

United States Securities and Exchange Commission
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2017

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

For the transition period from _____ to _____

Commission File Number: **333-203449**



SmartFinancial, Inc.

(Exact name of small business issuer as specified in its charter)

Tennessee

(State or other jurisdiction of incorporation or organization)

62-1173944

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

5401 Kingston Pike, Suite 600 Knoxville, Tennessee

(Address of principal executive offices)

37919

(Zip Code)

865-453-2650

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such 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 the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Emerging growth company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

As of August 8, 2017 there were 8,221,761 shares of common stock, \$1.00 par value per share, issued and outstanding.

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FORWARD-LOOKING STATEMENTS

SmartFinancial, Inc. (“SmartFinancial”) may from time to time make written or oral statements, including statements contained in this report (including, without limitation, certain statements in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Item 2), that constitute forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934 (the “Exchange Act”). The words “expect,” “anticipate,” “intend,” “consider,” “plan,” “believe,” “seek,” “should,” “estimate,” and similar expressions are intended to identify such forward-looking statements, but other statements may constitute forward-looking statements. These statements should be considered subject to various risks and uncertainties. Such forward-looking statements are made based upon management’s belief as well as assumptions made by, and information currently available to, management pursuant to “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995. SmartFinancial’s actual results may differ materially from the results anticipated in forward-looking statements due to a variety of factors. Such factors include, without limitation, those specifically described in Item 1A of Part I of the Company’s 2016 Annual Report on Form 10-K, as well as the following: (i) the possibility that our asset quality would decline or that we experience greater loan losses than anticipated, (ii) increased levels of other real estate, primarily as a result of foreclosures, (iii) the impact of liquidity needs on our results of operations and financial condition, (iv) competition from financial institutions and other financial service providers, (v) economic conditions in the local markets where we operate, (vi) our ability to consummate and realize all of the anticipated benefits of the merger between Capstone and SmartBank and the acquisition of the Cleveland, TN branch, (vii) the impact of negative developments in the financial industry and U.S. and global capital and credit markets, (viii) the impact of recently enacted legislation on our business, (ix) the relatively greater credit risk of commercial real estate loans and construction and land development loans in our loan portfolio, (x) adverse impact on operations and financial condition of changes in interest rates, (xi) the impact of recently enacted legislation on our business, (xii) the impact of federal and state regulations on our operations and financial performance, (xiii) our ability to retain the services of key personnel, (xiv) the impact of Tennessee’s anti-takeover statutes and certain charter provisions on potential acquisitions of the holding company, and (xv) our ability to adapt to technological changes. Many of such factors are beyond SmartFinancial’s ability to control or predict, and readers are cautioned not to put undue reliance on such forward-looking statements. SmartFinancial does not intend to update or reissue any forward-looking statements contained in this report as a result of new information or other circumstances that may become known to SmartFinancial.

Non-GAAP Financial Measures

Under SEC Regulation G, public companies making disclosures containing financial measures that are not in accordance with GAAP must also disclose, along with each non-GAAP financial measure, certain additional information, including a reconciliation of the non-GAAP financial measure to the closest comparable GAAP financial measure, as well as a statement of the company’s reasons for utilizing the non-GAAP financial measure. The SEC has exempted from the definition of non-GAAP financial measures certain commonly used financial measures that are not based on GAAP. However, two non-GAAP financial measures commonly used by financial institutions, namely tax-equivalent net interest income and tax-equivalent net interest margin (as presented in the tables in the section labeled “Net Interest Income and Yield Analysis”), have not been specifically exempted by the SEC, and may therefore constitute non-GAAP financial measures under Regulation G. We are unable to state with certainty whether the SEC would regard those measures as subject to Regulation G. Management believes that these non-GAAP financial measures are useful in evaluating the Company’s financial performance and facilitate comparisons with the performance of other financial institutions. However, that information should be considered supplemental in nature and not as a substitute for related financial information prepared in accordance with GAAP.

PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SMARTFINANCIAL, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

	Unaudited June 30, 2017	December 31, 2016
ASSETS		
Cash and due from banks	\$ 54,553,718	\$ 34,290,617
Interest-bearing deposits at other financial institutions	28,281,708	34,457,691
Total cash and cash equivalents	82,835,426	68,748,308
Securities available for sale	132,761,710	129,421,914
Restricted investments, at cost	6,080,700	5,627,950
Loans, net of allowance for loan losses of \$5,498,169 at June 30, 2017 and \$5,105,255 at December 31, 2016	859,922,516	808,271,003
Bank premises and equipment, net	33,764,516	30,535,594
Foreclosed assets	2,369,056	2,386,239
Goodwill and core deposit intangible, net	7,492,177	6,635,655
Cash surrender value of life insurance	11,391,637	1,320,723
Other assets	8,861,374	9,508,899
Total assets	\$ 1,145,479,112	\$ 1,062,456,285
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Noninterest-bearing demand deposits	\$ 183,324,236	\$ 153,482,650
Interest-bearing demand deposits	156,149,846	162,702,457
Money market and savings deposits	324,014,445	274,604,724
Time deposits	318,146,778	316,275,340
Total deposits	981,635,305	907,065,171
Securities sold under agreement to repurchase	22,945,984	26,621,984
Federal Home Loan Bank advances and other borrowings	—	18,505,390
Accrued expenses and other liabilities	6,163,812	5,023,600
Total liabilities	1,010,745,101	957,216,145
Stockholders' equity:		
Preferred stock - \$1 par value; 2,000,000 shares authorized; None issued and outstanding in 2017. 12,000 issued and outstanding in 2016.	—	12,000
Common stock - \$1 par value; 40,000,000 shares authorized; 8,219,261 and 5,896,033 shares issued and outstanding in 2017 and 2016, respectively	8,219,261	5,896,033
Additional paid-in capital	106,793,832	83,463,051
Retained earnings	19,968,434	16,871,296
Accumulated other comprehensive loss	(247,516)	(1,002,240)
Total stockholders' equity	134,734,011	105,240,140
Total liabilities and stockholders' equity	\$ 1,145,479,112	\$ 1,062,456,285

The Notes to Consolidated Financial Statements are an integral part of these statements.

SMARTFINANCIAL, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME

	Unaudited Three Months Ended June 30,		Unaudited Six Months Ended June 30,	
	2017	2016	2017	2016
INTEREST INCOME				
Loans, including fees	\$ 10,747,217	\$ 9,954,218	\$ 20,962,823	\$ 19,328,675
Securities and interest-bearing deposits at other financial institutions	692,223	665,402	1,353,043	1,381,982
Federal funds sold and other earning assets	78,049	50,171	150,946	113,481
Total interest income	<u>11,517,489</u>	<u>10,669,791</u>	<u>22,466,812</u>	<u>20,824,138</u>
INTEREST EXPENSE				
Deposits	1,241,551	1,012,684	2,339,089	1,973,951
Securities sold under agreements to repurchase	15,588	15,279	31,539	31,739
Federal Home Loan Bank advances and other borrowings	11,682	29,263	27,156	74,549
Total interest expense	<u>1,268,821</u>	<u>1,057,226</u>	<u>2,397,784</u>	<u>2,080,239</u>
Net interest income before provision for loan losses	10,248,668	9,612,565	20,069,028	18,743,899
Provision for loan losses	298,033	218,420	310,482	355,976
Net interest income after provision for loan losses	<u>9,950,635</u>	<u>9,394,145</u>	<u>19,758,546</u>	<u>18,387,923</u>
NONINTEREST INCOME				
Customer service fees	290,626	258,877	555,299	554,680
Gain on sale of securities	—	98,100	—	181,363
Gain on sale of loans and other assets	405,418	197,479	680,583	419,405
(Loss) gain on sale of foreclosed assets	500	(3,734)	(15,064)	54,243
Other noninterest income	555,963	410,155	958,396	822,018
Total noninterest income	<u>1,252,507</u>	<u>960,877</u>	<u>2,179,214</u>	<u>2,031,709</u>
NONINTEREST EXPENSES				
Salaries and employee benefits	4,757,618	4,486,148	9,404,367	8,981,156
Net occupancy and equipment expense	962,593	1,136,648	1,941,052	2,155,075
Depository insurance	60,987	150,943	214,286	286,747
Foreclosed assets	12,008	63,773	10,521	120,431
Advertising	129,398	184,065	293,659	357,510
Data processing	475,343	554,612	808,558	895,992
Professional services	473,351	551,432	1,043,192	1,006,605
Amortization of intangible assets	61,071	93,353	113,648	186,706
Service contracts	312,905	315,611	608,534	601,239
Other operating expenses	1,583,888	935,740	2,536,257	1,832,765
Total noninterest expenses	<u>8,829,162</u>	<u>8,472,325</u>	<u>16,974,074</u>	<u>16,424,226</u>
Income before income tax expense	2,373,980	1,882,697	4,963,686	3,995,406
Income tax expense	725,694	691,067	1,671,548	1,454,913
Net income	<u>1,648,286</u>	<u>1,191,630</u>	<u>3,292,138</u>	<u>2,540,493</u>
Preferred stock dividends	—	270,000	195,000	482,000
Net income available to common stockholders	<u>\$ 1,648,286</u>	<u>\$ 921,630</u>	<u>\$ 3,097,138</u>	<u>\$ 2,058,493</u>
EARNINGS PER COMMON SHARE				
Basic	<u>\$ 0.20</u>	<u>\$ 0.16</u>	<u>\$ 0.39</u>	<u>\$ 0.35</u>
Diluted	<u>0.20</u>	<u>0.15</u>	<u>0.39</u>	<u>0.34</u>
Weighted average common shares outstanding				
Basic	<u>8,216,567</u>	<u>5,820,342</u>	<u>7,872,609</u>	<u>5,813,915</u>
Diluted	<u>8,325,538</u>	<u>6,131,820</u>	<u>7,977,282</u>	<u>6,118,530</u>

Dividends per share

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The Notes to Consolidated Financial Statements are an integral part of these statements.

SMARTFINANCIAL, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Unaudited Three Months Ended June 30,	
	2017	2016
Net income	\$ 1,648,286	\$ 1,191,630
Other comprehensive income, net of tax:		
Unrealized holding gains arising during the period, net of tax expense of \$270,461 and \$76,857 in 2017 and 2016, respectively	435,890	124,607
Reclassification adjustment for gains included in net income, net of tax expense of \$0 and \$32,278 in 2017 and 2016, respectively	—	(60,822)
Total other comprehensive income	435,890	63,785
Comprehensive income	<u>\$ 2,084,176</u>	<u>\$ 1,255,415</u>

	Unaudited Six Months Ended June 30,	
	2017	2016
Net income	\$ 3,292,138	\$ 2,540,493
Other comprehensive income, net of tax:		
Unrealized holding gains arising during the period, net of tax expense of \$468,293 and \$458,148 in 2017 and 2016, respectively	754,724	739,315
Reclassification adjustment for gains included in net income, net of tax expense of \$- and \$68,918 in 2017 and 2016, respectively	—	(112,445)
Total other comprehensive income	754,724	626,870
Comprehensive income	<u>\$ 4,046,862</u>	<u>\$ 3,167,363</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

SMARTFINANCIAL, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY - UNAUDITED
For the Six Months Ended June 30, 2017

	Preferred Shares	Common Shares	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
BALANCE, December 31, 2016	12,000	5,896,033	\$ 12,000	\$ 5,896,033	\$ 83,463,051	\$ 16,871,296	\$ (1,002,240)	\$ 105,240,140
Net income	—	—	—	—	—	3,292,138	—	3,292,138
Other comprehensive income	—	—	—	—	—	—	754,724	754,724
Issuance of common stock	—	1,840,000	—	1,840,000	31,094,676	—	—	32,934,676
Issuance of stock grants	—	1,511	—	1,511	30,280	—	—	31,791
Exercise of stock options	—	481,717	—	481,717	4,143,295	—	—	4,625,012
Cash dividend on preferred stock	—	—	—	—	—	(195,000)	—	(195,000)
Redemption of preferred stock	(12,000)	—	(12,000)	—	(11,988,000)	—	—	(12,000,000)
Stock compensation expense	—	—	—	—	50,530	—	—	50,530
BALANCE, June 30, 2017	—	8,219,261	\$ —	\$ 8,219,261	\$ 106,793,832	\$ 19,968,434	\$ (247,516)	\$ 134,734,011

The Notes to Consolidated Financial Statements are an integral part of these statements.

