summit Financial Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)

Impaired loans: Impaired loans include the following:

§ Loans which we risk-rate (consisting of loan relationships having aggregate balances in excess of \$2.0 million, or loans exceeding \$500,000 and exhibiting credit weakness) through our normal loan review procedures and which, based on current information and events, it is probable that we will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement. Risk-rated loans with insignificant delays or insignificant short falls in the amount of payments expected to be collected are not considered to be impaired.

§ Loans that have been modified in a troubled debt restructuring.

Both commercial and consumer loans are deemed impaired upon being contractually modified in a troubled debt restructuring. Troubled debt restructurings typically result from our loss mitigation activities and occur when we grant a concession to a borrower who is experiencing financial difficulty in order to minimize our economic loss and to avoid foreclosure or repossession of collateral. Once restructured in a troubled debt restructuring, a loan is generally considered impaired until its maturity, regardless of whether the borrower performs under the modified terms. Although such a loan may be returned to accrual status if the criteria set forth in our accounting policy are met, the loan would continue to be evaluated for an asset-specific allowance for loan losses and we would continue to report the loan in the impaired loan table below.

The table below sets forth information about our impaired loans.

Method Used to Measure Impairment of Impaired Loans				
Dollars in thousands				
Loan Category	6/30/2014	12/31/2013	6/30/2013	Method used to measure impairment
Commerical	\$ 506	\$ 1,864	\$ 7,825	Fair value of collateral
	-	158	162	Discounted cash flow
Commerical real estate				
Owner-occupied	1,924	10,067	12,074	Fair value of collateral
	8,969	2,483	2,657	Discounted cash flow
Non-owner occupied	513	5,832	6,814	Fair value of collateral
	5,236	-	-	Discounted cash flow
Construction and development	14,023	24,625	26,710	

Land & land development				Fair value of collateral
	1,446	644	654	Discounted cash flow
Residential mortgage				
Non-jumbo	3,440	5,516	5,322	Fair value of collateral
	2,592	566	891	Discounted cash flow
Jumbo	6,648	8,768	17,824	Fair value of collateral
	2,073	-	-	Discounted cash flow
Home equity	186	212	213	Fair value of collateral
Consumer	37	47	62	Fair value of collateral
Total	\$ 47,593	\$ 60,782	\$ 81,208	

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Summit Financial Group, Inc. and Subsidiaries
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The following tables present loans individually evaluated for impairment at June 30, 2014, December 31, 2013 and June 30, 2013.

Dollars in thousands	June 30, 2014				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Balance	Interest Income Recognized while impaired
Without a related allowance					
Commercial	\$ 506	\$ 506	\$ -	\$ 506	\$ 35
Commercial real estate					
Owner-occupied	6,287	6,288	-	6,287	248
Non-owner occupied	5,012	5,014	-	5,012	249
Construction and development					
Land & land development	13,853	13,853	-	13,853	293
Construction	-	-	-	-	-
Residential real estate					
Non-jumbo	3,390	3,398	-	3,390	161
Jumbo	7,823	7,828	-	7,823	401
Home equity	186	186	-	186	11
Consumer	38	37	-	38	3
Total without a related allowance	\$ 37,095	\$ 37,110	\$ -	\$ 37,095	\$ 1,401
With a related allowance					
Commercial	\$ -	\$ -	\$ -	\$ -	\$ -
Commercial real estate					
Owner-occupied	4,605	4,605	266	4,605	213
Non-owner occupied	735	735	79	735	79
Construction and development					
Land & land development	1,616	1,616	898	1,616	40
Construction	-	-	-	-	-

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Residential real estate					
Non-jumbo	2,633	2,634	299	2,633	107
Jumbo	893	893	53	893	44
Home equity	-	-	-	-	-
Consumer	-	-	-	-	-
Total with a related allowance					
	\$ 10,482	\$ 10,483	\$ 1,595	\$ 10,482	\$ 483
Total					
Commercial	\$ 32,614	\$ 32,617	\$ 1,243	\$ 32,614	\$ 1,157
Residential real estate					
	14,925	14,939	352	14,925	724
Consumer	38	37	-	38	3
Total	\$ 47,577	\$ 47,593	\$ 1,595	\$ 47,577	\$ 1,884

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Summit Financial Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)

December 31, 2013					
Dollars in thousands	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Balance	Interest Income Recognized while impaired
Without a related allowance					
Commercial	\$ 1,161	\$ 1,167	\$ -	\$ 1,518	\$ 98
Commercial real estate					
Owner-occupied	8,434	8,434	-	7,675	226
Non-owner occupied	5,075	5,077	-	5,110	253
Construction and development					
Land & land development					
Construction	14,732	14,737	-	11,628	325
Residential real estate					
Non-jumbo	3,587	3,595	-	2,858	157
Jumbo	7,862	7,867	-	7,910	405
Home equity	186	186	-	186	11
Consumer	26	27	-	28	1
Total without a related allowance	41,063	41,090	-	36,913	1,476
With a related allowance					
Commercial	855	855	406	1,013	-
Commercial real estate					
Owner-occupied	4,116	4,116	305	3,945	184
Non-owner occupied	747	755	175	515	28
Construction and development					
Land & land development					
Construction	10,532	10,532	3,186	11,310	147
Residential real estate					
Non-jumbo	2,485	2,487	256	2,292	107
Jumbo	900	901	37	906	45
Home equity	27	26	22	27	-
Consumer	20	20	13	9	-

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Total with a related allowance	19,682	19,692	4,400	20,017	511
Total					
Commercial	45,652	45,673	4,072	42,714	1,261
Residential real estate	15,047	15,062	315	14,179	725
Consumer	46	47	13	37	1
Total	\$ 60,745	\$ 60,782	\$ 4,400	\$ 56,930	\$ 1,987

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Summit Financial Group, Inc. and Subsidiaries
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	June 30, 2013				
Dollars in thousands	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Balance	Interest Income Recognized while impaired
Without a related allowance					
Commercial	\$ 6,942	\$ 7,104	\$ -	\$ 8,133	\$ 435
Commercial real estate					
Owner-occupied	9,770	9,774	-	10,638	491
Non-owner occupied	5,396	5,398	-	3,969	199
Construction and development					
Land & land development					
Construction	16,904	16,904	-	16,853	725
Residential real estate					
Non-jumbo	3,250	3,258	-	3,035	120
Jumbo	7,911	7,916	-	9,352	503
Home equity	186	186	-	186	11
Consumer	37	38	-	37	2
Total without a related allowance	\$ 50,396	\$ 50,578	\$ -	\$ 52,203	\$ 2,486
With a related allowance					
Commercial	\$ 874	\$ 883	\$ 387	\$ 565	\$ 4
Commercial real estate					
Owner-occupied	4,957	4,957	741	3,967	186
Non-owner occupied	1,415	1,416	165	1,421	28
Construction and development					
Land & land development					
Construction	10,460	10,460	1,844	10,483	65
Residential real estate					
Non-jumbo	2,952	2,955	307	2,963	141
Jumbo	9,907	9,908	1,044	10,277	45
Home equity	28	27	27	28	-
Consumer	25	24	13	25	2

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Total with a related allowance	\$	30,618	\$ 30,630	\$ 4,528	\$ 29,729	\$ 471
Total						
Commercial	\$	56,718	\$ 56,896	\$ 3,137	\$ 56,029	\$ 2,133
Residential real estate		24,234	24,250	1,378	25,841	820
Consumer		62	62	13	62	4
Total	\$	81,014	\$ 81,208	\$ 4,528	\$ 81,932	\$ 2,957

A modification of a loan is considered a troubled debt restructuring (“TDR”) when a borrower is experiencing financial difficulty and the modification constitutes a concession that we would not otherwise consider. This may include a transfer of real estate or other assets from the borrower, a modification of loan terms, or a combination of both. A loan continues to be classified as a TDR for the life of the loan. Included in impaired loans are TDRs of \$33.2 million, of which \$31.6 million were current with respect to restructured contractual payments at June 30, 2014, and \$34.5 million, of which \$33.6 million were current with respect to restructured contractual payments at December 31, 2013. There were no commitments to lend additional funds under these restructurings at either balance sheet date.

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Summit Financial Group, Inc. and Subsidiaries
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The following table presents by class the TDRs that were restructured during the three and six months ended June 30, 2014 and 2013. Generally, the modifications were extensions of term, modifying the payment terms from principal and interest to interest only for an extended period, or reduction in interest rate. All TDRs are evaluated individually for allowance for loan loss purposes.

dollars in thousands	For the Three Months Ended June 30, 2014			For the Three Months Ended June 30, 2013		
	Number of Modifications	Pre-modification Recorded Investment		Number of Modifications	Pre-modification Recorded Investment	
		Investment	Modification		Investment	Modification
Commercial	3	\$ 82	\$ 86	1	\$ 23	\$ 23
Commercial real estate						
Owner-occupied-		-	-	-	-	-
Non-owner occupied	-	-	-	-	-	-
Construction and development						
Land & land development	-	-	-	-	-	-
Construction	-	-	-	-	-	-
Residential real estate						
Non-jumbo	-	-	-	2	241	241
Jumbo	-	-	-	-	-	-
Home equity	-	-	-	-	-	-
Consumer	-	-	-	-	-	-
Total	3	\$ 82	\$ 86	3	\$ 264	\$ 264

dollars in thousands	For the Six Months Ended June 30, 2014			For the Six Months Ended June 30, 2013		
	Number of Modifications	Pre-modification Recorded Investment		Number of Modifications	Pre-modification Recorded Investment	
		Investment	Modification		Investment	Modification
Commercial	3	\$ 82	\$ 86	1	\$ 23	\$ 23
Commercial real estate						
Owner-occupied-		-	-	-	-	-
Non-owner occupied	-	-	-	-	-	-
Construction and development						
Land & land development	-	-	-	1	49	50
Construction	-	-	-	-	-	-

Residential real estate							
Non-jumbo	-	-	-	2	241	241	
Jumbo	-	-	-	-	-	-	
Home equity	-	-	-	-	-	-	
Consumer	-	-	-	-	-	-	
Total	3	\$ 82	\$ 86	4	\$ 313	\$ 314	

The following table presents defaults during the stated period of TDRs that were restructured during the past twelve months. For purposes of these tables, a default is considered as either the loan was past due 30 days or more at any time during the period, or the loan was fully or partially charged off during the period.

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Summit Financial Group, Inc. and Subsidiaries
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	For the Three Months Ended June 30, 2014		For the Six Months Ended June 30, 2014	
	Number of Defaults	Recorded Investment at Default Date	Number of Defaults	Recorded Investment at Default Date
dollars in thousands				
Commercial	2	\$ 78	2	\$ 78
Commercial real estate				
Owner-occupied-				
Non-owner occupied	-	-	-	-
Construction and development				
Land & land development	1	695	1	698
Construction	-	-	-	-
Residential real estate				
Non-jumbo	2	335	2	334
Jumbo	-	-	-	-
Home equity	-	-	-	-
Consumer	-	-	-	-
Total	5	\$ 1,108	5	\$ 1,110

The following table details the activity regarding TDRs by loan type for the three months and six months ended June 30, 2014, and the related allowance on TDRs.

	For the Three Months Ended June 30, 2014										
	Construction & Land Development		Commercial Real Estate		Residential Real Estate		Consumer		Other		Total
Dollars in thousands	Land & Land Development	Construction	Commercial	Owner Occupied	Non-Owner Occupied	Non-jumbo	Jumbo	Home Equity	sumer	Other	
Troubled debt restructurings											
Balance June 30, 2013	\$ 6,069	\$ -	\$ 509	\$ 9,644	\$ 5,492	\$ 5,513	\$ 6,237	\$ -	\$ 40	\$ -	\$ 33,504
Additions	-	-	86	-	-	-	-	-	-	-	86
Charge-offs	-	-	-	-	-	-	-	-	-	-	-

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Net (paydowns) advances	(101)	-	(97)	(55)	(27)	(19)	(36)	-	(2)	-	(337)
Transfer into OREO	-	-	-	-	-	-	-	-	-	-	-
Refinance out of TDR status	-	-	-	-	-	-	-	-	-	-	-
Balance June 30, 2014	\$ 5,968	\$ -	\$ 498	\$ 9,589	\$ 5,465	\$ 5,494	\$ 6,201	\$ -	\$ 38	\$ -	\$ 33,253

Allowance related to troubled debt restructurings	\$ 171	\$ -	\$ -	\$ 188	\$ 79	\$ 298	\$ 52	\$ -	\$ -	\$ -	\$ 788
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For the Six Months Ended June 30, 2014

Dollars in thousands	Construction & Land Development		Commercial Real Estate		Residential Real Estate		Home Equity		Consumer Other		Total
	Land & Develop-ment	Construc-tion	Commer-cial	Owner Occupied	Non-Owner Occupied	Non-jumbo	Jumbo	Equity	sumer	Other	
Troubled debt restructurings											
Balance January 1, 2014	\$ 6,163	\$ -	\$ 1,243	\$ 9,699	\$ 5,544	\$ 5,541	\$ 6,278	\$ -	\$ 47	\$ -	\$ 34,515
Additions	-	-	86	-	-	-	-	-	-	-	86
Charge-offs	-	-	-	-	-	-	-	-	(3)	-	(3)
Net (paydowns) advances	(195)	-	(831)	(110)	(79)	(47)	(77)	-	(6)	-	(1,345)
Transfer into OREO	-	-	-	-	-	-	-	-	-	-	-
Refinance out of TDR status	-	-	-	-	-	-	-	-	-	-	-
Balance June 30, 2014	\$ 5,968	\$ -	\$ 498	\$ 9,589	\$ 5,465	\$ 5,494	\$ 6,201	\$ -	\$ 38	\$ -	\$ 33,253
Allowance related to troubled debt restructurings	\$ 171	\$ -	\$ -	\$ 188	\$ 79	\$ 298	\$ 52	\$ -	\$ -	\$ -	\$ 788

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Summit Financial Group, Inc. and Subsidiaries
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We categorize loans into risk categories based on relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. We analyze loans individually by classifying the loans as to credit risk. We internally grade all commercial loans at the time of loan origination. In addition, we perform an annual loan review on all non-homogenous commercial loan relationships with an aggregate exposure of \$2 million, at which time these loans are re-graded. We use the following definitions for our risk grades:

Pass: Loans graded as Pass are loans to borrowers of acceptable credit quality and risk. They are higher quality loans that do not fit any of the other categories described below.

OLEM (Special Mention): Commercial loans categorized as OLEM are potentially weak. The credit risk may be relatively minor yet represent a risk given certain specific circumstances. If the potential weaknesses are not monitored or mitigated, the asset may weaken or inadequately protect our position in the future.

Substandard: Commercial loans categorized as Substandard are inadequately protected by the borrower's ability to repay, equity, and/or the collateral pledged to secure the loan. These loans have identified weaknesses that could hinder normal repayment or collection of the debt. These loans are characterized by the distinct possibility that we will sustain some loss if the identified weaknesses are not mitigated.

Doubtful: Commercial loans categorized as Doubtful have all the weaknesses inherent in those loans classified as Substandard, with the added elements that the full collection of the loan is improbable and the possibility of loss is high.

Loss: Loans classified as loss are considered to be non-collectible and of such little value that their continuance as a bankable asset is not warranted. This does not mean that the loan has absolutely no recovery value, but rather it is neither practical nor desirable to defer writing off the loan, even though partial recovery may be obtained in the future.

The following table presents the recorded investment in construction and development, commercial, and commercial real estate loans which are generally evaluated based upon the internal risk ratings defined above.

Loan Risk Profile by Internal
Risk Rating

	Construction and Development				Commercial Real Estate					
	Land and land development		Construction		Commercial		Owner Occupied		Non-Owner Occupied	
Dollars in thousands	6/30/2014	12/31/2013	6/30/2014	12/31/2013	6/30/2014	12/31/2013	6/30/2014	12/31/2013	6/30/2014	12/31/2013
Pass	\$ 45,624	\$ 41,662	\$ 20,432	\$ 15,022	\$ 88,446	\$ 82,323	\$ 150,578	\$ 143,982	\$ 303,213	\$ 268,967
OLEM (Special Mention)	4,539	5,550	470	133	1,203	4,544	1,903	1,412	9,483	10,222
Substandard	14,083	24,131	-	-	447	1,485	1,779	4,224	1,743	1,601
Doubtful	-	110	-	-	-	-	-	-	-	-
Loss	-	-	-	-	-	-	-	-	-	-

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Total \$ 64,246 \$ 71,453 \$ 20,902 \$ 15,155 \$ 90,096 \$ 88,352 \$ 154,260 \$ 149,618 \$ 314,439 \$ 280,790

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Summit Financial Group, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (unaudited)

The following table presents the recorded investment in consumer, residential real estate, and home equity loans, which are generally evaluated based on the aging status of the loans, which was previously presented, and payment activity.

Dollars in thousands	Performing			Nonperforming		
	6/30/2014	12/31/2013	6/30/2013	6/30/2014	12/31/2013	6/30/2013
Residential real estate						
Non-jumbo	\$ 216,619	\$ 210,500	\$ 212,426	\$ 2,950	\$ 2,446	\$ 4,333
Jumbo	52,487	53,406	49,567	-	-	9,000
Home Equity	60,909	54,844	53,503	339	-	271
Consumer	19,648	19,761	20,056	129	128	91
Other	6,798	3,276	3,397	-	-	-
Total	\$ 356,461	\$ 341,787	\$ 338,949	\$ 3,418	\$ 2,574	\$ 13,695

Loan commitments: ASC Topic 815, Derivatives and Hedging, requires that commitments to make mortgage loans should be accounted for as derivatives if the loans are to be held for sale, because the commitment represents a written option and accordingly is recorded at the fair value of the option liability.

NOTE 7. ALLOWANCE FOR LOAN LOSSES

An analysis of the allowance for loan losses for the six month periods ended June 30, 2014 and 2013, and for the year ended December 31, 2013 is as follows:

Dollars in thousands	Six Months Ended		Year
	June 30,	June 30,	Ended December 31,
	2014	2013	2013
Balance, beginning of year	\$ 12,659	\$ 17,933	\$ 17,933
Losses:			
Commercial	390	54	723
Commercial real estate			
Owner occupied	11	66	1,031
Non-owner occupied	-	9	9
Construction and development			
	3,533	2,166	3,596

Land and land development			
Construction	-	-	-
Residential real estate			
Non-jumbo	46	384	541
Jumbo	63	3,625	4,741
Home equity	-	76	77
Consumer	80	34	79
Other	51	51	162
Total	4,174	6,465	10,959
Recoveries:			
Commercial	17	4	12
Commercial real estate			
Owner occupied	31	2	8
Non-owner occupied	4	-	674
Construction and development			
Land and land development	165	9	187
Construction	-	-	-
Real estate - mortgage			
Non-jumbo	53	43	127
Jumbo	163	3	6
Home equity	3	1	5
Consumer	41	37	79
Other	44	55	87
Total	521	154	1,185
Net losses	3,653	6,311	9,774
Provision for loan losses	2,000	2,500	4,500
Balance, end of year	\$ 11,006	\$ 14,122	\$ 12,659

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Activity in the allowance for loan losses by loan class during the first six months of 2014 is as follows:

Dollars in thousands	Construction & Land Development		Commercial Real Estate		Residential Real Estate		Non-jumbo	Home Equity	Consumer	Other	Total
	Land & Land Development	Construction	Commercial	Owner Occupied	Non-Owner Occupied	Jumbo					
Allowance for loan losses											
Beginning balance	\$5,455	\$269	\$1,324	\$969	\$641	\$1,842	\$1,888	\$173	\$47	\$51	\$12,659
Charge-offs	3,533	-	390	11	-	46	63	-	80	51	4,174
Recoveries	165	-	17	31	4	53	163	3	41	44	521
Provision	1,722	85	124	8	98	(318)	93	83	38	67	2,000
Ending balance	\$3,809	\$354	\$1,075	\$997	\$743	\$1,531	\$2,081	\$259	\$46	\$111	\$11,006
Allowance related to:											
Loans individually evaluated for impairment	\$898	\$-	\$-	\$267	\$79	\$299	\$52	\$-	\$-	\$-	\$1,595
Loans collectively evaluated for impairment	2,911	354	1,075	730	664	1,232	2,029	259	46	111	9,411
Loans acquired with deteriorated credit quality	-	-	-	-	-	-	-	-	-	-	-
Total	\$3,809	\$354	\$1,075	\$997	\$743	\$1,531	\$2,081	\$259	\$46	\$111	\$11,006
Loans individually evaluated for impairment	\$15,469	\$-	\$506	\$10,893	\$5,749	\$6,032	\$8,721	\$186	\$37	\$-	\$47,593

Loans collectively evaluated for impairment	48,777	20,902	89,590	143,367	308,690	213,537	43,766	61,062	19,740	6,798	\$956,229
Loans acquired with deteriorated credit quality	-	-	-	-	-	-	-	-	-	-	-
Total	\$64,246	\$20,902	\$90,096	\$154,260	\$314,439	\$219,569	\$52,487	\$61,248	\$19,777	\$6,798	\$1,003,822

NOTE 8. GOODWILL AND OTHER INTANGIBLE ASSETS

The following tables present our goodwill by reporting unit at June 30, 2014 and other intangible assets by reporting unit at June 30, 2013 and December 31, 2013.