SMARTFINANCIAL, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Unaudited Six Months Ended June 30,	
	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 3,292,138	\$ 2,540,493
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,165,930	1,063,117
Provision for loan losses	310,482	355,976
Stock compensation expense	50,530	66,635
Gains from sale of securities	—	(181,363)
Net gains from sale of loans and other assets	(680,583)	(419,405)
Net losses (gains) from sale of foreclosed assets	15,064	(54,243)
Changes in other assets and liabilities:		
Accrued interest receivable	18,144	280,727
Accrued interest payable	13,117	4,315
Other assets and liabilities	1,457,176	5,330,459
Net cash provided by operating activities	<u>5,641,998</u>	<u>8,986,711</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from security sales, maturities, and paydowns	10,062,386	29,349,635
Purchase of securities	(12,507,860)	(5,000,000)
Purchase of bank owned life insurance	(10,070,914)	—
Purchase of restricted investments	(452,750)	(200)
Net cash for purchase of branch acquisition	(1,049,878)	—
Loan originations and principal collections, net	(27,248,001)	(45,399,008)
Purchase of bank premises and equipment	(1,226,898)	(1,454,765)
Proceeds from sale of foreclosed assets	41,636	652,364
Net cash used in investing activities	<u>(42,452,279)</u>	<u>(21,851,974)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in deposits	47,682,310	30,266,395
Net decrease in securities sold under agreements to repurchase	(3,676,000)	(1,185,467)
Issuance of common stock	37,591,479	135,079
Redemption of preferred stock	(12,000,000)	—
Payment of dividends on preferred stock	(195,000)	(482,000)
Proceeds from Federal Home Loan Bank advances and other borrowings	79,268,072	100,000
Repayment of Federal Home Loan Bank advances and other borrowings	(97,773,462)	(24,196,260)
Net cash provided by financing activities	<u>50,897,399</u>	<u>4,637,747</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	14,087,118	(8,227,516)
CASH AND CASH EQUIVALENTS, beginning of year	68,748,308	79,964,633
CASH AND CASH EQUIVALENTS, end of period	<u>\$ 82,835,426</u>	<u>\$ 71,737,117</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the period for interest	\$ 2,374,250	\$ 2,075,924
Cash paid during the period for taxes	1,366,172	726,528
NONCASH INVESTING AND FINANCING ACTIVITIES		
Change in unrealized losses on securities available for sale	\$ (1,223,017)	\$ (1,016,100)
Acquisition of real estate through foreclosure	39,517	1,296,077
Financed sales of foreclosed assets	—	1,120,138

The Notes to Consolidated Financial Statements are an integral part of these statements.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1. Presentation of Financial Information

Nature of Business:

SmartFinancial, Inc. (the “Company”) is a bank holding company whose principal activity is the ownership and management of its wholly-owned subsidiary, SmartBank (the “Bank”). The Company provides a variety of financial services to individuals and corporate customers through its offices in eastern Tennessee, northwest Florida, and north Georgia. The Company’s primary deposit products are interest-bearing demand deposits and certificates of deposit. Its primary lending products are commercial, residential, and consumer loans. On May 22, 2017, the Company along with the Bank entered into an agreement and plan of merger with Capstone Bancshares, Inc., an Alabama corporation and Capstone Bank, an Alabama-chartered commercial bank and wholly owned subsidiary of Capstone Bancshares, Inc where the Company will be the surviving entity and Capstone Bank will merge with and into the Bank. A copy of the agreement and plan of merger is attached as Exhibit 2.1 and is incorporated by reference herein.

Interim Financial Information (Unaudited):

The financial information in this report for June 30, 2017 and June 30, 2016 has not been audited. The information included herein should be read in conjunction with the Company’s 2016 annual consolidated financial statements and footnotes included elsewhere. The consolidated financial statements presented herein conform to U.S. generally accepted accounting principles and to general industry practices. In the opinion of SmartFinancial’s management, the accompanying interim financial statements contain all material adjustments necessary to present fairly the financial condition, the results of operations, and cash flows for the interim period. Results for interim periods are not necessarily indicative of the results to be expected for a full year.

Basis of Presentation and Accounting Estimates:

All adjustments consisting of normal recurring accruals, that in the opinion of management, are necessary for a fair presentation of the financial position and the results of operations for the periods covered by the report have been included. The accompanying unaudited consolidated financial statements and related notes should be read in conjunction with those appearing in the 2016 Annual Report previously filed on Form 10-K.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary. All significant intercompany balances and transactions have been eliminated in consolidation.

In preparing the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet, and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of foreclosed assets and deferred taxes, other-than-temporary impairments of securities, and the fair value of financial instruments.

The determination of the adequacy of the allowance for loan losses is based on estimates that are particularly susceptible to significant changes in the economic environment and market conditions. In connection with the determination of the estimated losses on loans, management obtains independent appraisals for significant collateral.

The Company’s loans are generally secured by specific items of collateral including real property, consumer assets, and business assets. Although the Company has a diversified loan portfolio, a substantial portion of its debtors’ ability to honor their contracts is dependent on local economic conditions.

While management uses available information to recognize losses on loans, further reductions in the carrying amounts of loans may be necessary based on changes in local economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the estimated losses on loans. Such agencies may require the Company to recognize additional losses based on their judgments about information available to them at the time of their examination. Because of these factors, it is reasonably possible that the estimated losses on loans may change materially in the near term. However, the amount of the change that is reasonably possible cannot be estimated.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 1. Presentation of Financial Information, Continued

Recently Issued Accounting Pronouncements:

During interim periods, the Company follows the accounting policies set forth in its annual audited financial statements for the year ended December 31, 2016 as filed with the Securities and Exchange Commission. The following is a summary of recent authoritative pronouncements not yet effective that could impact the accounting, reporting, and/or disclosure of financial information by the Company issued since December 31, 2016 .

In January 2017, FASB issued ASU No. 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business*. The ASU clarifies the definition of a business to assist with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The amendments in this update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company does not expect these amendments to have a material effect on its financial statements.

In January 2017, FASB issued ASU No. 2017-04, *Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment* . The ASU simplifies the subsequent measurement of goodwill and eliminates Step 2 from the goodwill impairment test. The Company should perform its goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An impairment charge should be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value. The impairment charge is limited to the amount of goodwill allocated to that reporting unit. The amendments in this update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted for goodwill impairment tests performed on testing dates after January 1, 2017. The Company does not expect these amendments to have a material effect on its financial statements.

In March 2017, FASB issued ASU No. 2017-08, *Receivables - Nonrefundable Fees and Other Costs (Topic 310-20): Premium Amortization on Purchased Callable Debt Securities*. The ASU shortens the amortization period for certain callable debt securities held at a premium. The premium on individual callable debt securities shall be amortized to the earliest call date. This guidance does not apply to securities for which prepayments are estimated on a large number of similar loans where prepayments are probable and reasonably estimable. The amendments in this update are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. This update should be adopted on a modified retrospective basis with a cumulative-effect adjustment to retained earnings on the date of adoption. The Company does not expect these amendments to have a material effect on its financial statements.

Reclassifications:

Certain captions and amounts in the 2016 financial statements were reclassified to conform to the 2017 presentation.

Earnings per common share:

Basic earnings per common share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate solely to outstanding stock options and are determined using the treasury stock method.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 2. Earnings per share

The following is a summary of the basic and diluted earnings per share for the three and six month periods ended June 30, 2017 and June 30, 2016 .

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Net income available to common shareholders	\$ 1,648,286	\$ 921,630	\$ 3,097,138	\$ 2,058,493
Weighted average common shares outstanding	8,216,567	5,820,342	7,872,609	5,813,915
Effect of dilutive stock options	108,971	311,478	104,673	304,615
Diluted shares	8,325,538	6,131,820	7,977,282	6,118,530
Basic earnings per common share	\$ 0.20	\$ 0.16	\$ 0.39	\$ 0.35
Diluted earnings per common share	\$ 0.20	\$ 0.15	\$ 0.39	\$ 0.34

For the three and six months ended June 30, 2017 and 2016 , the effects of outstanding antidilutive stock options are excluded from the computation of diluted earnings per common share because the exercise price of such options is higher than the market price. There were 13,916 and 18,100 antidilutive stock options as of June 30, 2017 and 2016 , respectively.

Note 3. Securities

The amortized cost and fair value of securities available-for-sale at June 30, 2017 and December 31, 2016 are summarized as follows (in thousands):

	June 30, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Government-sponsored enterprises (GSEs)	\$ 18,244	\$ 5	\$ (278)	\$ 17,971
Municipal securities	8,362	77	(42)	8,397
Other debt securities	972	—	(24)	948
Mortgage-backed securities	105,585	347	(486)	105,446
	\$ 133,163	\$ 429	\$ (830)	\$ 132,762

	December 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Government-sponsored enterprises (GSEs)	\$ 18,279	\$ 8	\$ (564)	\$ 17,723
Municipal securities	8,182	16	(179)	8,019
Mortgage-backed securities	104,585	185	(1,090)	103,680
	\$ 131,046	\$ 209	\$ (1,833)	\$ 129,422

At June 30, 2017 , securities with a fair value totaling approximately \$81,000,000 were pledged to secure public funds and securities sold under agreements to repurchase.

For the three and six months ended June 30, 2017 , there were no available-for-sale securities sold. For the three and six months ended June 30, 2016 there were available-for-sale securities sold with proceeds totaling \$3,098,100 and \$8,170,600 which resulted in gross gains realized of \$98,100 and \$181,363 , respectively.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 3. Securities, Continued

The amortized cost and estimated fair value of securities at June 30, 2017, by contractual maturity, are shown below (in thousands). Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Due in one year or less	\$ 4,179	\$ 4,182
Due from one year to five years	11,165	10,961
Due from five years to ten years	8,789	8,703
Due after ten years	3,445	3,470
	<u>27,578</u>	<u>27,316</u>
Mortgage-backed securities	105,585	105,446
	<u>\$ 133,163</u>	<u>\$ 132,762</u>

The following tables present the gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities available-for-sale have been in a continuous unrealized loss position, as of June 30, 2017 and December 31, 2016 (in thousands):

	As of June 30, 2017					
	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. Government- sponsored enterprises (GSEs)	13,572	(278)	—	—	13,572	(278)
Municipal securities	2,897	(41)	253	(1)	3,150	(42)
Other debt securities	948	(24)	—	—	948	(24)
Mortgage-backed securities	33,086	(139)	17,662	(347)	50,748	(486)
	<u>50,503</u>	<u>(482)</u>	<u>17,915</u>	<u>(348)</u>	<u>68,418</u>	<u>(830)</u>

	As of December 31, 2016					
	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. Government- sponsored enterprises (GSEs)	\$ 14,702	\$ (564)	\$ —	\$ —	\$ 14,702	\$ (564)
Municipal securities	6,368	(179)	—	—	6,368	(179)
Mortgage-backed securities	67,063	(690)	8,948	(400)	76,011	(1,090)
	<u>\$ 88,133</u>	<u>\$ (1,433)</u>	<u>\$ 8,948</u>	<u>\$ (400)</u>	<u>\$ 97,081</u>	<u>\$ (1,833)</u>

At June 30, 2017, the categories of temporarily impaired securities, and management's evaluation of those securities, are as follows:

U.S. Government-sponsored enterprises : At June 30, 2017, 4 (or four) investment in U.S. GSE securities had unrealized losses. These unrealized losses related principally to changes in market interest rates. The contractual terms of the investments do not permit the issuer to settle the securities at a price less than the amortized cost bases of the investments. Because the Bank does not intend to sell the investments and it is more likely than not that the Bank will not be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Bank does not consider these investments to be other-than temporarily impaired at June 30, 2017.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 3. Securities, Continued

Municipal securities : At June 30, 2017 , 8 (or eight) investments in obligations of municipal securities had unrealized losses. The Bank believes the unrealized losses on those investments were caused by the interest rate environment and do not relate to the underlying credit quality of the issuers. Because the Bank does not intend to sell the investments and it is not more likely than not that the Bank will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Bank does not consider these investments to be other-than temporarily impaired at June 30, 2017 .

Other debt securities : At June 30, 2017 , 1 (or one) investment in other debt securities had unrealized losses. The Bank believes the unrealized loss on this investment was caused by the interest rate environment and does not relate to the underlying credit quality of the issuer. Because the Bank does not intend to sell the investment and it is not more likely than not that the Bank will be required to sell the investment before recovery of its amortized cost bases, which may be maturity, the Bank does not consider this investment to be other-than temporarily impaired at June 30, 2017 .