Dollars in thousands	Goodwill Activity		
	Banking	Services	Total
Balance, January 1, 2014	\$ 1,488	\$ 4,710	\$ 6,198
Acquired goodwill, net	-	-	-
Balance, June 30, 2014	\$ 1,488	\$ 4,710	\$ 6,198

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Summit Financial Group, Inc. and Subsidiaries
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Dollars in thousands	Other Intangible Assets					
	June 30, 2014			December 31, 2013		
	Community Banking	Insurance Services	Total	Community Banking	Insurance Services	Total
Unidentifiable intangible assets						
Gross carrying amount	\$ 2,267	\$ -	\$ 2,267	\$ 2,267	\$ -	\$ 2,267
Less: accumulated amortization	2,267	-	2,267	2,216	-	2,216
Net carrying amount	\$ -	\$ -	\$ -	\$ 51	\$ -	\$ 51
Identifiable intangible assets						
Gross carrying amount	\$ -	\$ 3,000	\$ 3,000	\$ -	\$ 3,000	\$ 3,000
Less: accumulated amortization	-	1,400	1,400	-	1,300	1,300
Net carrying amount	\$ -	\$ 1,600	\$ 1,600	\$ -	\$ 1,700	\$ 1,700

We recorded amortization expense of approximately \$150,000 for the six months ended June 30, 2014 relative to our other intangible assets. Annual amortization is expected to be approximately \$251,000 in 2014, and \$200,000 for each of the years ending 2015 through 2018.

NOTE 9. DEPOSITS

The following is a summary of interest bearing deposits by type as of June 30, 2014 and 2013 and December 31, 2013:

Dollars in thousands	June 30,	December	June 30,
	2014	31, 2013	2013
Demand deposits, interest bearing	\$ 187,855	\$ 186,578	\$ 187,244
Savings deposits	243,323	193,446	196,069
Time deposits	520,483	530,951	562,703
Total	\$ 951,661	\$ 910,975	\$ 946,016

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Included in time deposits are deposits acquired through a third party (“brokered deposits”) totaling \$159.0 million, \$160.8 million and \$192.1 million at June 30, 2014, December 31, 2013, and June 30, 2013, respectively.

A summary of the scheduled maturities for all time deposits as of June 30, 2014 is as follows:

Dollars in thousands	
Six month period ending December 31, 2014	\$ 117,062
Year ending December 31, 2015	125,062
Year ending December 31, 2016	116,389
Year ending December 31, 2017	43,842
Year ending December 31, 2018	44,658
Thereafter	73,470
	\$ 520,483

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The following is a summary of the maturity distribution of all certificates of deposit in denominations of \$100,000 or more as of June 30, 2014:

Dollars in thousands	Amount	Percent
Three months or less	\$ 49,136	12.8%
Three through six months	27,033	7.0%
Six through twelve months	53,313	13.9%
Over twelve months	254,190	66.3%
Total	\$ 383,672	100.0%

NOTE 10. BORROWED FUNDS

Short-term borrowings: A summary of short-term borrowings is presented below:

Dollars in thousands	Six Months Ended June 30,			
	2014	Federal Funds		2013
	Short-term FHLB Advances	Purchased and Lines of Credit	Short-term FHLB Advances	Federal Funds Purchased and Lines of Credit
Balance at June 30	\$ 86,050	\$ 5,679	\$ 15,800	\$ 962
Average balance outstanding for the period	69,108	8,336	17,938	3,474
Maximum balance outstanding at any month end during period	87,550	8,976	45,000	5,961
Weighted average interest rate for the period	0.31 %	0.25 %	0.25 %	0.25%

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Weighted average
interest rate for
balances

outstanding at June 30	0.29	%	0.25	%	0.25	%	0.25%
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Dollars in thousands	Year Ended December 31, 2013	
	Short-term FHLB Advances	Federal Funds Purchased and Lines of Credit
Balance at December 31	\$ 53,800	\$ 8,969
Average balance outstanding for the period	29,786	4,313
Maximum balance outstanding at any month end during period	55,300	8,969
Weighted average interest rate for the period	0.28	% 0.25%
Weighted average interest rate for balances outstanding at December 31	0.26	% 0.25%

Long-term borrowings: Our long-term borrowings of \$121.9 million, \$163.5 million and \$163.6 million at June 30, 2014, December 31, 2013, and June 30, 2013 respectively, consisted primarily of advances from the Federal Home Loan Bank (“FHLB”) and structured reverse repurchase agreements with two unaffiliated institutions. All FHLB advances are collateralized primarily by similar amounts of residential mortgage loans, certain commercial loans, mortgage backed securities and securities of U. S. Government agencies and corporations.

Dollars in thousands	Balance at June 30,		Balance at December 31,
	2014	2013	2013
Long-term FHLB advances	\$ 41,026	\$ 82,649	\$ 82,600
Long-term reverse repurchase agreements	72,000	72,000	72,000

Term loans	8,916	8,916	8,916
Total	\$ 121,942	\$ 163,565	\$ 163,516

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The term loans are secured by the common stock of our subsidiary bank. \$5.4 million bears a variable interest rate of prime minus 50 basis points with a final maturity of 2017, and \$3.5 million bears a fixed rate of 8% with a final maturity of 2023.

Our long term FHLB borrowings and reverse repurchase agreements bear both fixed and variable rates and mature in varying amounts through the year 2026.

The average interest rate paid on long-term borrowings for the six month period ended June 30, 2014 was 4.01% compared to 3.86% for the first six months of 2013.

Subordinated debentures: We have subordinated debt totaling \$16.8 million at June 30, 2014, December 31, 2013, and June 30, 2013. The subordinated debt qualifies as Tier 2 capital under Federal Reserve Board guidelines until the debt is within 5 years of its maturity; thereafter the amount qualifying as Tier 2 capital is reduced by 20 percent each year until maturity. During 2009, we issued \$6.8 million in subordinated debt, of which \$5 million was issued to an affiliate of a director of Summit. We also issued \$1.0 million and \$0.8 million to two unrelated parties. These three issuances bear an interest rate of 10 percent per annum, a term of 10 years, and are not prepayable by us within the first five years. During 2008, we issued \$10 million of subordinated debt to an unrelated institution, which bears a variable interest rate of 1 month LIBOR plus 275 basis points and a term of 7.5 years.

Subordinated debentures owed to unconsolidated subsidiary trusts: We have three statutory business trusts that were formed for the purpose of issuing mandatorily redeemable securities (the "capital securities") for which we are obligated to third party investors and investing the proceeds from the sale of the capital securities in our junior subordinated debentures (the "debentures"). The debentures held by the trusts are their sole assets. Our subordinated debentures totaled \$19.6 million at June 30, 2014, December 31, 2013, and June 30, 2013.

In October 2002, we sponsored SFG Capital Trust I, in March 2004, we sponsored SFG Capital Trust II, and in December 2005, we sponsored SFG Capital Trust III, of which 100% of the common equity of each trust is owned by us. SFG Capital Trust I issued \$3.5 million in capital securities and \$109,000 in common securities and invested the proceeds in \$3.61 million of debentures. SFG Capital Trust II issued \$7.5 million in capital securities and \$232,000 in common securities and invested the proceeds in \$7.73 million of debentures. SFG Capital Trust III issued \$8.0 million in capital securities and \$248,000 in common securities and invested the proceeds in \$8.25 million of debentures. Distributions on the capital securities issued by the trusts are payable quarterly at a variable interest rate equal to 3 month LIBOR plus 345 basis points for SFG Capital Trust I, 3 month LIBOR plus 280 basis points for SFG Capital Trust II, and 3 month LIBOR plus 145 basis points for SFG Capital Trust III, and equals the interest rate earned on the debentures held by the trusts, and is recorded as interest expense by us. The capital securities are subject to mandatory redemption in whole or in part, upon repayment of the debentures. We have entered into agreements which, taken collectively, fully and unconditionally guarantee the capital securities subject to the terms of the guarantee. The debentures of each Capital Trust are redeemable by us quarterly.

The capital securities held by SFG Capital Trust I, SFG Capital Trust II, and SFG Capital Trust III qualify as Tier 1 capital under Federal Reserve Board guidelines. In accordance with these Guidelines, trust preferred securities generally are limited to 25% of Tier 1 capital elements, net of goodwill. The amount of trust preferred securities and certain other elements in excess of the limit can be included in Tier 2 capital.

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A summary of the maturities of all long-term borrowings and subordinated debentures for the next five years and thereafter is as follows:

Dollars in thousands	Long-term borrowings	Subordinated debentures	Subordinated debentures owed to unconsolidated subsidiary trusts
Year Ending December 31,	2014\$ 43,952	\$ -	\$ -
	2015 1,909	10,000	-
	2016 28,911	-	-
	2017 918	-	-
	2018 45,017	-	-
	Thereafter 1,235	6,800	19,589
	\$ 121,942	\$ 16,800	\$ 19,589

NOTE 11. SHARE BASED COMPENSATION

The 2014 Long-Term Incentive Plan (“2014 LTIP”) was adopted by our shareholders in May 2014 to enhance the ability of the Company to attract and retain exceptionally qualified individuals to serve as key employees. The LTIP provides for the issuance of up to 500,000 shares of common stock, in the form of equity awards including stock options, restricted stock, restricted stock units, stock appreciation rights, performance units, other stock-based awards or any combination thereof, to our key employees. No awards have been granted under the 2014 LTIP.

Stock options awarded under the 2009 Officer Stock Option Plan and the 1998 Officer Stock Option Plan (collectively, the “Plans”) were not altered by the 2014 LTIP, and remain subject to the terms of the Plans. However, under the terms of the 2014 LTIP, all shares of common stock remaining issuable under the Plans at the time the 2014 LTIP was adopted ceased to be available for future issuance.

The fair value of our employee stock options granted under the Plans is estimated at the date of grant using the Black-Scholes option-pricing model. This model requires the input of highly subjective assumptions, changes to which can materially affect the fair value estimate. Additionally, there may be other factors that would otherwise have a significant effect on the value of employee stock options granted but are not considered by the model. Because our employee stock options have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the fair value estimate, in management’s opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options at the time of grant. There were no options granted during the first six months of 2014 or 2013.

We recognize compensation expense based on the estimated number of stock awards expected to actually vest, exclusive of the awards expected to be forfeited. During the first six months of 2014 and 2013, our stock

compensation expense and related deferred taxes were insignificant.

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A summary of activity in our Plans during the first six months of 2014 and 2013 is as follows:

	For the Six Months Ended June 30,			
	2014		2013	
	Options	Weighted-Average Exercise Price	Options	Weighted-Average Exercise Price
Outstanding, January 1	185,410	\$ 19.59	249,700	\$ 18.98
Granted	-	-	-	-
Exercised (3,200)	-	4.63	(12,000)	5.09
Forfeited	-	-	(1,750)	19.69
Expired (2,500)	-	17.43	(39,700)	23.41
Outstanding, June 30	179,710	\$ 19.88	196,250	\$ 18.92

Other information regarding options outstanding and exercisable at June 30, 2014 is as follows:

Range of exercise price	# of shares	Options Outstanding			Options Exercisable		
		Wted. Avg. Remaining	Wted. Avg. Aggregate Intrinsic	Contractual Value (in thousands)	# of shares	Wted. Avg. Aggregate Intrinsic	Contractual Value (in thousands)
2.54 - \$6.00	13,550	\$ 4.69	4.20	\$ 81	11,550	\$ 5.06	\$ 64
6.01 - 10.00	23,160	9.07	2.73	36	22,560	9.14	34
10.01 - 17.50	-	-	-	-	-	0	-
17.51 - 20.00	38,500	17.80	2.50	-	38,500	17.8	-
20.01 - 25.93	104,500	25.04	2.24	-	104,500	25.04	-
	179,710	19.88		\$ 117	177,110	20.12	\$ 98

NOTE 12. COMMITMENTS AND CONTINGENCIES

Off-Balance Sheet Arrangements

We are a party to certain financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of our customers. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the statement of financial position. The contract amounts of these instruments reflect the extent of involvement that we have in this class of financial instruments.

Many of our lending relationships contain both funded and unfunded elements. The funded portion is reflected on our balance sheet. The unfunded portion of these commitments is not recorded on our balance sheet until a draw is made under the loan facility. Since many of the commitments to extend credit may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash flow requirements.

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Summit Financial Group, Inc. and Subsidiaries
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A summary of the total unfunded, or off-balance sheet, credit extension commitments follows:

	June 30,
Dollars in thousands	2014
Commitments to extend credit:	
Revolving home equity and credit card lines	\$ 51,340
Construction loans	22,618
Other loans	43,683
Standby letters of credit	1,668
Total	\$ 119,309

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. We evaluate each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if we deem necessary upon extension of credit, is based on our credit evaluation. Collateral held varies but may include accounts receivable, inventory, equipment or real estate.

Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. Standby letters of credit generally are contingent upon the failure of the customer to perform according to the terms of the underlying contract with the third party.

Our exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual amount of those instruments. We use the same credit policies in making commitments and conditional obligations as we do for on-balance sheet instruments.

Legal Contingencies

On May 13, 2014, the ResCap Liquidating Trust ("ResCap"), as successor to Residential Funding Company, LLC f/k/a Residential Funding Corporation ("RFC"), filed a complaint against Summit Financial Mortgage, LLC ("Summit Mortgage"), a former residential mortgage subsidiary of Summit whose operations were discontinued in 2007, in the United States Bankruptcy Court for the Southern District of New York and subsequently amended its complaint on July 25, 2014. The Amended Complaint asserts the following three causes of action related to Summit Mortgage's origination and subsequent sale of mortgage loans to Residential Funding Corporation: 1) Summit Mortgage breached its representations and warranties made in the contract governing the sale of the mortgage loans to RFC; 2) an indemnification claim against Summit Mortgage for damages paid by ResCap to settle claims in RFC's bankruptcy proceeding which allegedly relate to mortgage loans Summit Mortgage sold to RFC; 3) a claim for damages against

Summit Community Bank, Inc., former parent of Summit Mortgage, arising out of a guaranty in which the Bank guaranteed Summit Mortgage's full performance under the contract governing the sale of mortgage loans to RFC. An estimate as to possible loss resulting from the Amended Complaint cannot be provided at this time because such an estimate cannot be made. Summit intends to defend these claims vigorously.

We are not a party to any other litigation except for matters that arise in the normal course of business. While it is impossible to ascertain the ultimate resolution or range of financial liability with respect to these contingent matters, in the opinion of management, the outcome of these matters will not have a significant adverse effect on the consolidated financial statements.

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Summit Financial Group, Inc. and Subsidiaries
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NOTE 13. REGULATORY MATTERS

We and our subsidiaries are subject to various regulatory capital requirements administered by the banking regulatory agencies. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, we and each of our subsidiaries must meet specific capital guidelines that involve quantitative measures of our and our subsidiaries' assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. We and each of our subsidiaries' capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require us and each of our subsidiaries to maintain minimum amounts and ratios of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). We believe, as of June 30, 2014, that we and each of our subsidiaries met all capital adequacy requirements to which they were subject.

The most recent notifications from the banking regulatory agencies categorized us and each of our subsidiaries as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, we and each of our subsidiaries must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the table below.

Our actual capital amounts and ratios as well as our subsidiary, Summit Community Bank's ("Summit Community") are presented in the following table.

Dollars in thousands As of June 30, 2014	Actual		Minimum Required Regulatory Capital				To be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio		
Total Capital (to risk weighted assets)								
Summit	\$ 146,096	14.2 %	\$ 82,556	8.0 %	\$ 103,195	10.0%		
Summit Community	160,462	15.6 %	82,035	8.0 %	102,543	10.0%		
Tier I Capital (to risk weighted assets)								
Summit	127,490	12.4 %	41,278	4.0 %	61,917	6.0%		
Summit Community	149,456	14.5 %	41,281	4.0 %	61,922	6.0%		
Tier I Capital (to average assets)								
Summit	127,490	9.0 %	56,474	4.0 %	70,592	5.0%		
Summit Community	149,456	10.6 %	56,452	4.0 %	70,565	5.0%		

As of
December 31,
2013

Total Capital (to risk weighted
assets)

Summit	144,202	14.5	%	79,638	8.0	%	99,547	10.0%
Summit Community	156,473	15.7	%	79,627	8.0	%	99,534	10.0%

Tier I Capital (to risk weighted
assets)

Summit	122,918	12.4	%	39,499	4.0	%	59,248	6.0%
Summit Community	143,989	14.5	%	39,814	4.0	%	59,720	6.0%

Tier I Capital
(to average
assets)

Summit	122,918	8.9	%	55,151	4.0	%	68,938	5.0%
Summit Community	143,989	10.4	%	55,150	4.0	%	68,938	5.0%

Summit Financial Group, Inc. (“Summit”) and its bank subsidiary, Summit Community Bank, Inc. (the “Bank”), have entered into informal Memoranda of Understanding (“MOU’s”) with their respective regulatory authorities. A memorandum of understanding is characterized by the regulatory authorities as an informal action that is not published or publicly available and that is used when circumstances warrant a milder form of action than a formal supervisory action, such as a formal written agreement or order.

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Under the Summit MOU, Summit has agreed among other things to:

§ Summit suspending all cash dividends on its common stock until further notice. Dividends on all preferred stock, as well as interest payments on subordinated notes underlying Summit's trust preferred securities, continue to be permissible; and,

§ Summit not incurring any additional debt, other than trade payables, without the prior written consent of the principal banking regulators.

Additional information regarding Summit's MOU is included in Part I. Item 1A – Risk Factors on our Form 10-K for the year ended December 31, 2013.

On October 25, 2012, the Bank entered into a revised MOU ("Bank MOU") which replaced the Bank MOU effective September 24, 2009 and subsequently amended on February 1, 2011. In general, the Bank MOU includes provisions substantially similar to those in the prior Bank MOU with the exception that several provisions deemed no longer applicable by the regulatory authorities were removed and a provision relative to reducing the Bank's levels of classified assets was added.

In summary, we have agreed, among other things, to address the following matters relative to the Bank:

§ maintaining a Board committee which monitors and promotes compliance with the provisions of the Bank MOU;

§ providing the Bank's regulatory authorities with updated reports of criticized assets and/or formal workout plans for all nonperforming borrower relationships with an aggregate outstanding balance exceeding \$1 million;

§ developing and submitting to regulatory authorities a written plan to reduce the Bank's risk exposure in each adversely classified credit relationship in excess of \$1 million and all OREO;

§ establishing procedures to report all loans with balances exceeding \$500,000 that have credit weaknesses or that fall outside of the Bank's policy;

§ annually reviewing the organizational structure and operations of the Bank's loan department;

§ maintaining an adequate allowance for loan and lease losses through charges to current operating income;

§ reviewing overall liquidity objectives and developing and submitting to regulatory authorities plans and procedures aimed to improve liquidity and reduce reliance on volatile liabilities;

§ preparing comprehensive budgets and earnings forecasts for the Bank and submitting reports comparing actual performance to the budget plan;

§ maintaining a minimum Tier 1 Leverage Capital ratio of at least 8% and a Total Risk-based Capital ratio of at least 11%;

§ not paying any cash dividends without the prior written consent of the banking regulators; and,

§

providing quarterly progress reports to the Bank's regulatory authorities detailing steps taken to comply with the Bank MOU.

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Summit Financial Group, Inc. and Subsidiaries
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NOTE 14. SEGMENT INFORMATION

We operate two business segments: community banking and insurance & financial services. These segments are primarily identified by the products or services offered. The community banking segment consists of our full service banks which offer customers traditional banking products and services through various delivery channels. The insurance & financial services segment includes three insurance agency offices that sell insurance products. The accounting policies discussed throughout the notes to the consolidated financial statements apply to each of our business segments.

Inter-segment revenue and expense consists of management fees allocated to the community banking and the insurance & financial services segments for all centralized functions that are performed by the parent, including overall direction in the areas of strategic planning, investment portfolio management, asset/liability management, financial reporting and other financial and administrative services. Information for each of our segments is included below:

In thousands	Six Months Ended June 30, 2014				
	Community Banking	Insurance & Financial Services	Parent	Eliminations	Total
Net interest income	\$ 21,311	\$ -	\$ (953)	\$ -	\$ 20,358
Provision for loan losses	2,000	-	-	-	2,000
Net interest income after provision for loan losses	19,311	-	(953)	-	18,358
Other income	2,901	2,588	590	(590)	5,489
Other expenses	14,672	2,089	857	(590)	17,028
Income (loss) before income taxes	7,540	499	(1,220)	-	6,819
Income tax expense (benefit)	2,187	172	(362)	-	1,997
Net income (loss)	5,353	327	(858)	-	4,822
Dividends on preferred shares	-	-	387	-	387
Net income (loss) applicable to common shares	\$ 5,353	\$ 327	\$ (1,245)	\$ -	\$ 4,435
Inter-segment revenue (expense)	\$ (532)	\$ (58)	\$ 590	\$ -	\$ -
Average assets	\$ 1,454,597	\$ 6,064	\$ 162,023	\$ (217,039)	\$ 1,405,645

Six Months Ended June 30, 2013
Insurance
&
Community Financial

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In thousands	Banking	Services	Parent	Eliminations	Total
Net interest income	\$ 20,212	\$ -	\$ (950)	\$ -	\$ 19,262
Provision for loan losses	2,500	-	-	-	2,500
Net interest income after provision for loan losses	17,712	-	(950)	-	16,762
Other income	2,941	2,509	544	(544)	5,450
Other expenses	15,525	2,325	794	(544)	18,100
Income (loss) before income taxes	5,128	184	(1,200)	-	4,112
Income tax expense (benefit)	1,447	66	(411)	-	1,102
Net income (loss)	3,681	118	(789)	-	3,010
Dividends on preferred shares	-	-	388	-	388
Net income (loss) applicable to common shares	\$ 3,681	\$ 118	\$ (1,177)	\$ -	\$ 2,622
Intersegment revenue (expense)	\$ (490)	\$ (54)	\$ 544	\$ -	\$ -
Average assets	\$ 1,442,999	\$ 6,304	\$ 156,502	\$ (217,203)	\$ 1,388,602