Mortgage-backed securities : At June 30, 2017 , 43 (or forty three) investments in residential mortgage-backed securities had unrealized losses. This impairment is believed to be caused by the current interest rate environment. The contractual cash flows of those investments are guaranteed by an agency of the U.S. Government. Because the decline in market value is attributable to the current interest rate environment and not credit quality, and because the Bank does not intend to sell the investments and it is not more likely than not that the Bank will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Bank does not deem these investments to be other-than-temporarily impaired at June 30, 2017 .

Note 4. Loans and Allowance for Loan Losses

Portfolio Segmentation:

At June 30, 2017 and December 31, 2016 , loans are summarized as follows (in thousands):

	June 30, 2017			December 31, 2016		
	PCI Loans	All Other Loans	Total	PCI Loans	All Other Loans	Total
Commercial real estate	\$ 14,417	\$ 430,772	\$ 445,189	\$ 14,943	\$ 400,265	\$ 415,208
Consumer real estate	8,071	198,596	206,667	9,004	178,798	187,802
Construction and land development	1,474	99,682	101,156	1,678	116,191	117,869
Commercial and industrial	1,249	103,984	105,233	1,568	83,454	85,022
Consumer and other	—	7,176	7,176	—	7,475	7,475
Total loans	25,211	840,210	865,421	27,193	786,183	813,376
Less: Allowance for loan losses	—	(5,498)	(5,498)	—	(5,105)	(5,105)
Loans, net	\$ 25,211	\$ 834,712	\$ 859,923	\$ 27,193	\$ 781,078	\$ 808,271

For purposes of the disclosures required pursuant to the adoption of ASC 310, the loan portfolio was disaggregated into segments. A portfolio segment is defined as the level at which an entity develops and documents a systematic method for determining its allowance for credit losses. There are five loan portfolio segments that include commercial real estate, consumer real estate, construction and land development, commercial and industrial, and consumer and other.

The following describe risk characteristics relevant to each of the portfolio segments:

Commercial Real Estate: Commercial real estate loans include owner-occupied commercial real estate loans and loans secured by income-producing properties. Owner-occupied commercial real estate loans to operating businesses are long-term financing of land and buildings. These loans are repaid by cash flow generated from the business operation. Real estate loans for income-producing properties such as apartment buildings, office and industrial buildings, and retail shopping centers are repaid from rent income derived from the properties. Loans within this portfolio segment are particularly sensitive to the valuation of real estate.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 4. Loans and Allowance for Loan Losses, Continued

Portfolio Segmentation (continued):

Consumer Real Estate: Consumer real estate loans include real estate loans secured by first liens, second liens, or open end real estate loans, such as home equity lines. These are repaid by various means such as a borrower's income, sale of the property, or rental income derived from the property. One to four family first mortgage loans are repaid by various means such as a borrower's income, sale of the property, or rental income derived from the property. Loans within this portfolio segment are particularly sensitive to the valuation of real estate.

Construction and Land Development: Loans for real estate construction and development are repaid through cash flow related to the operations, sale or refinance of the underlying property. This portfolio segment includes extensions of credit to real estate developers or investors where repayment is dependent on the sale of the real estate or income generated from the real estate collateral. Loans within this portfolio segment are particularly sensitive to the valuation of real estate.

Commercial and Industrial: The commercial and industrial loan portfolio segment includes commercial, financial, and agricultural loans. These loans include those loans to commercial customers for use in normal business operations to finance working capital needs, equipment purchases, or expansion projects. Loans are repaid by business cash flows. Collection risk in this portfolio is driven by the creditworthiness of the underlying borrower, particularly cash flows from the customers' business operations.

Consumer and Other: The consumer loan portfolio segment includes direct consumer installment loans, overdrafts and other revolving credit loans, and educational loans. Loans in this portfolio are sensitive to unemployment and other key consumer economic measures.

Credit Risk Management:

The Company employs a credit risk management process with defined policies, accountability and routine reporting to manage credit risk in the loan portfolio segments. Credit risk management is guided by credit policies that provide for a consistent and prudent approach to underwriting and approvals of credits. Within the Credit Policy, procedures exist that elevate the approval requirements as credits become larger and more complex. All loans are individually underwritten, risk-rated, approved, and monitored.

Responsibility and accountability for adherence to underwriting policies and accurate risk ratings lies in each portfolio segment. For the consumer real estate and consumer and other portfolio segments, the risk management process focuses on managing customers who become delinquent in their payments. For the other portfolio segments, the risk management process focuses on underwriting new business and, on an ongoing basis, monitoring the credit of the portfolios, including a third party review of the largest credits on an annual basis or more frequently as needed. To ensure problem credits are identified on a timely basis, several specific portfolio reviews occur periodically to assess the larger adversely rated credits for proper risk rating and accrual status.

Credit quality and trends in the loan portfolio segments are measured and monitored regularly. Detailed reports, by product, collateral, accrual status, etc., are reviewed by the Senior Credit Officer and the Directors Loan Committee.

The allowance for loan losses is a valuation reserve allowance established through provisions for loan losses charged against income. The allowance for loan losses, which is evaluated quarterly, is maintained at a level that management deems sufficient to absorb probable losses inherent in the loan portfolio. Loans deemed to be uncollectible are charged against the allowance for loan losses, while recoveries of previously charged-off amounts are credited to the allowance for loan losses. The allowance for loan losses is comprised of specific valuation allowances for loans evaluated individually for impairment and general allocations for pools of homogeneous loans with similar risk characteristics and trends.

The allowance for loan losses related to specific loans is based on management's estimate of potential losses on impaired loans as determined by (1) the present value of expected future cash flows; (2) the fair value of collateral if the loan is determined to be collateral dependent or (3) the loan's observable market price. The Company's homogeneous loan pools include commercial real estate loans, consumer real estate loans, construction and land development loans, commercial and industrial loans, and consumer and other loans. The general allocations to these loan pools are based on the historical loss rates for specific loan types and the internal risk grade, if applicable, adjusted for both internal and external qualitative risk factors.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 4. Loans and Allowance for Loan Losses, Continued

Credit Risk Management (continued):

The qualitative factors considered by management include, among other factors, (1) changes in local and national economic conditions; (2) changes in asset quality; (3) changes in loan portfolio volume; (4) the composition and concentrations of credit; (5) the impact of competition on loan structuring and pricing; (6) the impact of interest rate changes on portfolio risk and (7) effectiveness of the Company's loan policies, procedures and internal controls. The total allowance established for each homogeneous loan pool represents the product of the historical loss ratio adjusted for qualitative factors and the total dollar amount of the loans in the pool.

The composition of loans by loan classification for impaired and performing loan status at June 30, 2017 and December 31, 2016, is summarized in the tables below (amounts in thousands):

	June 30, 2017					
	Commercial Real Estate	Consumer Real Estate	Construction and Land Development	Commercial and Industrial	Consumer and Other	Total
Performing loans	\$ 430,653	\$ 197,755	\$ 99,135	\$ 103,940	\$ 7,176	\$ 838,659
Impaired loans	119	841	547	44	—	1,551
	430,772	198,596	99,682	103,984	7,176	840,210
PCI loans	14,417	8,071	1,474	1,249	—	25,211
Total	\$ 445,189	\$ 206,667	\$ 101,156	\$ 105,233	\$ 7,176	\$ 865,421

	December 31, 2016					
	Commercial Real Estate	Consumer Real Estate	Construction and Land Development	Commercial and Industrial	Consumer and Other	Total
Performing loans	\$ 400,146	\$ 177,977	\$ 115,326	\$ 83,244	\$ 7,475	\$ 784,168
Impaired loans	119	821	865	210	—	2,015
	400,265	178,798	116,191	83,454	7,475	786,183
PCI loans	14,943	9,004	1,678	1,568	—	27,193
Total loans	\$ 415,208	\$ 187,802	\$ 117,869	\$ 85,022	\$ 7,475	\$ 813,376

The following tables show the allowance for loan losses allocation by loan classification for impaired, PCI, and performing loans as of June 30, 2017 and December 31, 2016 (amounts in thousands):

	June 30, 2017					
	Commercial Real Estate	Consumer Real Estate	Construction and Land Development	Commercial and Industrial	Consumer and Other	Total
Performing loans	\$ 2,489	\$ 1,556	\$ 609	\$ 644	\$ 103	\$ 5,401
Impaired loans	—	97	—	—	—	97
Total	\$ 2,489	\$ 1,653	\$ 609	\$ 644	\$ 103	\$ 5,498

	December 31, 2016					
	Commercial Real Estate	Consumer Real Estate	Construction and Land Development	Commercial and Industrial	Consumer and Other	Total
Performing loans	\$ 2,369	\$ 1,382	\$ 717	\$ 516	\$ 117	\$ 5,101
Impaired loans	—	—	—	4	—	4
Total	\$ 2,369	\$ 1,382	\$ 717	\$ 520	\$ 117	\$ 5,105

There was no allowance for PCI loans at June 30, 2017 or December 31, 2016.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 4. Loans and Allowance for Loan Losses, Continued

Credit Risk Management (continued):

The following tables detail the changes in the allowance for loan losses for the six month period ending June 30, 2017 and year ending December 31, 2016 , by loan classification (amounts in thousands):

	June 30, 2017					
	Commercial Real Estate	Consumer Real Estate	Construction and Land Development	Commercial and Industrial	Consumer and Other	Total
Beginning balance	\$ 2,369	\$ 1,382	\$ 717	\$ 520	\$ 117	\$ 5,105
Loans charged off	—	(6)	—	—	(40)	(46)
Recoveries of loans charged off	6	47	8	32	36	129
Provision (reallocation) charged to operating expense	114	230	(116)	92	(10)	310
Ending balance	<u>\$ 2,489</u>	<u>\$ 1,653</u>	<u>\$ 609</u>	<u>\$ 644</u>	<u>\$ 103</u>	<u>\$ 5,498</u>

	December 31, 2016					
	Commercial Real Estate	Consumer Real Estate	Construction and Land Development	Commercial and Industrial	Consumer and Other	Total
Beginning balance	\$ 1,906	\$ 1,015	\$ 627	\$ 777	\$ 29	\$ 4,354
Loans charged off	—	(102)	(14)	(35)	(155)	(306)
Recoveries of charge-offs	45	76	22	58	68	269
Provision (reallocation) charged to operating expense	418	393	82	(280)	175	788
Ending balance	<u>\$ 2,369</u>	<u>\$ 1,382</u>	<u>\$ 717</u>	<u>\$ 520</u>	<u>\$ 117</u>	<u>\$ 5,105</u>

A description of the general characteristics of the risk grades used by the Company is as follows:

Pass: Loans in this risk category involve borrowers of acceptable-to-strong credit quality and risk who have the apparent ability to satisfy their loan obligations. Loans in this risk grade would possess sufficient mitigating factors, such as adequate collateral or strong guarantors possessing the capacity to repay the debt if required, for any weakness that may exist.

Special Mention: Loans in this risk grade are the equivalent of the regulatory definition of "Other Assets Especially Mentioned" classification. Loans in this category possess some credit deficiency or potential weakness, which requires a high level of management attention. Potential weaknesses include declining trends in operating earnings and cash flows and /or reliance on the secondary source of repayment. If left uncorrected, these potential weaknesses may result in noticeable deterioration of the repayment prospects for the asset or in the Company's credit position.

Substandard: Loans in this risk grade are inadequately protected by the borrower's current financial condition and payment capability or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the orderly repayment of debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful: Loans in this risk grade have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or orderly repayment in full, on the basis of current existing facts, conditions and values, highly questionable and improbable. Possibility of loss is extremely high, but because of certain important and reasonably specific factors that may work to the advantage and strengthening of the exposure, its classification as an estimated loss is deferred until its more exact status may be determined.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 4. Loans and Allowance for Loan Losses, Continued

Credit Risk Management (continued):

Uncollectible: Loans in this risk grade are considered to be non-collectible and of such little value that their continuance as bankable assets is not warranted. This does not mean 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. Charge-offs against the allowance for loan losses are taken in the period in which the loan becomes uncollectible. Consequently, the Company typically does not maintain a recorded investment in loans within this category.