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In thousands	Three Months Ended June 30, 2014				
	Community Banking	Insurance & Financial Services	Parent	Eliminations	Total
Net interest income	\$ 10,800	\$ -	\$ (480)	\$ -	\$ 10,320
Provision for loan losses	1,000	-	-	-	1,000
Net interest income after provision for loan losses	9,800	-	(480)	-	9,320
Other income	1,491	1,214	297	(297)	2,705
Other expenses	7,323	1,061	443	(297)	8,530
Income (loss) before income taxes	3,968	153	(626)	-	3,495
Income tax expense (benefit)	1,205	50	(192)	-	1,063
Net income (loss)	2,763	103	(434)	-	2,432
Dividends on preferred shares	-	-	193	-	193
Net income (loss) applicable to common shares	\$ 2,763	\$ 103	\$ (627)	\$ -	\$ 2,239
Inter-segment revenue (expense)	\$ (268)	\$ (29)	\$ 297	\$ -	\$ -
Average assets	\$ 1,467,261	\$ 6,149	\$ 163,682	\$ (218,027)	\$ 1,419,065

In thousands	Three Months Ended June 30, 2013				
	Community Banking	Insurance & Financial Services	Parent	Eliminations	Total
Net interest income	\$ 9,986	\$ -	\$ (482)	\$ -	\$ 9,504
Provision for loan losses	1,000	-	-	-	1,000
Net interest income after provision for loan losses	8,986	-	(482)	-	8,504
Other income	1,497	1,206	272	(272)	2,703
Other expenses	8,332	1,129	349	(272)	9,538
Income (loss) before income taxes	2,151	77	(559)	-	1,669
	622	31	(201)	-	452

Income tax expense (benefit)					
Net income (loss)	1,529	46	(358)	-	1,217
Dividends on preferred shares	-	-	194	-	194
Net income (loss) applicable to common shares	\$ 1,529	\$ 46	\$ (552)	\$ -	\$ 1,023
Intersegment revenue (expense)	\$ (245)	\$ (27)	\$ 272	\$ -	\$ -
Average assets	\$ 1,439,506	\$ 6,344	\$ 157,189	\$ (217,703)	\$ 1,385,336

NOTE 15. DERIVATIVE FINANCIAL INSTRUMENTS

We use derivative instruments primarily to protect against the risk of adverse interest rate movements on the cash flows of certain liabilities. Derivative instruments represent contracts between parties that usually require little or no initial net investment and result in one party delivering cash or another type of asset to the other party based upon a notional amount and an underlying as specified in the contract. A notional amount represents the number of units of a specific item, such as currency units. An underlying represents a variable, such as an interest rate or price index. The amount of cash or other asset delivered from one party to the other is determined based upon the interaction of the notional amount of the contract with the underlying. Derivatives can also be implicit in certain contracts and commitments.

As with any financial instrument, derivative instruments have inherent risks, primarily market and credit risk. Market risk associated with changes in interest rates is managed by establishing and monitoring limits as to the degree of risk that may be undertaken as part of our overall market risk monitoring process. Credit risk occurs when a counterparty to a derivative contract with an unrealized gain fails to perform according to the terms of the agreement. Credit risk is managed by monitoring the size and maturity structure of the derivative portfolio, and applying uniform credit standards to all activities with credit risk.

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In accordance with ASC 815, Derivatives and Hedging, all derivative instruments are recorded on the balance sheet at fair value. Changes in the fair value of derivatives are recorded each period in current earnings or other comprehensive income, depending on whether a derivative is designated as part of a hedge transaction and, if it is, depending on the type of hedge transaction.

Fair-value hedges – For transactions in which we are hedging changes in fair value of an asset, liability, or a firm commitment, changes in the fair value of the derivative instrument are generally offset in the income statement by changes in the hedged item’s fair value.

Cash-flow hedges – For transactions in which we are hedging the variability of cash flows related to a variable-rate asset, liability, or a forecasted transaction, changes in the fair value of the derivative instrument are reported in other comprehensive income. The gains and losses on the derivative instrument, which are reported in comprehensive income, are reclassified to earnings in the periods in which earnings are impacted by the variability of cash flows of the hedged item.

The ineffective portion of all hedges is recognized in current period earnings.

Other derivative instruments – For risk management purposes that do not meet the hedge accounting criteria and, therefore, do not qualify for hedge accounting. These derivative instruments are accounted for at fair value with changes in fair value recorded in the income statement.

We have entered into three forward-starting, pay-fixed/receive LIBOR interest rate swaps. \$40 million notional with an effective date of July 18, 2016, was designated as a cash flow hedge of \$40 million of forecasted variable rate Federal Home Loan Bank advances. Under the terms of this swap we will pay a fixed rate of 2.98% for a 3 year period. \$30 million notional with an effective date of April 18, 2016, was designated as a cash flow hedge of \$30 million of forecasted variable rate Federal Home Loan Bank advances. Under the terms of this swap we will pay a fixed rate of 2.89% for a 4.5 year period. \$40 million notional with an effective date of October 18, 2016, was designated as a cash flow hedge of \$40 million of forecasted variable rate Federal Home Loan Bank advances. Under the terms of the swap we will pay a fixed rate of 2.841% for a 3 year period.

A summary of our derivative financial instruments as of June 30, 2014 and December 31, 2013 follows:

Dollars in thousands	Notional Amount	June 30, 2014 Derivative Fair Value		Net Ineffective Hedge Gains/(Losses)
		Asset	Liability	
CASH FLOW HEDGES				
Pay-fixed/receive-variable interest rate swaps				
Long term borrowings	\$ 110,000	\$ -	\$ 1,582	\$ -
	\$ 110,000	\$ -	\$ 1,582	\$ -

Dollars in thousands	Notional Amount	December 31, 2013 Derivative Fair Value		Net Ineffective Hedge Gains/(Losses)
		Asset	Liability	
CASH FLOW				
HEDGES				
Pay-fixed/receive-variable interest rate swaps				
	Long term			
borrowings	\$ 70,000	\$ 803	\$ -	\$ -
	\$ 70,000	\$ 803	\$ -	\$ -

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INTRODUCTION

The following discussion and analysis focuses on significant changes in our financial condition and results of operations of Summit Financial Group, Inc. ("Company" or "Summit") and our operating segments, Summit Community Bank ("Summit Community"), and Summit Insurance Services, LLC for the periods indicated. See Note 14 of the accompanying consolidated financial statements for our segment information. This discussion and analysis should be read in conjunction with our 2013 audited financial statements and Annual Report on Form 10-K.

The Private Securities Litigation Act of 1995 indicates that the disclosure of forward-looking information is desirable for investors and encourages such disclosure by providing a safe harbor for forward-looking statements by us. Our following discussion and analysis of financial condition and results of operations contains certain forward-looking statements that involve risk and uncertainty. In order to comply with the terms of the safe harbor, we note that a variety of factors could cause our actual results and experience to differ materially from the anticipated results or other expectations expressed in those forward-looking statements.

OVERVIEW

Our primary source of income is net interest income from loans and deposits. Business volumes tend to be influenced by the overall economic factors including market interest rates, business spending, and consumer confidence, as well as competitive conditions within the marketplace.

Interest earning assets increased by 0.91% for the first six months in 2014 compared to the same period of 2013 while our net interest earnings on a tax equivalent basis increased 5.51%. Our tax equivalent net interest margin increased 14 basis points as our reduced cost of interest bearing funds continues to positively impact our net interest earnings.

BUSINESS SEGMENT RESULTS

We are organized and managed along two major business segments, as described in Note 14 of the accompanying consolidated financial statements. The results of each business segment are intended to reflect each segment as if it were a stand alone business. Net income by segment follows:

In thousands	Three Months Ended		Six Months Ended June	
	June 30,		30,	
	2014	2013	2014	2013
Community banking	\$ 2,763	\$ 1,529	\$ 5,353	\$ 3,681
Insurance & financial services	103	46	327	118
Parent	(627)	(552)	(1,245)	(1,177)
Consolidated net income	\$ 2,239	\$ 1,023	\$ 4,435	\$ 2,622

CRITICAL ACCOUNTING POLICIES

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and follow general practices within the financial services industry. Application of these principles requires us to make estimates, assumptions, and judgments that affect the amounts reported in our financial statements and accompanying notes. These estimates, assumptions, and judgments are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements could reflect different estimates, assumptions, and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions, and judgments and as such have a greater possibility of producing results that could be materially different than originally reported.

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Our most significant accounting policies are presented in the notes to the consolidated financial statements of our 2013 Annual Report on Form 10-K. These policies, along with the other disclosures presented in the financial statement notes and in this financial review, provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined.

Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions, and estimates underlying those amounts, we have identified the determination of the allowance for loan losses, the valuation of goodwill, fair value measurements and deferred tax assets to be the accounting areas that require the most subjective or complex judgments, and as such could be most subject to revision as new information becomes available.

Allowance for Loan Losses: The allowance for loan losses represents our estimate of probable credit losses inherent in the loan portfolio. Determining the amount of the allowance for loan losses is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan portfolio also represents the largest asset type on our consolidated balance sheet. To the extent actual outcomes differ from our estimates, additional provisions for loan losses may be required that would negatively impact earnings in future periods. Note 6 to the consolidated financial statements of our 2013 Annual Report on Form 10-K describes the methodology used to determine the allowance for loan losses and a discussion of the factors driving changes in the amount of the allowance for loan losses is included in the Asset Quality section of the financial review of the 2013 Annual Report on Form 10-K.

Goodwill: Goodwill is subject to an analysis by reporting unit at least annually to determine whether write-downs of the recorded balances are necessary. Initially, an assessment of qualitative factors (Step 0) is performed to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, we determine it is not more likely than not that the fair value of a reporting unit is less than its carrying value, then performing the two-step impairment test is unnecessary. However, if we conclude otherwise, then we are required to perform the first step (Step 1) of the two-step impairment test by calculating the fair value of the reporting unit and comparing the fair value with the carrying amount of the reporting unit. If the fair value is less than the carrying value, an expense may be required on our books to write down the goodwill to the proper carrying value. Step 2 of impairment testing, which is necessary only if the reporting unit does not pass Step 1, compares the implied fair value of the reporting unit goodwill with the carrying amount of the goodwill for the reporting unit. The implied fair value of goodwill is determined in the same manner as goodwill that is recognized in a business combination.

Community Banking – During third quarter 2013, we performed the Step 0 assessment of our goodwill of our community banking reporting unit and determined that it was not more likely than not that the fair value was less than its carrying value. In performing the qualitative Step 0 assessments, we considered certain events and circumstances such as macroeconomic conditions, industry and market considerations, overall financial performance and cost factors when evaluating whether it is more likely than not that the fair value is less than its carrying amount. No indicators of impairment were noted as of September 30, 2013.

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Insurance Services – During third quarter 2013, we performed the Step 0 assessment of our goodwill of our insurance services reporting unit. We considered certain events and circumstances specific to the reporting unit, such as macroeconomic conditions, industry and market considerations, overall financial performance and cost factors when evaluating whether it is more likely than not that the fair value of our insurance services reporting unit is less than its carrying value and deemed it necessary to perform the further 2-step impairment test. We performed an internal valuation utilizing the income approach to determine the fair value of our insurance services reporting unit. This methodology consisted of discounting the expected future cash flows of this unit based upon a forecast of its operations considering long-term key business drivers such as anticipated commission revenue growth. The long term growth rate used in determining the terminal value was estimated at 2%, and a discount rate of 10.0% was applied to the insurance services unit's estimated future cash flows. We did not fail this Step 1 test as of September 30, 2013, therefore Step 2 testing was not necessary.