The following tables outline the amount of each loan classification and the amount categorized into each risk rating as of June 30, 2017 and December 31, 2016 (amounts in thousands):

Non PCI Loans

	June 30, 2017					
	Commercial Real Estate	Consumer Real Estate	Construction and Land Development	Commercial and Industrial	Consumer and Other	Total
Pass	\$ 430,490	\$ 197,314	\$ 99,048	\$ 103,031	\$ 6,959	\$ 836,842
Watch	159	509	87	870	—	1,625
Special mention	—	16	—	—	217	233
Substandard	123	757	547	83	—	1,510
Doubtful	—	—	—	—	—	—
Total	<u>\$ 430,772</u>	<u>\$ 198,596</u>	<u>\$ 99,682</u>	<u>\$ 103,984</u>	<u>\$ 7,176</u>	<u>\$ 840,210</u>

PCI Loans

	June 30, 2017					
	Commercial Real Estate	Consumer Real Estate	Construction and Land Development	Commercial and Industrial	Consumer and Other	Total
Pass	\$ 11,548	\$ 6,116	\$ 816	\$ 970	\$ —	\$ 19,450
Watch	865	1,221	646	16	—	2,748
Special mention	—	—	—	238	—	238
Substandard	2,004	734	12	—	—	2,750
Doubtful	—	—	—	25	—	25
Total	<u>\$ 14,417</u>	<u>\$ 8,071</u>	<u>\$ 1,474</u>	<u>\$ 1,249</u>	<u>\$ —</u>	<u>\$ 25,211</u>
Total loans	<u>\$ 445,189</u>	<u>\$ 206,667</u>	<u>\$ 101,156</u>	<u>\$ 105,233</u>	<u>\$ 7,176</u>	<u>\$ 865,421</u>

Non PCI Loans

	December 31, 2016					
	Commercial Real Estate	Consumer Real Estate	Construction and Land Development	Commercial and Industrial	Consumer and Other	Total
Pass	\$ 399,505	\$ 177,466	\$ 115,237	\$ 82,992	\$ 7,238	\$ 782,438
Watch	640	550	89	252	—	1,531
Special mention	—	104	—	—	237	341
Substandard	120	678	865	210	—	1,873
Doubtful	—	—	—	—	—	—
Total	<u>\$ 400,265</u>	<u>\$ 178,798</u>	<u>\$ 116,191</u>	<u>\$ 83,454</u>	<u>\$ 7,475</u>	<u>\$ 786,183</u>

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 4. Loans and Allowance for Loan Losses, Continued

Credit Risk Management (continued):

PCI Loans

	December 31, 2016					
	Commercial Real Estate	Consumer Real Estate	Construction and Land Development	Commercial and Industrial	Consumer and Other	Total
Pass	\$ 11,836	\$ 6,811	\$ 1,019	\$ 1,507	\$ —	\$ 21,173
Watch	1,045	1,577	645	22	—	3,289
Special mention	—	—	—	12	—	12
Substandard	2,062	616	14	—	—	2,692
Doubtful	—	—	—	27	—	27
Total	\$ 14,943	\$ 9,004	\$ 1,678	\$ 1,568	\$ —	\$ 27,193
Total loans	\$ 415,208	\$ 187,802	\$ 117,869	\$ 85,022	\$ 7,475	\$ 813,376

Past Due Loans:

A loan is considered past due if any required principal and interest payments have not been received as of the date such payments were required to be made under the terms of the loan agreement. Generally, management places a loan on nonaccrual when there is a clear indicator that the borrower's cash flow may not be sufficient to meet payments as they become due, which is generally when a loan is 90 days past due.

The following tables present the aging of the recorded investment in loans as of June 30, 2017 and December 31, 2016 (amounts in thousands):

	June 30, 2017						
	30-89 Days Past Due and Accruing	Past Due 90 Days or More and Accruing	Nonaccrual	Total Past Due and NonAccrual	PCI Loans	Current Loans	Total Loans
Commercial real estate	\$ 240	\$ —	\$ 123	\$ 363	\$ 14,417	\$ 430,409	\$ 445,189
Consumer real estate	1,193	—	414	1,607	8,071	196,989	206,667
Construction and land development	—	—	547	547	1,474	99,135	101,156
Commercial and industrial	9	19	—	28	1,249	103,956	105,233
Consumer and other	40	11	—	51	—	7,125	7,176
Total	\$ 1,482	\$ 30	\$ 1,084	\$ 2,596	\$ 25,211	\$ 837,614	\$ 865,421

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 4. Loans and Allowance for Loan Losses, Continued

Past Due Loans (continued):

	December 31, 2016						
	30-89 Days Past Due and Accruing	Past Due 90 Days or More and Accruing	Nonaccrual	Total Past Due and NonAccrual	PCI Loans	Current Loans	Total Loans
Commercial real estate	\$ 395	\$ —	\$ —	\$ 395	\$ 14,943	\$ 399,870	\$ 415,208
Consumer real estate	695	699	386	1,780	9,004	177,018	187,802
Construction and land development	690	—	865	1,555	1,678	114,636	117,869
Commercial and industrial	257	—	164	421	1,568	83,033	85,022
Consumer and other	17	—	—	17	—	7,458	7,475
Total	\$ 2,054	\$ 699	\$ 1,415	\$ 4,168	\$ 27,193	\$ 782,015	\$ 813,376

Impaired Loans:

The following is an analysis of the impaired loan portfolio, excluding PCI loans, detailing the related allowance recorded as of June 30, 2017 and December 31, 2016 (amounts in thousands):

	At June 30, 2017			For the six months ended June 30, 2017	
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
Impaired loans without a valuation allowance:					
Commercial real estate	\$ 119	\$ 124	\$ —	\$ 159	\$ 6
Consumer real estate	93	93	—	427	5
Construction and land development	547	547	—	682	—
Commercial and industrial	44	44	—	45	1
Consumer and other	—	—	—	—	—
	803	808	—	1,313	12
Impaired loans with a valuation allowance:					
Commercial real estate	—	—	—	—	—
Consumer real estate	748	772	97	458	14
Construction and land development	—	—	—	—	—
Commercial and industrial	—	—	—	109	—
Consumer and other	—	—	—	—	—
	748	772	97	567	14
Total impaired loans	\$ 1,551	\$ 1,580	\$ 97	\$ 1,880	\$ 26

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 4. Loans and Allowance for Loan Losses, Continued

Impaired Loans (continued):

	At December 31, 2016			For the year ended December 31, 2016	
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
Impaired loans without a valuation allowance:					
Commercial real estate	\$ 119	\$ 119	\$ —	\$ 1,311	\$ 73
Consumer real estate	821	849	—	2,334	100
Construction and land development	865	865	—	967	3
Commercial and industrial	46	46	—	47	4
Consumer and other	—	—	—	—	—
	<u>1,851</u>	<u>1,879</u>	<u>—</u>	<u>4,659</u>	<u>180</u>
Impaired loans with a valuation allowance:					
Commercial real estate	—	—	—	—	—
Consumer real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Commercial and industrial	164	243	4	306	70
Consumer and other	—	—	—	—	—
	<u>164</u>	<u>243</u>	<u>4</u>	<u>306</u>	<u>70</u>
Total impaired loans	<u>\$ 2,015</u>	<u>\$ 2,122</u>	<u>\$ 4</u>	<u>\$ 4,965</u>	<u>\$ 250</u>

Troubled Debt Restructurings:

At June 30, 2017 and December 31, 2016, impaired loans included loans that were classified as Troubled Debt Restructurings ("TDRs"). The restructuring of a loan is considered a TDR if both (i) the borrower is experiencing financial difficulties and (ii) the creditor has granted a concession.

In assessing whether or not a borrower is experiencing financial difficulties, the Company considers information currently available regarding the financial condition of the borrower. This information includes, but is not limited to, whether (i) the debtor is currently in payment default on any of its debt; (ii) a payment default is probable in the foreseeable future without the modification; (iii) the debtor has declared or is in the process of declaring bankruptcy; and (iv) the debtor's projected cash flow is sufficient to satisfy contractual payments due under the original terms of the loan without a modification.

The Company considers all aspects of the modification to loan terms to determine whether or not a concession has been granted to the borrower. Key factors considered by the Company include the debtor's ability to access funds at a market rate for debt with similar risk characteristics, the significance of the modification relative to unpaid principal balance or collateral value of the debt, and the significance of a delay in the timing of payments relative to the original contractual terms of the loan.

The most common concessions granted by the Company generally include one or more modifications to the terms of the debt, such as (i) a reduction in the interest rate for the remaining life of the debt; (ii) an extension of the maturity date at an interest rate lower than the current market rate for new debt with similar risk; (iii) a temporary period of interest-only payments; and (iv) a reduction in the contractual payment amount for either a short period or remaining term of the loan. As of June 30, 2017 and December 31, 2016, management had approximately, \$44,000 and \$608,000, respectively, in loans that met the criteria for restructured, which included approximately \$0 and \$442,000, respectively, of loans on nonaccrual. A loan is placed back on accrual status when both principal and interest are current and it is probable that management will be able to collect all amounts due (both principal and interest) according to the terms of the loan agreement.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 4. Loans and Allowance for Loan Losses, Continued

Troubled Debt Restructurings (continued):

There were no loans that were modified as troubled debt restructurings during the six month period ended June 30, 2017.

The following table presents a summary of loans that were modified as troubled debt restructurings during the twelve month period ended December 31, 2016 (amounts in thousands):

December 31, 2016	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Construction and land development	1	\$ 278	\$ 278
Commercial and industrial	1	\$ 164	\$ 164

There were no loans that were modified as troubled debt restructurings during the past twelve months and for which there was a subsequent payment default.

Purchased Credit Impaired Loans:

The Company has acquired loans which there was, at acquisition, evidence of deterioration of credit quality since origination and it was probable, at acquisition, that all contractually required payments would not be collected. The carrying amount of those loans as of is as follows (amounts in thousands):

	June 30, 2017	December 31, 2016
Commercial real estate	\$ 17,713	\$ 18,473
Consumer real estate	11,030	12,111
Construction and land development	1,778	2,553
Commercial and industrial	1,978	2,482
Consumer and other	—	—
Total loans	32,499	35,619
Less remaining purchase discount	(7,288)	(8,426)
Total loans, net of purchase discount	25,211	27,193
Less: Allowance for loan losses	—	—
Carrying amount, net of allowance	\$ 25,211	\$ 27,193

Activity related to the accretable portion of the purchase discount on loans acquired with deteriorated credit quality is as follows for the three and six months period ended June 30, 2017 and 2016 :

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 4. Loans and Allowance for Loan Losses, Continued

Purchased Credit Impaired Loans (continued):

	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016	Six Months Ended June 30, 2017	Six Months Ended June 30, 2016
Accretable yield, beginning of period	\$ 8,482	\$ 9,606	\$ 8,950	\$ 10,216
Additions	—	—	—	—
Accretion income	(973)	(586)	(1,670)	(1,215)
Reclassification to accretable	366	1,378	610	1,337
Other changes, net	600	(189)	585	(129)
Accretable yield	<u>\$ 8,475</u>	<u>\$ 10,209</u>	<u>\$ 8,475</u>	<u>\$ 10,209</u>

Note 5. Employee Benefit Plans

401(k) Plan:

The Company provides a deferred salary reduction plan (“Plan”) under Section 401(k) of the Internal Revenue Code covering substantially all employees. After one year of service the Company matches 100 percent of employee contributions up to 3 percent of compensation and 50 percent of employee contributions on the next 2 percent of compensation. The Company's contribution to the Plan for the three month period ending June 30, 2017 and 2016 respectively was \$106,130 and \$99,568 and for the six month period ending June 30, 2017 and 2016 respectively was \$ 208,846 and \$ 190,423

Stock Option Plans:

The Company has one currently active equity incentive plan administered by the Board of Directors, and four plans or programs, pursuant to which the Company has outstanding prior grants. These plans are described below:

Legacy Cornerstone Bancshares, Inc. 2002 Long Term Incentive Plan – The plan provided Cornerstone Bancshares, Inc. officers and employees incentive stock options or non-qualified stock options to purchase shares of common stock. The exercise price for incentive stock options was not less than 100 percent of the fair market value of the common stock on the date of the grant. The exercise price of the non-qualified stock options was equal to or more or less than the fair market value of the common stock on the date of the grant. This plan expired in 2012.

Legacy Cornerstone Non-Qualified Plan Options — During 2013 and 2014, Cornerstone issued non-qualified options to employees and directors. The options were originally documented in 2013 as being issued out of the Cornerstone Bancshares, Inc. 2002 Long Term Incentive Plan but that plan expired in 2012. The non-qualified options are governed by the grant document issued to the holders which incorporate the terms of the plan by reference.

Legacy SmartBank Stock Option Plan – This plan was assumed by the Company on August 31, 2015. The plan provides for incentive stock options and nonqualified stock options. The maximum number of common shares that could be sold or optioned under the plan is 525,000 shares. Under the plan, the exercise price of each option could not be less than 100 percent of the fair market value of the common stock on the date of grant.

Legacy SmartFinancial, Inc. 2010 Incentive Plan - This plan was assumed by the Company on August 31, 2015. This plan provides for incentive stock options, nonqualified stock options, stock appreciation rights, restricted stock, performance awards, dividend equivalents and stock or other stock-based awards. The maximum number of common shares that could be sold or optioned under the plan is 525,000 shares. Under the plan, the exercise price of each option could not be less than 100 percent of the fair market value of the common stock on the date of grant.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 5. Employee Benefit Plans, Continued

Stock Option Plans (Continued):

2015 Stock Incentive Plan – This plan provides for incentive stock options, nonqualified stock options, and restricted stock. The maximum number of shares of common stock that can be sold or optioned under the plan is 2,000,000 shares. The term of each option shall be no more than ten years from the date of grant. In the case of an incentive stock option granted to a participant who, at the time the option is granted, owns stock representing more than ten percent of the voting power of all classes of stock of the Company or any parent or subsidiary thereof, the term of the option shall be five years from the date of grant or such shorter term as may be provided in the award agreement.

The per share exercise price for the shares to be issued upon exercise of an option shall be such price as is determined by the plan administrator, subject to the following: In the case of an incentive stock option: (1) granted to an employee who, at the time of grant of such option, owns stock representing more than ten percent of the voting power of all classes of stock of the company or any parent or subsidiary thereof, the exercise price shall be no less than one hundred and ten percent of the fair market value per share on the date of grant; or (2) granted to any other employee, the per share exercise price shall be no less than one hundred percent of the fair market value per share on the date of grant. In the case of a nonstatutory stock option, the per share exercise price shall be no less than one hundred percent of the fair market value per share on the date of grant, unless otherwise determined by the Administrator.

The incentive stock options vest 30% on the second anniversary of the grant date, 30% on the third anniversary of the grant date and 40% on the fourth anniversary of the grant date. Director non-qualified stock options vest 50% on the first anniversary of the grant date and 50% on the second anniversary of the grant date.

A summary of the status of these stock option plans is presented in the following table:

	Number	Weighted Average Exercisable Price
Outstanding at December 31, 2016	717,524	\$ 10.57
Exercised	(481,717)	9.60
Forfeited	(22,721)	19.72
Outstanding at June 30, 2017	213,086	\$ 11.77

	Number	Weighted Average Exercisable Price
Outstanding at December 31, 2015	817,414	\$ 10.62
Exercised	(89,556)	8.98
Forfeited	(10,334)	28.49
Outstanding at December 31, 2016	717,524	\$ 10.57

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 5. Employee Benefit Plans, Continued

Stock Option Plans (continued):

Information pertaining to options outstanding at June 30, 2017, is as follows:

Exercise Prices	Options Outstanding			Options Exercisable		
	Number Outstanding	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price	
6.60	39,000	4.7 years	6.60	39,000	6.60	
6.80	17,625	3.7 years	6.80	17,625	6.80	
9.48	27,375	5.7 years	9.48	27,375	9.48	
9.60	35,625	6.7 years	9.60	35,625	9.60	
10.48	20,245	0.2 years	10.48	20,245	10.48	
11.67	3,250	3.6 years	11.67	3,250	11.67	
14.40	13,305	1.7 years	14.40	13,305	14.40	
15.05	42,745	8.3 years	15.05	4,104	15.05	
31.96	13,916	0.7 years	31.96	13,916	31.96	
Outstanding, end of period	<u>213,086</u>	4.9 years	11.77	<u>174,445</u>	11.05	

The Company recognized stock-based compensation expense of \$23,718 and \$33,000 for the three months ended June 30, 2017 and June 30, 2016, respectively and \$ 50,530 and \$ 66,635 for the six months ended June 30, 2017 and June 30, 2016, respectively. For the six months period ended June 30, 2017, direct stock grant expense issued to local advisory board members of \$31,791 was included in professional services. There was no direct grant stock grant expense for the six months period ended June 30, 2016. The total fair value of shares underlying the options which vested during the six months period ended June 30, 2017 and June 30, 2016 was \$0 and \$16,800, respectively. There were no income tax benefits recognized for the exercise of options for the periods ended June 30, 2017 and June 30, 2016, respectively.

The intrinsic value of options exercised during the period ended June 30, 2017 was \$5,135,088. The aggregate intrinsic value of total options outstanding and exercisable options at June 30, 2017 was \$2,692,426 and \$2,351,226, respectively. Cash received from options exercised under all share-based payment arrangements for the period ended June 30, 2017 was \$4,625,012.

Information related to non-vested options for the period ended June 30, 2017, is as follows:

	Number	Weighted Average Grant-Date Fair Value
Nonvested at December 31, 2016	47,970	\$ 12.31
Granted	—	—
Vested	—	—
Forfeited/expired	(9,329)	12.31
Nonvested at June 30, 2017	<u>38,641</u>	<u>\$ 12.31</u>

As of June 30, 2017, there was approximately \$316,824 of total unrecognized compensation cost related to nonvested stock-based compensation arrangements granted under the Plans. The cost is expected to be recognized over a weighted-average period of 1.3 years. There were no stock options granted during the six months period ended June 30, 2017.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 6. Commitments and Contingent Liabilities

Off Balance Sheet Arrangements In the normal course of business, the Bank has entered into off-balance sheet financial instruments which include commitments to extend credit (i.e., including unfunded lines of credit) and standby letters of credit. Commitments to extend credit are usually the result of lines of credit granted to existing borrowers under agreements that the total outstanding indebtedness will not exceed a specific amount during the term of the indebtedness. Typical borrowers are commercial concerns that use lines of credit to supplement their treasury management functions; thus their total outstanding indebtedness may fluctuate during any time period based on the seasonality of their business and the resultant timing of their cash flows. Other typical lines of credit are related to home equity loans granted to consumers. Commitments to extend credit generally have fixed expiration dates or other termination clauses and may require payment of a fee.

Standby letters of credit are generally issued on behalf of an applicant (our client) to a specifically named beneficiary and are the result of a particular business arrangement that exists between the applicant and the beneficiary. Standby letters of credit have fixed expiration dates and are usually for terms of two years or less unless terminated beforehand due to criteria specified in the standby letter of credit. A typical arrangement involves the applicant routinely being indebted to the beneficiary for such items as inventory purchases, insurance, utilities, lease guarantees or other third party commercial transactions. The standby letter of credit would permit the beneficiary to obtain payment from the Bank under certain prescribed circumstances. Subsequently, the Bank would seek reimbursement from the applicant pursuant to the terms of the standby letter of credit.

The Bank follows the same credit policies and underwriting practices when making these commitments as it does for on-balance sheet instruments. Each client's creditworthiness is evaluated on a case-by-case basis, and the amount of collateral obtained, if any, is based on management's credit evaluation of the customer. Collateral held varies but may include cash, real estate and improvements, marketable securities, accounts receivable, inventory, equipment and personal property.

The contractual amounts of these commitments are not reflected in the consolidated financial statements and would only be reflected if drawn upon. Since many of the commitments are expected to expire without being drawn upon, the contractual amounts do not necessarily represent future cash requirements. However, should the commitments be drawn upon and should customers default on their resulting obligation to the Bank the maximum exposure to credit loss, without consideration of collateral, is represented by the contractual amount of those instruments.

A summary of the Bank's total contractual amount for all off-balance sheet commitments at June 30, 2017 is as follows:

Commitments to extend credit	\$	154.1 million
Standby letters of credit	\$	2.8 million

Various legal claims also arise from time to time in the normal course of business. In the opinion of management, the resolution of claims outstanding at June 30, 2017 will not have a material effect on SmartFinancial's consolidated financial statements.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 7. Fair Value Disclosures

Determination of Fair Value:

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. In accordance with the “Fair Value Measurements and Disclosures” ASC Topic 820, the fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

ASC Topic 820 provides a consistent definition of fair value, which focuses on exit price in an orderly transaction between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions.

Fair Value Hierarchy:

In accordance with this guidance, the Company groups its financial assets and financial liabilities generally measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

Level 1 - Valuation is based on quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 1 assets and liabilities generally include debt and equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 - Valuation is based on inputs other than quoted prices included within Level I that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

Level 3 - Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which determination of fair value requires significant management judgment or estimation.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

The following methods and assumptions were used by the Company in estimating fair value disclosures for financial instruments:

Cash and Cash Equivalents: For cash and due from banks, interest-bearing deposits, and federal funds sold, the carrying amount is a reasonable estimate of fair value based on the short-term nature of the assets and are considered Level 1 inputs.

Securities Available for Sale: Where quoted prices are available in an active market, management classifies the securities within Level 1 of the valuation hierarchy. If quoted market prices are not available, management estimates fair values using pricing models and discounted cash flows that consider standard input factors such as observable market data, benchmark yields, interest rate volatilities, broker/dealer quotes, and credit spreads. Examples of such instruments, which would generally be classified within Level 2 of the valuation hierarchy, including GSE obligations, corporate bonds, and other securities. Mortgage-backed securities are included in Level 2 if observable inputs are available. In certain cases where there is limited activity or less transparency around inputs to the valuation, management classifies those securities in Level 3.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 7. Fair Value Disclosures, Continued

Fair Value Hierarchy (continued):

Restricted Investments: It is not practicable to determine the fair value of restricted investments due the restrictions placed on its transferability.

Loans: For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair value for fixed rate loans are estimated using discounted cash flow analyses, using market interest rates for comparable loans. Fair values for nonperforming loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable. These methods are considered Level 3 inputs.

Deposits: The fair values disclosed for demand deposits (for example, interest and noninterest checking, savings, and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts) and are considered Level 1 inputs. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates on comparable instruments to a schedule of aggregated expected monthly maturities on time deposits, and are considered Level 2 inputs.

Securities Sold Under Agreement to Repurchase: The carrying value of these liabilities approximates their fair value, and are considered Level 1 inputs.

Federal Home Loan Bank Advances and Other Borrowings: The fair value of the FHLB fixed rate borrowings are estimated using discounted cash flows, based on the current incremental borrowing rates for similar types of borrowing arrangements, and are considered Level 2 inputs.

Commitments to Extend Credit and Standby Letters of Credit: Because commitments to extend credit and standby letters of credit are made using variable rates and have short maturities, the carrying value and the fair value are immaterial for disclosure.

Measurements of Fair Value:

Assets and liabilities recorded at fair value on a recurring basis are as follows (in thousands):

	Balance as of June 30, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Debt securities available-for-sale:				
U.S. Government-sponsored enterprises (GSEs)	\$ 17,971	\$ —	\$ 17,971	\$ —
Mortgage-backed securities	105,446	—	105,446	—
Other debt securities	948	—	948	—
Municipal securities	8,397	—	8,397	—
Total securities available-for-sale	\$ 132,762	\$ —	\$ 132,762	\$ —

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 7. Fair Value Disclosures, Continued

Measurements of Fair Value (continued):

	Balance as of December 31, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Debt securities available-for-sale:				
U.S. Government-sponsored enterprises (GSEs)	\$ 17,723	\$ —	\$ 17,723	\$ —
Mortgage-backed securities:	103,680	—	103,680	—
Municipal securities	8,019	—	8,019	—
Total securities available-for-sale	\$ 129,422	\$ —	\$ 129,422	\$ —

The Company has no assets or liabilities whose fair values are measured on a recurring basis using Level 3 inputs. Additionally, there were no transfers between Level 1 and Level 2 in the fair value hierarchy.

Assets Measured at Fair Value on a Nonrecurring Basis:

Under certain circumstances management makes adjustments to fair value for assets and liabilities although they are not measured at fair value on an ongoing basis. The following tables present the financial instruments carried on the consolidated balance sheets by caption and by level in the fair value hierarchy, for which a nonrecurring change in fair value has been recorded (in thousands):

	Balance as of June 30, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Impaired loans	\$ 651	\$ —	\$ —	\$ 651
Foreclosed assets	2,369	—	—	2,369

	Balance as of December 31, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Impaired loans	\$ 239	\$ —	\$ —	\$ 239
Foreclosed assets	2,386	—	—	2,386

For Level 3 assets measured at fair value on a non-recurring basis as of June 30, 2017 and December 31, 2016, the significant unobservable inputs used in the fair value measurements are presented below (in thousands).