We cannot assure you that future goodwill impairment tests will not result in a charge to earnings. See Note 9 of the consolidated financial statements of our Annual Report on Form 10-K for further discussion of our intangible assets, which include goodwill.

Fair Value Measurements: ASC Topic 820 Fair Value Measurements and Disclosures provides a definition of fair value, establishes a framework for measuring fair value, and requires expanded disclosures about fair value measurements. Fair value is the price that could be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. Based on the observability of the inputs used in the valuation techniques, we classify our financial assets and liabilities measured and disclosed at fair value in accordance with the three-level hierarchy (e.g., Level 1, Level 2 and Level 3) established under ASC Topic 820. Fair value determination in accordance with this guidance requires that we make a number of significant judgments. In determining the fair value of financial instruments, we use market prices of the same or similar instruments whenever such prices are available. We do not use prices involving distressed sellers in determining fair value. If observable market prices are unavailable or impracticable to obtain, then fair value is estimated using modeling techniques such as discounted cash flow analyses. These modeling techniques incorporate our assessments regarding assumptions that market participants would use in pricing the asset or the liability, including assumptions about the risks inherent in a particular valuation technique and the risk of nonperformance.

Fair value is used on a recurring basis for certain assets and liabilities in which fair value is the primary basis of accounting. Additionally, fair value is used on a non-recurring basis to evaluate assets or liabilities for impairment or for disclosure purposes in accordance with ASC Topic 825 Financial Instruments.

Deferred Income Tax Assets: At June 30, 2014, we had net deferred tax assets of \$11.0 million. Based on our ability to offset the net deferred tax asset against taxable income in carryback years and expected future taxable income in carryforward years, there was no impairment of the deferred tax asset at June 30, 2014. All available evidence, both positive and negative, was considered to determine whether, based on the weight of that evidence, impairment should be recognized. However, our forecast process includes judgmental and quantitative elements that may be subject to significant change. If our forecast of taxable income within the carryback/carryforward periods available under applicable law is not sufficient to cover the amount of net deferred tax assets, such assets may become impaired.

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RESULTS OF OPERATIONS

Earnings Summary

Net income applicable to common shares for the six months ended June 30, 2014 increased to \$4.4 million, or \$0.50 per diluted share as compared to \$2.6 million or \$0.31 per diluted share for the same period of 2013. Net income applicable to common shares for the quarter ended June 30, 2014 totaled \$2.2 million, or \$0.25 per diluted share as compared to \$1.0 million, or \$0.13 per diluted share for the quarter ended June 30, 2013. Earnings for both the quarter and six months ended June 30, 2014 were positively impacted by increased net interest income and lower write-downs of foreclosed properties to their estimated fair values. Included in earnings for the six months ended June 30, 2013 was \$129,000 in losses on the sales of assets, primarily foreclosed properties, and \$1.9 million of charges resulting from the write down of a portion of our foreclosed properties to fair value. Returns on average equity and assets for the first six months of 2014 were 8.42% and 0.69%, respectively, compared with 5.47% and 0.43% for the same period of 2013.

Net Interest Income

Net interest income is the principal component of our earnings and represents the difference between interest and fee income generated from earning assets and the interest expense paid on deposits and borrowed funds. Fluctuations in interest rates as well as changes in the volume and mix of earning assets and interest bearing liabilities can materially impact net interest income.

Our net interest income on a fully tax-equivalent basis totaled \$21.1 million for the six months ended June 30, 2014 compared to \$20.0 million for the same period of 2013, representing an increase of \$1.1 million or 5.5%. While our tax-equivalent earnings on interest earning assets decreased \$460,000, this decrease was more than offset by a reduction in the cost of interest bearing liabilities (see Table II). Average interest earning assets increased 0.91% from \$1.27 billion during the first six months of 2013 to \$1.28 billion for the first six months of 2014. Average interest bearing liabilities increased 0.59% from \$1.176 billion at June 30, 2013 to \$1.183 billion at June 30, 2014, at an average cost for the first six months of 2014 of 1.37% compared to 1.65% for the same period of 2013.

Our consolidated net interest margin increased to 3.32% for the six months ended June 30, 2014, compared to 3.18% for the same period in 2013. The margin continues to be affected by elevated levels of nonaccruing loans. The present continued low interest rate environment has served to positively impact our net interest margin due to our liability sensitive balance sheet. For the six months ended June 30, 2014 compared to June 30, 2013, the yields on earning assets decreased 12 basis points, while the cost of our interest bearing funds decreased by 28 basis points.

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Assuming no significant change in market interest rates, we anticipate modest growth in our net interest income to continue over the near term due to modest growth in the volume of interest earning assets coupled with expected moderate improvement in net interest margin over the same period. We continue to monitor the net interest margin through net interest income simulation to minimize the potential for any significant negative impact. See the "Market Risk Management" section for further discussion of the impact changes in market interest rates could have on us. Further analysis of our yields on interest earning assets and interest bearing liabilities are presented in Tables I and II below.

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Table I - Average Balance Sheet and Net Interest

Income Analysis

Dollars in thousands

	Average Balance	For the Six Months Ended			Average Balance	Earnings/ Expense	Yield/ Rate
		June 30, 2014	Earnings/ Expense	Yield/ Rate			
Interest earning assets							
Loans, net of unearned income (1)							
Taxable	\$ 968,221	\$ 24,572	5.12 %	\$ 955,425	\$ 25,569	5.40%	
Tax-exempt							
(2)	6,719	241	7.23 %	5,714	203	7.16%	
Securities							
Taxable	215,220	2,480	2.32 %	221,998	1,955	1.78%	
Tax-exempt							
(2)	79,218	1,815	4.62 %	75,297	1,842	4.93%	
Federal funds sold and interest bearing deposits with other banks							
	8,666	4	0.09 %	8,023	3	0.08%	
Total interest earning assets	1,278,044	29,112	4.59 %	1,266,457	29,572	4.71%	
Noninterest earning assets							
Cash & due from banks	3,841			4,384			
Premises and equipment	20,506			21,059			
Other assets	115,454			113,334			
Allowance for loan losses	(12,200)			(16,632)			
Total assets	\$ 1,405,645			\$ 1,388,602			
Interest bearing liabilities							
Interest bearing demand deposits	\$ 188,573	\$ 106	0.11 %	\$ 176,811	\$ 132	0.15%	
Savings deposits	223,240	707	0.64 %	196,464	597	0.61%	
Time deposits	527,097	3,763	1.44 %	577,669	4,859	1.70%	
Short-term borrowings	77,444	111	0.29 %	20,872	26	0.25%	

Long-term borrowings and capital trust securities	167,013	3,368	4.07	%	204,584	4,001	3.94%
Total interest bearing liabilities	1,183,367	8,055	1.37	%	1,176,400	9,615	1.65%
Noninterest bearing liabilities and shareholders' equity							
Demand deposits	98,525				94,501		
Other liabilities	9,155				7,632		
Total liabilities	1,291,047				1,278,533		
Shareholders' equity - preferred	9,287				9,324		
Shareholders' equity - common	105,311				100,745		
Total liabilities and shareholders' equity	\$ 1,405,645				\$ 1,388,602		
Net interest earnings		\$ 21,057				\$ 19,957	
Net yield on interest earning assets			3.32	%			3.18%

(1) - For purposes of this table, nonaccrual loans are included in average loan balances.

(2) - Interest income on tax-exempt securities and loans has been adjusted assuming an effective tax rate of 34% for all periods presented.

The tax equivalent adjustment resulted in an increase in interest income of \$698,000 and \$695,000 for the periods ended

June 30, 2014 and June 30, 2013, respectively.

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Table II - Changes in Interest Margin Attributable
to Rate and Volume

In thousands	For the Six Months Ended June 30, 2014 versus June 30, 2013		
	Volume	Rate	Net
Increase (Decrease) Due to Change in:			
Interest earned on:			
Loans			
Taxable	\$ 338	\$ (1,335)	\$ (997)
Tax-exempt	36	2	38
Securities			
Taxable	(62)	587	525
Tax-exempt	93	(120)	(27)
Federal funds sold and interest bearing deposits with other banks	-	1	1
Total interest earned on interest earning assets	405	(865)	(460)
Interest paid on:			
Interest bearing demand deposits	9	(35)	(26)
Savings deposits	84	26	110
Time deposits	(401)	(695)	(1,096)
Short-term borrowings	80	5	85
Long-term borrowings and capital trust securities	(755)	122	(633)

Total interest paid on interest bearing liabilities	(983)	(577)	(1,560)
Net interest income	\$ 1,388	\$ (288)	\$ 1,100

Noninterest Income

Total noninterest income increased to \$5.49 million for the first six months of 2014, compared to \$5.45 million for the same period of 2013. Further detail regarding noninterest income is reflected in the following table.

Table III -
Noninterest Income

Dollars in thousands	For the Quarter Ended June 30,		For the Six Months Ended June 30,	
	2014	2013	2014	2013
Insurance commissions	\$ 1,091	\$ 1,132	\$ 2,273	\$ 2,316
Service fees related to deposit accounts	1,101	1,085	2,144	2,096
Realized securities gains (losses)	(43)	(57)	(64)	(16)
Other-than-temporary impairment of securities	(1)	(27)	(1)	(80)
Bank owned life insurance income	270	236	539	474
Other	287	334	598	660
Total	\$ 2,705	\$ 2,703	\$ 5,489	\$ 5,450

Other-than-temporary impairment of securities: We do not anticipate material charges for other-than-temporary impairment of securities in the near term.

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Noninterest Expense

Total noninterest expense decreased 10.6% for the six months ended June 30, 2014, as compared to the same period in 2013, with lower losses on sales of foreclosed properties and write-downs of foreclosed properties having the largest positive impacts. Table IV below shows the breakdown of the changes.

Table IV -
Noninterest
Expense

Dollars in thousands	For the Quarter Ended June 30, Change				For the Six Months Ended June 30, Change			
	2014	\$	%	2013	2014	\$	%	2013
Salaries, commissions, and employee benefits	\$ 4,045	\$ 58	1.5 %	\$ 3,987	\$ 8,026	\$ (79)	-1.0 %	\$ 8,105
Net occupancy expense	505	29	6.1 %	476	1,046	114	12.2 %	932
Equipment expense	513	(46)	-8.2 %	559	1,079	(67)	-5.8 %	1,146
Professional fees	282	(78)	-21.7 %	360	598	(24)	-3.9 %	622
Amortization of intangibles	63	(25)	-28.4 %	88	150	(26)	-14.8 %	176
FDIC premiums	495	(20)	-3.9 %	515	997	(58)	-5.5 %	1,055
Foreclosed properties expense	229	(66)	-22.4 %	295	482	(93)	-16.2 %	575
Loss on sales of foreclosed properties	54	(469)	-89.7 %	523	129	(434)	-77.1 %	563
Write-downs of foreclosed properties	962	(532)	-35.6 %	1,494	1,891	(532)	-22.0 %	2,423
Other	1,382	141	11.4 %	1,241	2,630	126	5.0 %	2,504
Total	\$ 8,530	\$ (1,008)	-10.6 %	\$ 9,538	\$ 17,028	\$ (1,073)	-5.9 %	\$ 18,101

Credit Experience

As a result of a historically slow economic recovery, our portfolio of OREO properties remains elevated. Prior elevated levels of loan delinquencies have returned to acceptable levels.