	Balance as of June 30, 2017	Valuation Technique	Significant Other Unobservable Input	Weighted Average of Input
Impaired loans	\$ 651	Appraisal	Appraisal Discounts	13.0%
Foreclosed assets	2,369	Appraisal	Appraisal Discounts	22.5%

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 7. Fair Value Disclosures, Continued

Assets Measured at Fair Value on a Nonrecurring Basis (continued):

	Balance as of December 31, 2016 (in thousands)	Valuation Technique	Significant Other Unobservable Input	Weighted Average of Input
Impaired loans	\$ 239	Cash Flow	Discounted Cash Flow / Appraisal Discounts	2.4%
Foreclosed assets	2,386	Appraisal	Appraisal Discounts	12.2%

Impaired Loans: Loans considered impaired under ASC 310-10-35, *Receivables*, are loans for which, based on current information and events, it is probable that the Company will be unable to collect all principal and interest payments due in accordance with the contractual terms of the loan agreement. Impaired loans can be measured based on the present value of expected payments using the loan's original effective rate as the discount rate, the loan's observable market price, or the fair value of the collateral less selling costs if the loan is collateral dependent.

The fair value of impaired loans were measured based on the value of the collateral securing these loans or the discounted cash flows of the loans, as applicable. Impaired loans are classified within Level 3 of the fair value hierarchy. Collateral may be real estate and/or business assets including equipment, inventory, and/or accounts receivable. The Company determines the value of the collateral based on independent appraisals performed by qualified licensed appraisers. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Appraised values are discounted for costs to sell and may be discounted further based on management's historical knowledge, changes in market conditions from the date of the most recent appraisal, and/or management's expertise and knowledge of the customer and the customer's business. Such discounts by management are subjective and are typically significant unobservable inputs for determining fair value. Impaired loans are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly, based on the same factors discussed above.

Foreclosed assets: Foreclosed assets, consisting of properties obtained through foreclosure or in satisfaction of loans, are initially recorded at fair value less estimated costs to sell upon transfer of the loans to other real estate. Subsequently, other real estate is carried at the lower of carrying value or fair value less costs to sell. Fair values are generally based on third party appraisals of the property and are classified within Level 3 of the fair value hierarchy. The appraisals are sometimes further discounted based on management's historical knowledge, and/or changes in market conditions from the date of the most recent appraisal, and/or management's expertise and knowledge of the customer and the customer's business. Such discounts are typically significant unobservable inputs for determining fair value. In cases where the carrying amount exceeds the fair value, less estimated costs to sell, a loss is recognized in noninterest expense.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 7. Fair Value Disclosures, Continued

Carrying value and estimated fair value:

The carrying amount and estimated fair value of the Company's financial instruments at June 30, 2017 and December 31, 2016 are as follows (in thousands):

	June 30, 2017		December 31, 2016	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets:				
Cash and cash equivalents	\$ 82,835	\$ 82,835	\$ 68,748	\$ 68,748
Securities available for sale	132,762	132,762	129,422	129,422
Restricted investments	6,081	N/A	5,628	N/A
Loans, net	859,923	851,841	808,271	803,057
Liabilities:				
Noninterest-bearing demand deposits	183,324	183,324	153,483	153,483
Interest-bearing demand deposits	156,150	156,150	162,702	162,702
Money Market and Savings deposits	324,014	324,014	274,605	274,605
Time deposits	318,147	318,211	316,275	316,734
Securities sold under agreements to repurchase	22,946	22,946	26,622	26,622
Federal Home Loan Bank advances and other borrowings	—	—	18,505	18,505

Limitations

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on many judgments. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on existing on and off-balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Significant assets and liabilities that are not considered financial instruments include deferred income taxes and premises and equipment. In addition, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in the estimates.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

Note 8. Small Business Lending Fund

During 2011, the Company issued to the Secretary of the Treasury 12,000 shares of preferred stock at \$1,000 per share under the Small Business Lending Fund Program (the "SBLF Program"). Subject to regulatory approval, the Company may redeem the preferred stock for \$1,000 per share, plus accrued and unpaid dividends, in whole or in part at any time. The SBLF Program is a voluntary program authorized under the Business Jobs Acts of 2010, whereby the United States Treasury can make capital investments in eligible institutions; the capital investments, in turn, are designed to increase the availability of credit for small businesses and promote economic growth by providing capital to qualified community banks at favorable rates. The Company paid cash dividends at a one percent rate or \$120,000 for the year ended December 31, 2015. On February 4, 2016 the dividend rate for the preferred shares increased to nine percent and as a result the company incurred preferred stock dividends of \$1,022,000 for the year ended December 31, 2016.

On January 30, 2017, the Company completed a public offering of 2,010,084 million shares of its common stock, par value \$1.00 per share, with the net proceeds to the Company of approximately \$33.2 million. Subsequent to the public offering the Company used proceeds from the offering to redeem the \$12 million of preferred stock and pay the \$195 thousand accrued dividend on March 6, 2017.

Note 9. Business Combination

On December 8, 2016, the Bank entered into a purchase and assumption agreement with Atlantic Capital Bank, N.A. that provided for the acquisition and assumption by the Bank of certain assets and liabilities associated with Atlantic Capital Bank's branch office located at 3200 Keith Street NW, Cleveland, Tennessee 37312. The purchase was completed on May 19, 2017 for total cash consideration of \$1,183,007.

The assets and liabilities as of the effective date of the merger were recorded at their respective estimated fair values. The excess of the purchase price over the net estimated fair values of the acquired assets and liabilities was allocated to identifiable intangible assets with the remaining excess allocated to goodwill.

In the periods following the acquisition, the financial statements will include the results attributable to the Cleveland branch purchase beginning on the date of purchase. For the six months period ended June 30, 2017, the revenues and net income attributable to the Cleveland branch were \$178,847 and \$52,465, respectively. It is impracticable to determine the pro-forma impact to the 2016 revenues and net income if the acquisition had occurred on January 1, 2016 as the Company does not have access to those records for a single branch.

The following table details the financial impact of the merger, including the allocation of the purchase price to the fair values of net assets assumed and goodwill recognized:

Allocation of Purchase Price (amounts in thousands)	
Total consideration in cash	\$ 1,183
Fair value of assets acquired and liabilities assumed:	
Cash and cash equivalents	133
Loans	24,073
Premises and equipment	2,839
Core deposit intangible	310
Prepaid and other assets	77
Deposits	(26,888)
Payables and other liabilities	(21)
Total fair value of net assets acquired	523
Goodwill	\$ 660

As of June 30, 2017 there have not been any changes to the initial fair values recorded as part of the business combination.

SMARTFINANCIAL, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

SmartFinancial, Inc. (the "Company" or "SmartFinancial") is a bank holding company incorporated under the laws of Tennessee and headquartered in Knoxville, Tennessee. The Company conducts its business operations primarily through its wholly-owned subsidiary, SmartBank, a Tennessee chartered community bank providing services through fourteen branches, one loan production office, and one mortgage production office located in East Tennessee, the Florida Panhandle, and North Georgia.

Executive Summary

The following is a summary of the Company's financial highlights and significant events during the second quarter and the first six months of 2017 :

- Net income available to common shareholders totaled \$1.6 million , or \$0.20 per share, during the second quarter of 2017 compared to \$0.9 million , or \$0.15 per share, during the second quarter of 2016 .
- Closed acquisition of Cleveland, Tennessee, branch purchasing approximately \$24.4 million in loans and assuming \$26.8 million in deposits, in book value, resulting in approximately \$1.0 million in intangible assets.
- Annualized return on average assets was 0.61 percent in the second quarter of 2017 , compared to 0.48 percent a year ago.
- Gross loan growth of \$52.0 million for first six months of 2017 , including loans purchased in 2017 which had a net carrying of approximately \$20.6 million at quarter end.
- Net interest margin, taxable equivalent, of 4.11 percent for first six months of 2017 , up from 4.06 percent a year ago.
- Asset quality was outstanding with nonperforming assets to total assets dropping to just 0.30 percent .
- Announced pending acquisition of Capstone Bancshares, Inc of Tuscaloosa, Alabama which upon completion the Company is expected to have assets in excess of \$1.5 billion.

Analysis of Results of Operations

Second quarter of 2017 compared to 2016

Net income was \$1.6 million in the second quarter of 2017 , which was up from \$1.2 million in the second quarter of 2016 . Net income available to common shareholders was \$1.6 million , or \$0.20 per diluted common share, in the second quarter of 2017 , an increase from \$0.9 million , or \$0.15 per diluted common share, in the second quarter of 2016 . Net interest income to average assets of 3.81 percent in the second quarter of 2017 was down from 3.87 percent in the second quarter of 2016 as the percentage of non-earning assets increased compared to the prior year. Noninterest income to average assets of 0.47 percent was up from 0.39 percent in the second quarter of 2016 primarily due to gains from higher sales volumes of SBA and mortgage loans. Noninterest expense to average assets decreased from 3.41 percent in the second quarter of 2016 to 3.29 percent in second quarter of 2017 primarily due to increases in average assets as the Company continues to capitalize on efficiencies of scale.

The first six months of 2017 compared to 2016

Net income was \$3.3 million in the first six months of 2017 , which was up from \$2.5 million in the first six months of 2016 . Net income available to common shareholders was \$3.1 million , or \$0.39 per diluted common share, in the first six months of 2017 , an increase from \$2.1 million , or \$0.34 per diluted common share, in the first six months of 2016 . Net interest income to average assets of 3.81 percent in the first six months of 2017 was up from 3.77 percent in the first six months of 2016 due to increases in the net interest spread. Noninterest income to average assets of 0.41 percent was unchanged from 0.41 percent in the first six months of 2016 . Noninterest expense to average assets decreased from 3.30 percent in the first six months of 2016 to 3.22 percent in first six months of 2017 primarily due to increases in average assets as the Company continues to capitalize on efficiencies of scale.

Net Interest Income and Yield Analysis

Second quarter of 2017 compared to 2016

Net interest income, taxable equivalent, improved to \$10.3 million in the second quarter of 2017 from \$9.6 million in the second quarter of 2016. The increase in net interest income was primarily due to increases in average loan balances. Average earning assets increased from \$928.7 million in the second quarter of 2016 to \$992.1 million in the second quarter of 2017. Over this period, average loan balances increased by \$83.2 million primarily as a result of organic growth. In addition, average interest-bearing deposits increased by \$38.5 million and average noninterest-bearing deposits increased \$25.2 million, a result of organic growth combined with the acquired deposits. Net interest income to average assets of 3.81 percent for the second quarter in 2017 was down from 3.87 percent during the same period in 2016 as the percentage of non-earning assets increased compared to the prior year. Net interest margin, taxable equivalent, was 4.15 percent in the quarter, compared to 4.16 percent a year ago as a result of higher costs on interest-bearing deposits. The yield on earning assets increased from 4.62 percent a year ago to 4.66 percent in the quarter due to higher loan balances and higher yields on securities.

The following table summarizes the major components of net interest income and the related yields and costs for the periods presented.

	Three Months Ended June 30, 2017			Three Months Ended June 30, 2016		
	Average		Yield/	Average		Yield/
	Balance	Interest *	Cost*	Balance	Interest *	Cost*
Assets						
Loans (1)	\$ 834,665	\$ 10,752	5.17%	\$ 751,425	\$ 9,960	5.32%
Investment securities and interest-bearing due from banks (2)	138,965	707	2.04%	171,526	678	1.59%
Federal funds and other	18,503	78	1.69%	5,719	50	3.51%
Total interest-earning assets	992,133	11,537	4.66%	928,670	10,688	4.62%
Noninterest-earning assets	85,553			66,530		
Total assets	\$ 1,077,686			\$ 995,200		
Liabilities and Stockholders' Equity						
Interest-bearing demand deposits	\$ 156,387	\$ 115	0.29%	\$ 153,881	\$ 69	0.18%
Money market and savings deposits	300,448	424	0.57%	248,401	299	0.48%
Time deposits	305,171	702	0.92%	321,244	645	0.81%
Total interest-bearing deposits	762,006	1,241	0.65%	723,526	1,013	0.56%
Securities sold under agreement to repurchase	19,903	16	0.32%	19,742	15	0.31%
Federal Home Loan Bank advances and other borrowings	3,482	11	1.27%	11,287	29	1.03%
Total interest-bearing liabilities	785,391	1,268	0.65%	754,555	1,057	0.56%
Noninterest-bearing deposits	157,965			132,765		
Other liabilities	659			5,261		
Total liabilities	944,015			891,431		
Stockholders' equity	133,671			102,619		
Total liabilities and stockholders' equity	\$ 1,077,686			\$ 995,200		
Net interest income, taxable equivalent		\$ 10,269		\$ 9,631		
Interest rate spread (3)			4.01%			4.06%
Tax equivalent net interest margin (4)			4.15%			4.16%
Percentage of average interest-earning assets to average interest-bearing liabilities			126.32%			123.08%
Percentage of average equity to average assets			12.40%			10.31%
* Taxable equivalent basis						

- (1) Loans include nonaccrual loans. Loan fees included in loan income was \$589 thousand and \$714 thousand for the quarters ended June 2017 and 2016, respectively. Yields related to loans exempt from income taxes are stated on a taxable-equivalent basis assuming a federal income tax rate of 34.0 percent. The taxable-equivalent adjustment was \$5 thousand for the period ended June 30, 2017 and \$6 thousand for the period ended June 30, 2016.
- (2) Yields related to investment securities exempt from income taxes are stated on a taxable-equivalent basis assuming a federal income tax rate of 34.0 percent. The taxable-equivalent adjustment was \$15 thousand for the period ended June 30, 2017 and \$13 thousand for the period ended June 30, 2016.
- (3) Net interest spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.
- (4) Net interest margin represents net interest income divided by average interest-earning assets.