The provision for loan losses represents charges to earnings necessary to maintain an adequate allowance for probable credit losses inherent in the loan portfolio. Our determination of the appropriate level of the allowance is based on an

ongoing analysis of credit quality and loss potential in the loan portfolio, change in the composition and risk characteristics of the loan portfolio, and the anticipated influence of national and local economic conditions. The adequacy of the allowance for loan losses is reviewed quarterly and adjustments are made as considered necessary.

We recorded \$2.0 million and \$2.5 million provisions for loan losses for the first six months of 2014 and 2013, respectively. This decline is a result of lower levels of specific reserves necessary as a result of lower levels of impaired loans at June 30, 2014 compared to June 30, 2013.

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As illustrated in Table V below, our non-performing assets have decreased since year end 2013.

Table V - Summary of
Non-Performing Assets

Dollars in thousands	2014	June 30, 2013	December 31, 2013
Accruing loans past due 90 days or more	\$ -	\$ -	\$ -
Nonaccrual loans			
Commercial	415	3,996	1,224
Commercial real estate	1,537	1,695	2,318
Commercial construction and development	3,601	-	3,782
Residential construction and development	5,248	11,505	9,048
Residential real estate	3,289	13,605	2,446
Consumer	129	91	128
Total nonaccrual loans	14,219	30,892	18,946
Foreclosed properties			
Commercial	110	-	-
Commercial real estate	5,762	10,310	9,903
Commercial construction and development	10,363	11,492	11,125
Residential construction and development	20,557	21,591	20,485
Residential real estate	11,991	3,865	11,879
Total foreclosed properties	48,783	47,258	53,392
Repossessed assets	-	2	8
Total nonperforming assets	\$ 63,002	\$ 78,152	\$ 72,346
Total nonperforming loans as a percentage of total loans	1.42 %	3.29 %	1.99%
Total nonperforming assets as a percentage of total assets	4.39 %	5.70 %	5.22%
Allowance for loan losses as a percentage of nonperforming loans	77.40 %	55.10 %	66.82%
Allowance for loan losses as a percentage of period end loans	1.10 %	1.14 %	1.33%

The following table details the activity regarding our foreclosed properties for the three months and six months ended June 30, 2014 and 2013.

Property Activity	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2014	2013	2014	2013
Dollars in thousands				
Beginning balance	\$ 52,241	\$ 54,625	\$ 53,392	\$ 56,172
Acquisitions	672	1,467	1,949	2,798
Improvements	39	34	39	107
Disposals	(3,207)	(7,374)	(4,706)	(9,396)
Writedowns to fair value	(962)	(1,494)	(1,891)	(2,423)
Balance June 30	\$ 48,783	\$ 47,258	\$ 48,783	\$ 47,258

The following table details our most significant nonperforming loan relationships at June 30, 2014.

Table VII - Significant Nonperforming Loan Relationships

June 30,

2014

Dollars in thousands

Location	Underlying Collateral	Loan Origination Date	Loan Nonaccrual Date	Loan Balance	Method Used to Measure Impairment	Most Recent Appraised Value	Amount Allocated to Allowance for Loan Losses	Amount Previously Charged-off
Eastern Panhandle WV	Residential development & undeveloped acreage	Mar. 2008 & June 2008	Jun. 2011	\$3,000	Collateral value	\$4,617 (1)	\$-	\$ 5,424
Eastern Panhandle WV	Commercial development	Aug. 2006 & Apr. 2007	Aug. 2013	\$3,601	Collateral Value	\$5,979 (1)	\$-	\$ -

(1) - Values are based upon recent external appraisal.

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Refer to Note 6 of the accompanying consolidated financial statements for information regarding our past due loans, impaired loans, nonaccrual loans, and troubled debt restructurings.

We maintain the allowance for loan losses at a level considered adequate to provide for estimated probable credit losses inherent in the loan portfolio. The allowance is comprised of three distinct reserve components: (1) specific reserves related to loans individually evaluated, (2) quantitative reserves related to loans collectively evaluated, and (3) qualitative reserves related to loans collectively evaluated. A summary of the methodology we employ on a quarterly basis with respect to each of these components in order to evaluate the overall adequacy of our allowance for loan losses is as follows:

Specific Reserve for Loans Individually Evaluated

First, we identify loan relationships having aggregate balances in excess of \$500,000 and that may also have credit weaknesses. Such loan relationships are identified primarily through our analysis of internal loan evaluations, past due loan reports, and loans adversely classified by regulatory authorities. Each loan so identified is then individually evaluated to determine whether it is impaired – that is, based on current information and events, it is probable that we will be unable to collect all amounts due in accordance with the contractual terms of the underlying loan agreement. Substantially all of our impaired loans historically have been collateral dependent, meaning repayment of the loan is expected to be provided solely from the sale of the loan's underlying collateral. For such loans, we measure impairment based on the fair value of the loan's collateral, which is generally determined utilizing current appraisals. A specific reserve is established in an amount equal to the excess, if any, of the recorded investment in each impaired loan over the fair value of its underlying collateral, less estimated costs to sell. Our policy is to re-evaluate the fair value of collateral dependent loans at least every twelve months unless there is a known deterioration in the collateral's value, in which case a new appraisal is obtained.

Quantitative Reserve for Loans Collectively Evaluated

Second, we stratify the loan portfolio into the following ten loan pools: land and land development, construction, commercial, commercial real estate -- owner-occupied, commercial real estate -- non-owner occupied, conventional residential mortgage, jumbo residential mortgage, home equity, consumer, and other. Loans within each pool are then further segmented between (1) loans which were individually evaluated for impairment and not deemed to be impaired, (2) larger-balance loan relationships exceeding \$2 million which are assigned an internal risk rating in conjunction with our normal ongoing loan review procedures and (3) smaller-balance homogenous loans.

Quantitative reserves relative to each loan pool are established as follows: for all loan segments detailed above, an allocation equaling 100% of the respective pool's average 12 month historical net loan charge-off rate (determined based upon the most recent twelve quarters) is applied to the aggregate recorded investment in the pool of loans.

Qualitative Reserve for Loans Collectively Evaluated

Third, we consider the necessity to adjust our average historical net loan charge-off rates relative to each of the above ten loan pools for potential risk factors that could result in actual losses deviating from prior loss experience. For example, if we observe a significant increase in delinquencies within the conventional mortgage loan pool above historical trends, an additional allocation to the average historical loan charge-off rate is applied. Such qualitative risk factors considered are: (1) levels of and trends in delinquencies and impaired loans, (2) levels of and trends in charge-offs and recoveries, (3) trends in volume and term of loans, (4) effects of any changes in risk selection and underwriting standards, and other changes in lending policies, procedures, and practice, (5) experience, ability, and

depth of lending management and other relevant staff, (6) national and local economic trends and conditions, (7) industry conditions, and (8) effects of changes in credit concentrations.

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Relationship between Allowance for Loan Losses, Net Charge-offs and Nonperforming Loans

In analyzing the relationship between the allowance for loan losses, net loan charge-offs and nonperforming loans, it is helpful to understand the process of how loans are treated as they deteriorate over time. Reserves for loans are established at origination through the quantitative and qualitative reserve process discussed above.

Charge-offs, if necessary, are typically recognized in a period after the reserves were established. If the previously established reserves exceed that needed to satisfactorily resolve the problem credit, a reduction in the overall level of the reserve could be recognized. In summary, if loan quality deteriorates, the typical credit sequence is periods of reserve building, followed by periods of higher net charge-offs.

Consumer loans are generally charged off to the allowance for loan losses upon reaching specified stages of delinquency, in accordance with the Federal Financial Institutions Examination Council policy. For example, credit card loans are charged off by the end of the month in which the account becomes 180 days past due or within 60 days from receiving notification about a specified event (e.g., bankruptcy of the borrower), whichever is earlier. Residential mortgage loans are generally charged off to net realizable value no later than when the account becomes 180 days past due. Other consumer loans, if collateralized, are generally charged off to net realizable value at 120 days past due.

Commercial-related loans (which are risk-rated) are charged off to the allowance for loan losses when the loss has been confirmed. This determination includes many factors, including the prioritization of our claim in bankruptcy, expectations of the workout/restructuring of the loan and valuation of the borrower's equity.

Substantially all of our nonperforming loans are secured by real estate. The majority of these loans were underwritten in accordance with our loan-to-value policy guidelines which range from 70-85% at the time of origination. The fair values of the underlying collateral value remains in excess of the recorded investment in many of our nonperforming loans, and therefore, no specific reserve allocation is required; as of June 30, 2014, approximately 78% of our impaired loans required no reserves or have been charged down to their fair value.

At June 30, 2014, December 31, 2013, and June 30, 2013, our allowance for loan losses totaled \$11.0 million, or 1.10% of total loans, \$12.7 million, or 1.33% of total loans and \$14.1 million, or 1.50% of total loans, respectively, and is considered adequate to cover our estimate of probable credit losses inherent in our loan portfolio.

At June 30, 2014, December 31, 2013, and June 30, 2013, we had approximately \$48.8 million, \$53.4 million and \$47.3 million, respectively, in other real estate owned which was obtained as the result of foreclosure proceedings. Although foreclosed property is recorded at fair value less estimated costs to sell, the prices ultimately realized upon their sale may or may not result in us recognizing loss.

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FINANCIAL CONDITION

Our total assets were \$1.436 billion at June 30, 2014, compared to \$1.387 billion at December 31, 2013, representing a 3.6% increase. Table VIII below serves to illustrate significant changes in our financial position between December 31, 2013 and June 30, 2014.

Table VIII - Summary of Significant Changes in Financial Position

Dollars in thousands	Balance	Increase (Decrease)		Balance
	December 31, 2013	Amount	Percentage	June 30, 2014
Assets				
Securities available for sale	\$ 288,780	(897)	-0.3 %	\$ 287,883
Loans, net of unearned interest	937,070	55,746	5.9 %	992,816
Liabilities				
Deposits	\$ 1,003,812	\$ 53,983	5.4 %	\$ 1,057,795
Short-term borrowings	62,769	28,960	46.1 %	91,729
Long-term borrowings	163,516	(41,574)	-25.4 %	121,942

Loan growth of 5.9% during the first six months of 2014 occurred principally in the commercial real estate and residential real estate portfolios, and was funded primarily with deposits.

Deposits increased approximately \$54.0 million during the first six months of 2014; savings deposits increased approximately \$49.9 million.

The increase in short-term borrowings and the decrease in long term borrowings is primarily attributable to maturities and repayments of long-term FHLB advances during the first six months of 2014, of which a portion was refinanced with short-term FHLB advances.

Refer to Notes 5, 6, 9, and 10 of the notes to the accompanying consolidated financial statements for additional information with regard to changes in the composition of our securities, loans, deposits and borrowings between June 30, 2014 and December 31, 2013.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity reflects our ability to ensure the availability of adequate funds to meet loan commitments and deposit withdrawals, as well as provide for other transactional requirements. Liquidity is provided primarily by funds invested in cash and due from banks (net of float and reserves), Federal funds sold, non-pledged securities, and available lines of credit with the Federal Home Loan Bank of Pittsburgh (“FHLB”) and Federal Reserve Bank of Richmond, which totaled approximately \$617 million or 42.97% of total consolidated assets at June 30, 2014.

Our liquidity strategy is to fund loan growth with deposits and other borrowed funds while maintaining an adequate level of short- and medium-term investments to meet normal daily loan and deposit activity. As a member of the FHLB, we have access to approximately \$479 million. As of June 30, 2014 and December 31, 2013, these advances totaled approximately \$127 million and \$136 million, respectively. At June 30, 2014, we had additional borrowing capacity of \$352 million through FHLB programs. We have established a line with the Federal Reserve Bank to be used as a contingency liquidity vehicle. The amount available on this line at June 30, 2014 was approximately \$94 million, which is secured by a pledge of our consumer and commercial and industrial loan portfolios. We have a \$6 million unsecured line of credit with a correspondent bank. Also, we classify all of our securities as available for sale to enable us to liquidate them if the need arises.

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Liquidity risk represents the risk of loss due to the possibility that funds may not be available to satisfy current or future commitments based on external market issues, customer or creditor perception of financial strength, and events unrelated to Summit such as war, terrorism, or financial institution market specific issues. The Asset/Liability Management Committee ("ALCO"), comprised of members of senior management and certain members of the Board of Directors, oversees our liquidity risk management process. The ALCO develops and recommends policies and limits governing our liquidity to the Board of Directors for approval with the objective of ensuring that we can obtain cost-effective funding to meet current and future obligations, as well as maintain sufficient levels of on-hand liquidity, under both normal and "stressed" circumstances.

We continuously monitor our liquidity position to ensure that day-to-day as well as anticipated funding needs are met. We are not aware of any trends, commitments, events or uncertainties that have resulted in or are reasonably likely to result in a material change to our liquidity.

One of our continuous goals is maintenance of a strong capital position. Through management of our capital resources, we seek to provide an attractive financial return to our shareholders while retaining sufficient capital to support future growth. Shareholders' equity at June 30, 2014 totaled \$117.5 million compared to \$111.1 million at December 31, 2013.

Summit and Summit Community have entered into informal Memoranda of Understanding ("MOU's") with their respective regulatory authorities. A memorandum of understanding is characterized by the regulatory authorities as an informal action that is not published or publicly available and that is used when circumstances warrant a milder form of action than a formal supervisory action, such as a formal written agreement or order.

See Note 13 of the notes to the accompanying consolidated financial statements and Risks Relating to Our Business of the Risk Factors section of the 2013 Annual Report on Form 10K for specific details of the MOUs.

Refer to Note 13 of the notes to the accompanying consolidated financial statements for additional information regarding regulatory restrictions on our capital as well as our subsidiaries' capital.

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CONTRACTUAL CASH OBLIGATIONS

During our normal course of business, we incur contractual cash obligations. The following table summarizes our contractual cash obligations at June 30, 2014.

Table IX -
Contractual
Cash
Obligations

	Long Term Debt	Capital Trust Securities	Operating Leases
Dollars in thousands			
2014	\$ 43,952	\$ -	\$ 125
2015	11,909	-	128
2016	28,911	-	90
2017	918	-	45
2018	45,017	-	-
Thereafter	8,035	19,589	-
Total	\$ 138,742	\$ 19,589	\$ 388

OFF-BALANCE SHEET ARRANGEMENTS

We are involved with some off-balance sheet arrangements that have or are reasonably likely to have an effect on our financial condition, liquidity, or capital. These arrangements at June 30, 2014 are presented in the following table.

Table X - Off-Balance Sheet
Arrangements

	June 30, 2014
Dollars in thousands	
Commitments to extend credit:	
Revolving home equity and credit card lines	\$ 51,340
Construction loans	22,618
Other loans	43,683
Standby letters of credit	1,668
Total	\$ 119,309

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MARKET RISK MANAGEMENT

Market risk is the risk of loss arising from adverse changes in the fair value of financial instruments due to changes in interest rates, exchange rates and equity prices. Interest rate risk is our primary market risk and results from timing differences in the repricing of assets, liabilities and off-balance sheet instruments, changes in relationships between rate indices and the potential exercise of imbedded options. The principal objective of asset/liability management is to minimize interest rate risk and our actions in this regard are taken under the guidance of our Asset/Liability Management Committee ("ALCO"), which is comprised of members of senior management and members of the Board of Directors. The ALCO actively formulates the economic assumptions that we use in our financial planning and budgeting process and establishes policies which control and monitor our sources, uses and prices of funds.

Some amount of interest rate risk is inherent and appropriate to the banking business. Our net income is affected by changes in the absolute level of interest rates. Our interest rate risk position is liability sensitive. The nature of our lending and funding activities tends to drive our interest rate risk position to being liability sensitive. That is, absent any changes in the volumes of our interest earning assets or interest bearing liabilities, liabilities are likely to reprice faster than assets, resulting in a decrease in net income in a rising rate environment. Net income would increase in a falling interest rate environment. Net income is also subject to changes in the shape of the yield curve. In general, a flattening yield curve would result in a decline in our earnings due to the compression of earning asset yields and funding rates, while a steepening would result in increased earnings as margins widen.

Several techniques are available to monitor and control the level of interest rate risk. We primarily use earnings simulations modeling to monitor interest rate risk. The earnings simulation model forecasts the effects on net interest income under a variety of interest rate scenarios that incorporate changes in the absolute level of interest rates and changes in the shape of the yield curve. Each increase or decrease in interest rates is assumed to gradually take place over the next 12 months, and then remain stable, except for the up 400 scenario, which assumes a gradual increase in rates over 24 months. Assumptions used to project yields and rates for new loans and deposits are derived from historical analysis. Securities portfolio maturities and prepayments are reinvested in like instruments. Mortgage loan prepayment assumptions are developed from industry estimates of prepayment speeds. Noncontractual deposit repricings are modeled on historical patterns.

The following table presents the estimated sensitivity of our net interest income to changes in interest rates, as measured by our earnings simulation model as of June 30, 2014. The sensitivity is measured as a percentage change in net interest income given the stated changes in interest rates (gradual change over 12 months, stable thereafter for the down 100 and the up 200 scenarios, and gradual change over 24 months for the up 400 scenario) compared to net interest income with rates unchanged in the same period. The estimated changes set forth below are dependent on the assumptions discussed above and are well within our ALCO policy limits shown below relative to reductions in net interest income over the ensuing twelve month period.

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Change in Interest Rates	Estimated % Change in Net Interest Income over:		
	0 - 12 Months	13 - 24 Months	
	Policy	Actual	Actual
Down 100 basis points (1)	-7 %	-0.22 %	1.02%
Up 200 basis points (1)	-10 %	-4.51 %	-5.70%
Up 400 basis points (2)	-15 %	-3.57 %	-10.82%

(1) assumes a parallel shift in the yield curve over 12 months

(2) assumes a parallel shift in the yield curve over 24 months

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CONTROLS AND PROCEDURES

Our management, including the Chief Executive Officer and Chief Financial Officer, has conducted as of June 30, 2014, an evaluation of the effectiveness of disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e). Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures as of June 30, 2014 were effective. There were no changes in our internal control over financial reporting that occurred during the quarter ended June 30, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Summit Financial Group, Inc. and Subsidiaries
Part II. Other Information

Item 1. Legal Proceedings

Refer to Note 12 of the Notes to the Consolidated Financial Statements in Part I, Item 1 for information regarding legal proceedings not reportable under this Item.

Item 1A. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2013.

Item 6. Exhibits

Exhibit Amended and Restated Articles of
3.i Incorporation of Summit Financial
Group, Inc.

Exhibit Articles of Amendment 2009
3.ii

Exhibit Articles of Amendment 2011
3.iii

Exhibit Amended and Restated By-Laws of
3.iv Summit Financial Group, Inc.

Exhibit Statement re: Computation of Earnings
11 per Share – Information contained in Note
4 to the Consolidated Financial
Statements on page 15 of this Quarterly
Report is incorporated herein by
reference.

Exhibit Sarbanes-Oxley Act Section 302
31.1 Certification of Chief Executive Officer

Exhibit Sarbanes-Oxley Act Section 302
31.2 Certification of Chief Financial Officer

Exhibit Sarbanes-Oxley Act Section 906
32.1 Certification of Chief Executive Officer

Exhibit Sarbanes-Oxley Act Section 906
32.2 Certification of Chief Financial Officer

Exhibit Interactive Data File (XBRL)
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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.

SUMMIT FINANCIAL GROUP, INC.
(registrant)

By: /s/ H. Charles Maddy, III
H. Charles Maddy, III,
President and Chief Executive Officer

By: /s/ Robert S. Tissue
Robert S. Tissue,
Senior Vice President and Chief Financial Officer

By: /s/ Julie R. Cook
Julie R. Cook,
Vice President and Chief Accounting Officer

Date: August 8, 2014

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EXHIBIT INDEX

Exhibit No.	Description	Page Number
(3)	Articles of Incorporation and By-laws:	
	(i) Amended and Restated Articles of Incorporation of Summit Financial Group, Inc.	(a)
	(ii) Articles of Amendment 2009	(b)
	(iii) Articles of Amendment 2011	(c)
	(iv) Amended and Restated By-laws of Summit Financial Group, Inc.	(d)
11	Statement re: Computation of Earnings per Share	15
31.1	Sarbanes-Oxley Act Section 302 Certification of Chief Executive Officer	
31.2	Sarbanes-Oxley Act Section 302 Certification of Chief Financial Officer	
32.1*	Sarbanes-Oxley Act Section 906 Certification of Chief Executive Officer	
32.2*	Sarbanes-Oxley Act Section 906 Certification of Chief Financial Officer	
101**	Interactive data file (XBRL)	

* Furnished, not filed.

**As provided in Rule 406T of Regulation S-T, this information is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934.

- (a) Incorporated by reference to Exhibit 3.i of Summit Financial Group, Inc.'s filing on Form 10-Q dated March 31, 2006.
- (b) Incorporated by reference to Exhibit 3.1 of Summit Financial Group, Inc.'s filing on Form 8-K dated September 30, 2009.
- (c) Incorporated by reference to Exhibit 3.1 of Summit Financial Group, Inc.'s filing on Form 8-K dated November 3, 2011.
- (d) Incorporated by reference to Exhibit 3.2 of Summit Financial Group, Inc.'s filing on Form 10-Q dated June 30, 2006.

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