The first six months of 2017 compared to 2016

Net interest income, taxable equivalent, improved to \$20.1 million in the first six months of 2017 from \$18.8 million in the first six months of 2016 . The increase in net interest income was primarily due to increases in average loan balances. Average earning assets increased from \$927.7 million in the first six months of 2016 to \$985.9 million in the first six months of 2017 . Over this period, average loan balances increased by \$80.0 million primarily as a result of organic growth. In addition, average interest-bearing deposits increased by \$24.1 million and average noninterest-bearing deposits increased \$25.7 million , a result of organic growth combined with the acquired deposits. Net interest income to average assets of 3.81 percent in the first six months of 2017 was up from 3.77 percent in the first six months of 2016 due to increases in the net interest spread. Net interest margin, taxable equivalent, was 4.11 percent in the quarter, compared to 4.06 percent a year ago due to higher yields on earning assets and increases in the balances of noninterest bearing deposits. The yield on earning assets increased from 4.51 percent a year ago to 4.60 percent due to higher loan balances and higher yields on securities.

The following table summarizes the major components of net interest income and the related yields and costs for the periods presented.

	Six Months Ended June 30, 2017			Six Months Ended June 30, 2016		
	Average Balance	Interest *	Yield/ Cost*	Average Balance	Interest *	Yield/ Cost*
Assets						
Loans (1)	\$ 823,157	\$ 20,972	5.14%	\$ 743,172	\$ 19,338	5.22%
Investment securities and interest-bearing due from banks (2)	150,117	1,384	1.86%	177,257	1,408	1.59%
Federal funds and other	12,595	151	2.42%	7,268	113	3.15%
Total interest-earning assets	985,869	22,507	4.60%	927,697	20,859	4.51%
Noninterest-earning assets	75,934			70,449		
Total assets	<u>\$ 1,061,803</u>			<u>\$ 998,146</u>		
Liabilities and Stockholders' Equity						
Interest-bearing demand deposits	\$ 157,813	\$ 208	0.27%	\$ 152,210	\$ 135	0.18%
Money market and savings deposits	288,081	752	0.53%	245,263	571	0.47%
Time deposits	303,721	1,379	0.92%	328,013	1,268	0.78%
Total interest-bearing deposits	749,615	2,339	0.63%	725,486	1,974	0.55%
Securities sold under agreement to repurchase	19,296	32	0.33%	20,490	32	0.31%
Federal Home Loan Bank advances and other borrowings	5,453	26	0.96%	17,396	74	0.85%
Total interest-bearing liabilities	774,364	2,397	0.62%	763,372	2,080	0.55%
Noninterest-bearing deposits	153,659			128,004		
Other liabilities	2,609			4,711		
Total liabilities	930,632			896,087		
Stockholders' equity	131,171			102,061		
Total liabilities and stockholders' equity	<u>\$ 1,061,803</u>			<u>\$ 998,148</u>		
Net interest income, taxable equivalent		<u>\$ 20,110</u>			<u>\$ 18,779</u>	
Interest rate spread (3)			<u>3.98%</u>			<u>3.96%</u>
Tax equivalent net interest margin (4)			<u>4.11%</u>			<u>4.06%</u>
Percentage of average interest-earning assets to average interest-bearing liabilities			<u>127.31%</u>			<u>121.53%</u>
Percentage of average equity to average assets			<u>12.35%</u>			<u>10.23%</u>
* Taxable equivalent basis						

- (1) Loans include nonaccrual loans. Loan fees included in loan income was \$1.2 million and \$1.3 million for the first six months ended June 2017 and 2016 , respectively. Yields related to loans exempt from income taxes are stated on a taxable-equivalent basis assuming a federal income tax rate of 34.0 percent. The taxable-equivalent adjustment was \$9 thousand for the period ended June 30, 2017 and \$11 thousand for the period ended June 30, 2016 .
- (2) Yields related to investment securities exempt from income taxes are stated on a taxable-equivalent basis assuming a federal income tax rate of 34.0 percent. The taxable-equivalent adjustment was \$31 thousand for the period ended June 30, 2017 and \$26 thousand for the period ended June 30, 2016 .
- (3) Net interest spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.
- (4) Net interest margin represents net interest income divided by average interest-earning assets.

Rate and Volume Analysis

Changes in net interest income are attributed to changes in average balances (volume change), changes in average rates (rate change), and, when applicable, changes in the number of days (days change) in the period presented (for earning assets and sources of funds on which interest is received or paid. Days change is calculated as change in days times current interest per day, volume change is calculated as change in volume times the previous rate, and rate change is change in rate times the previous volume. The change attributed to rates and volumes (change in rate times change in volume) is considered as a change in volume.

Second quarter of 2017 compared to 2016

Net interest income, taxable equivalent, increased by \$0.6 million between the quarters ended June 30, 2017 and 2016. The following is an analysis of the changes in net interest income comparing the changes attributable to days those attributable to rates and those attributable to volumes (in thousands):

	Three Months Ended June 30,		
	2017	Compared to	2016
	Increase (decrease) due to		
	Rate	Volume	Net
Interest-earning assets:			
Loans (1)	\$ (312)	\$ 1,104	\$ 792
Investment securities and interest-bearing due from banks (2)	158	(129)	29
Federal funds and other	(84)	112	28
Total interest-earning assets	(238)	1,087	849
Interest-bearing liabilities:			
Interest-bearing demand deposits	45	1	46
Money market and savings deposits	63	62	125
Time deposits	89	(32)	57
Total interest-bearing deposits	197	31	228
Securities sold under agreement to repurchase	1	—	1
Federal Home Loan Bank advances and other borrowings	2	(20)	(18)
Total interest-bearing liabilities	200	11	211
Net interest income	\$ (438)	\$ 1,076	\$ 638

- (1) Loans include nonaccrual loans. Yields related to loans exempt from income taxes are stated on a taxable-equivalent basis assuming a federal income tax rate of 34.0 percent. The taxable-equivalent adjustment was \$5 thousand for the period ended June 30, 2017 and \$6 thousand for the period ended June 30, 2016.
- (2) Yields related to investment securities exempt from income taxes are stated on a taxable-equivalent basis assuming a federal income tax rate of 34.0 percent. The taxable-equivalent adjustment was \$15 thousand for the period ended June 30, 2017 and \$13 thousand for the period ended June 30, 2016.

The first six months of 2017 compared to 2016

Net interest income, taxable equivalent, increased by \$1.3 million between the first six months ended June 30, 2017 and 2016 . The following is an analysis of the changes in net interest income comparing the changes attributable to days those attributable to rates and those attributable to volumes (in thousands):

	Six Months Ended June 30,			
	2017	Compared to		2016
	Increase (decrease) due to			
	Rate	Days	Volume	Net
Interest-earning assets:				
Loans (1)	\$ (342)	\$ (106)	\$ 2,082	\$ 1,634
Investment securities and interest-bearing due from banks (2)	199	(8)	(215)	(24)
Federal funds and other	(45)	(1)	84	38
Total interest-earning assets	(188)	(115)	1,951	1,648
Interest-bearing liabilities:				
Interest-bearing demand deposits	69	(1)	5	73
Money market and savings deposits	84	(3)	100	181
Time deposits	212	(7)	(94)	111
Total interest-bearing deposits	365	(11)	11	365
Securities sold under agreement to repurchase	2	—	(2)	—
Federal Home Loan Bank advances and other borrowings	3	—	(51)	(48)
Total interest-bearing liabilities	370	(11)	(42)	317
Net interest income	\$ (558)	\$ (104)	\$ 1,993	\$ 1,331

- (1) Loans include nonaccrual loans. Loan fees included in loan income was \$1.2 million and \$1.3 million for the first six months ended June 2017 and 2016 , respectively. Yields related to loans exempt from income taxes are stated on a taxable-equivalent basis assuming a federal income tax rate of 34.0 percent. The taxable-equivalent adjustment was \$9 thousand for the period ended June 30, 2017 and \$11 thousand for the period ended June 30, 2016 .
- (2) Yields related to investment securities exempt from income taxes are stated on a taxable-equivalent basis assuming a federal income tax rate of 34.0 percent. The taxable-equivalent adjustment was \$31 thousand for the period ended June 30, 2017 and \$26 thousand for the period ended June 30, 2016 .

Noninterest Income

Second quarter of 2017 compared to 2016

Noninterest income totaled \$1.3 million in the second quarter of 2017 , compared to \$1.0 million in the second quarter of 2016 . Noninterest income to average assets of 0.47 percent for the quarter was up from 0.39 percent in 2016 primarily due to gains from higher sales volumes of SBA and mortgage loans which were \$405 thousand , up from \$197 thousand a year ago.

(Dollars in thousands)	Three months ended June 30,	
	2017	2016
Service charges and fees on deposit accounts	\$ 291	\$ 259
Gain on sale of securities	—	98
Gain on sale of loans and other assets	405	198
Gain (loss) on sale of foreclosed assets	1	(4)
Other noninterest income	556	410
Total noninterest income	\$ 1,253	\$ 961

The first six months of 2017 compared to 2016

Noninterest income totaled \$2.2 million in the first six months of 2017, compared to \$2.0 million in the first six months of 2016. Noninterest income to average assets of 0.41 percent was unchanged from 0.41 percent in the first six months of 2016. Charges and fees on deposit accounts were unchanged from a year ago. Gains on the sale of loans, which includes mortgage and SBA loans, were \$681 thousand, up from \$419 thousand a year ago.

(Dollars in thousands)	Six months ended June 30,	
	2017	2016
Service charges and fees on deposit accounts	\$ 555	\$ 555
Gain on sale of securities	—	181
Gain on sale of loans and other assets	681	419
Gain (loss) on sale of foreclosed assets	(15)	54
Other noninterest income	958	822
Total noninterest income	<u>\$ 2,179</u>	<u>\$ 2,032</u>

Noninterest Expense

Second quarter of 2017 compared to 2016

Noninterest expense totaled \$8.8 million in the second quarter of 2017 compared to \$8.5 million in the second quarter of 2016. Noninterest expense to average assets decreased from 3.41 percent a year ago to 3.29 percent in the quarter. The increase in noninterest expense compared to the prior year was primarily due to annual merit based salary increases and merger and conversion costs related to this quarter's branch acquisition and the pending Capstone Bancshares acquisition.

(Dollars in thousands)	Three months ended June 30,	
	2017	2016
Salaries and employee benefits	\$ 4,758	\$ 4,486
Net occupancy and equipment expense	963	1,137
Depository insurance	61	151
Foreclosed assets	12	64
Advertising	129	184
Data processing	475	554
Professional services	473	551
Amortization of intangible assets	61	93
Service contracts	313	316
Other operating expenses	1,584	936
Total noninterest expense	<u>\$ 8,829</u>	<u>\$ 8,472</u>

The first six months of 2017 compared to 2016

Noninterest expense totaled \$17.0 million in the first six months of 2017 compared to \$16.4 million in the first six months of 2016 . Noninterest expense to average assets decreased from 3.30 percent a year ago to 3.22 percent in the during the period. The increase in noninterest expense compared to the prior year was primarily due to annual merit based salary increases and merger and conversion costs related to this quarter's branch acquisition and the pending Capstone Bancshares acquisition.

(Dollars in thousands)	Six months ended June 30,	
	2017	2016
Salaries and employee benefits	\$ 9,404	\$ 8,981
Net occupancy and equipment expense	1,941	2,155
Depository insurance	214	287
Foreclosed assets	11	120
Advertising	294	357
Data processing	808	896
Professional services	1,043	1,007
Amortization of intangible assets	114	187
Service contracts	609	601
Other operating expenses	2,536	1,833
Total noninterest expense	<u>\$ 16,974</u>	<u>\$ 16,424</u>

Taxes

Second quarter of 2017 compared to 2016

In the second quarter of 2017 income tax expense totaled \$726 thousand compared to \$691 thousand a year ago. The effective tax rate was approximately 36.7 percent a year ago compared to approximately 30.6 percent in the second quarter of 2017 .

The first six months of 2017 compared to 2016

In the first six months of 2017 income tax expense totaled \$1.7 million compared to \$1.5 million a year ago. The effective tax rate was approximately 36.4 percent a year ago compared to approximately 33.7 percent in the first six months of 2017 .

Loan Portfolio Composition

The Company had total net loans outstanding, including organic and purchased loans, of approximately \$859.9 million at June 30, 2017 and \$808.3 million at December 31, 2016 . Loans secured by real estate, consisting of commercial or residential property, are the principal component of our loan portfolio. We do not generally originate traditional long-term residential fixed rate mortgages for our portfolio but we do originate and hold traditional second mortgage residential real estate loans, adjustable rate mortgages and home equity lines of credit. Even if the principal purpose of the loan is not to finance real estate, when reasonable, we attempt to obtain a security interest in the real estate in addition to any other available collateral to increase the likelihood of ultimate repayment or collection of the loan.

Organic Loans

Our organic net loans increased by \$62.0 million , or 10.1 percent , from December 31, 2016 , to \$674.0 million at June 30, 2017 as we continue to originate well-underwritten loans. Our goal of streamlining the credit process has improved our efficiency and is a competitive advantage in many of our markets. In addition, the overall business environment continues to rebound from recessionary conditions. Organic loans include loans which were originally purchased non-credit impaired loans but have been renewed since purchase.

Purchased Loans

Purchased non-credit impaired loans of \$160.8 million at June 30, 2017 were down from \$169.2 million at December 31, 2016 as a result of loan payoffs and renewals. Since December 31, 2016, our net purchased credit impaired (“PCI”) loans decreased by \$2.0 million to \$25.2 million at June 30, 2017. The activity within the purchased credit impaired loans will be impacted by how quickly these loans are resolved and/or our future acquisition activity.

The following tables summarize the composition of our loan portfolio for the periods presented (dollars in thousands):

	June 30, 2017				% of Gross Total
	Organic Loans	Purchased Non-Credit Impaired Loans	Purchased Credit Impaired Loans	Total Amount	
Commercial real estate-mortgage	\$ 329,432	\$ 101,340	\$ 14,417	\$ 445,189	51.4%
Consumer real estate-mortgage	156,501	42,095	8,071	206,667	23.9%
Construction and land development	95,033	4,649	1,474	101,156	11.7%
Commercial and industrial	92,317	11,667	1,249	105,233	12.2%
Consumer and other	6,167	1,009	—	7,176	0.8%
Total gross loans receivable, net of deferred fees	679,450	160,760	25,211	865,421	100.0%
Allowance for loan and lease losses	(5,498)	—	—	(5,498)	
Total loans, net	\$ 673,952	\$ 160,760	\$ 25,211	\$ 859,923	

	December 31, 2016				% of Gross Total
	Organic Loans	Purchased Non-Credit Impaired Loans	Purchased Credit Impaired Loans	Total Amount	
Commercial real estate-mortgage	\$ 297,689	\$ 102,576	\$ 14,943	\$ 415,208	51.0%
Consumer real estate-mortgage	135,923	42,875	9,004	187,802	23.1%
Construction and land development	108,390	7,801	1,678	117,869	14.5%
Commercial and industrial	68,235	15,219	1,568	85,022	10.5%
Consumer and other	6,786	689	—	7,475	0.9%
Total gross loans receivable, net of deferred fees	617,023	169,160	27,193	813,376	100.0%
Allowance for loan and lease losses	(5,105)	—	—	(5,105)	
Total loans, net	\$ 611,918	\$ 169,160	\$ 27,193	\$ 808,271	

Loan Portfolio Maturities

The following table sets forth the maturity distribution of our loans, including the interest rate sensitivity for loans maturing after one year.

	One Year or Less	One through Five Years	Over Five Years	Total	Rate Structure for Loans Maturing Over One Year	
					Fixed Rate	Floating Rate
Commercial real estate-mortgage	\$ 30,973	\$ 208,909	\$ 205,307	\$ 445,189	\$ 279,353	\$ 134,863
Consumer real estate-mortgage	18,473	93,863	94,331	206,667	109,783	78,411
Construction and land development	21,783	44,822	34,551	101,156	40,620	38,753
Commercial and industrial	23,740	56,354	25,139	105,233	67,444	14,049
Consumer and other	2,581	3,943	652	7,176	2,694	1,901
Total Loans	\$ 97,550	\$ 407,891	\$ 359,980	\$ 865,421	\$ 499,894	\$ 267,977

Nonaccrual, Past Due, and Restructured Loans

Nonperforming loans as a percentage of total gross loans, net of deferred fees, was 0.13 percent as of June 30, 2017, which was down from 0.26 percent as of December 31, 2016. Total nonperforming assets as a percentage of total assets as of June 30, 2017 totaled 0.30 percent compared to 0.42 percent as of December 31, 2016. Acquired PCI loans that are included in loan pools are reclassified at acquisition to accrual status and thus are not included as nonperforming assets unless the pools are 90 days or greater past due.

The following table summarizes the Company's nonperforming assets for the periods presented.

(Dollars in thousands)	June 30, 2017	December 31, 2016
Nonaccrual loans	\$ 1,084	\$ 1,415
Accruing loans past due 90 days or more (1)	30	699
Total nonperforming loans	1,114	2,114
Foreclosed assets	2,369	2,386
Total nonperforming assets	\$ 3,483	\$ 4,500
Restructured loans not included above	\$ 44	\$ 166

(1) Balances include PCI loans past due 90 days or more that are grouped in pools which accrue interest based on pool yields.

Potential Problem Loans

At June 30, 2017 potential problem loans amounted to approximately \$906.2 thousand or 0.10 percent of total loans outstanding. Potential problem loans, which are not included in nonperforming loans, represent those loans with a well-defined weakness and where information about possible credit problems of borrowers has caused management to have doubts about the borrower's ability to comply with present repayment terms. This definition is believed to be substantially consistent with the standards established by the Bank's primary regulators, for loans classified as substandard or worse, but not considered nonperforming loans.

Allocation of the Allowance for Loan Losses

We maintain the allowance at a level that we deem appropriate to adequately cover the probable losses inherent in the loan portfolio. As of June 30, 2017 and December 31, 2016, our allowance for loan losses was \$5.5 million and \$5.1 million, respectively, which we deemed to be adequate at each of the respective dates. The increase in the allowance for loan losses in 2017 as compared to 2016 is the result of increases in the organic loan portfolio. Our allowance for loan loss as a percentage of total loans has increased slightly from 0.63 percent at December 31, 2016 to 0.64 percent at June 30, 2017. As a percentage of organic loans the allowance for loan losses decreased from 0.83 percent at December 31, 2016 to 0.81 percent at June 30, 2017.

Our purchased loans were recorded at fair value upon acquisition. The fair value adjustments on the performing purchased loans will be accreted into income over the life of the loans. As of June 30, 2017 the balance on PCI loans was \$32.5 million while the carrying value was \$25.2 million. These loans are subject to the same allowance methodology as our legacy portfolio. The calculated allowance is compared to the remaining fair value discount to determine if additional provisioning should be recognized. At June 30, 2017, there were no allowances on PCI loans.

The following table sets forth, based on our best estimate, the allocation of the allowance to types of loans as of June 30, 2017 and December 31, 2016 and the percentage of loans in each category to total loans (in thousands):

	June 30, 2017		December 31, 2016	
	Amount	Percent	Amount	Percent
Commercial real estate-mortgage	\$ 2,489	45.2%	\$ 2,369	46.4%
Consumer real estate-mortgage	1,653	30.1%	1,382	27.1%
Construction and land development	609	11.1%	717	14.0%
Commercial and industrial	644	11.7%	520	10.2%
Consumer and other	103	1.9%	117	2.3%
Total allowance for loan losses	<u>\$ 5,498</u>	<u>100.0%</u>	<u>\$ 5,105</u>	<u>100.0%</u>

The increase in the overall allowance for loan losses is due to the increased balance of organic loans offset by improvements of our loan portfolio and the reduction of nonperforming loans and net charge-offs, which is largely influenced by the overall improvement in the economies in our market areas. The allocation by category is determined based on the assigned risk rating, if applicable, and environmental factors applicable to each category of loans. For impaired loans, those loans are reviewed for a specific allowance allocation. Specific valuation allowances related to impaired loans were approximately \$4 thousand at December 31, 2016 compared to \$97 thousand at June 30, 2017.

Analysis of the Allowance for Loan Losses

The following is a summary of changes in the allowance for loan losses for the periods ended June 30, 2017 and December 31, 2016 including the ratio of the allowance for loan losses to total loans as of the end of each period (in thousands):

	June 30, 2017	December 31, 2016
Balance at beginning of period	\$ 5,105	\$ 4,354
Provision for loan losses	310	788
Charged-off loans:		
Commercial real estate-mortgage	—	—
Consumer real estate-mortgage	(6)	(102)
Construction and land development	—	(14)
Commercial and industrial	—	(35)
Consumer and other	(40)	(155)
Total charged-off loans	(46)	(306)
Recoveries of previously charged-off loans:		
Commercial real estate-mortgage	6	45
Consumer real estate-mortgage	47	76
Construction and land development	8	22
Commercial and industrial	32	58
Consumer and other	36	68
Total recoveries of previously charged-off loans	129	269
Net charge-offs	83	(37)
Balance at end of period	\$ 5,498	\$ 5,105
Ratio of allowance for loan losses to total loans outstanding at end of period	0.64 %	0.63%
Ratio of net charge-offs (recoveries) to average loans outstanding for the period	(0.04)%	0.09%

We assess the adequacy of the allowance at the end of each calendar quarter. This assessment includes procedures to estimate the allowance and test the adequacy and appropriateness of the resulting balance. The level of the allowance is based upon our evaluation of the loan portfolio, past loan loss experience, known and inherent risks in the portfolio, the views of the Bank's regulators, adverse situations that may affect the borrower's ability to repay (including the timing of future payments), the estimated value of any underlying collateral, composition of the loan portfolio, economic conditions, industry and peer bank loan quality indications and other pertinent factors. This evaluation is inherently subjective as it requires material estimates including the amounts and timing of future cash flows expected to be received on impaired loans that may be susceptible to significant change.

Investment Portfolio

Our investment portfolio, consisting primarily of Federal agency bonds, mortgage-backed securities, and state and municipal securities amounted to fair values of \$132.8 million and \$129.4 million at June 30, 2017 and December 31, 2016, respectively. Our investments to assets ratio decreased slightly from 12.2 percent at December 31, 2016 to 11.6 percent at June 30, 2017 as we reduced reinvestments when the five year treasury rate, and other fixed income investments of a similar term, fell in the latter part of the quarter. Our investment portfolio serves many purposes including serving as a potential liquidity source, collateral for public funds, and as a stable source of income.

The following table shows the amortized cost of the Company's investment securities. In the periods ended June 30, 2017 and December 31, 2016 all investment securities were classified as available for sale.

Book Value of Investment Securities

(in thousands)	June 30, 2017	December 31, 2016
U.S. Government agencies	\$ 18,244	\$ 18,279
State and political subdivisions	8,362	8,182
Mortgage-backed securities	105,585	104,585
Other debt securities	972	—
Total securities	\$ 133,163	\$ 131,046

The following table presents the contractual maturity of investment securities by contractual maturity date and average yields based on amortized cost (for all obligations on a fully taxable basis). The composition and maturity / repricing distribution of the securities portfolio is subject to change depending on rate sensitivity, capital and liquidity needs.

Contractual Maturity of Investment Securities

June 30, 2017

(in thousands)	Maturity By Years				
	1 or Less	1 to 5	5 to 10	Over 10	Total
Available for Sale					
U.S. Government agencies	\$ 3,999	\$ 11,000	\$ 3,245	\$ —	\$ 18,244
State and political subdivisions	180	165	4,572	3,445	8,362
Mortgage-backed securities	—	6,098	29,526	69,961	105,585
Other debt securities	—	—	972	—	972
Total securities available for sale	\$ 4,179	\$ 17,263	\$ 38,315	\$ 73,406	\$ 133,163
Weighted average yield (1)	1.31%	1.73%	1.91%	2.11%	1.97%

(1) Based on amortized cost, taxable equivalent basis

Deposits

Deposits are the primary source of funds for the Company's lending and investing activities. The Company provides a range of deposit services to businesses and individuals, including noninterest-bearing checking accounts, interest-bearing checking accounts, savings accounts, money market accounts, IRAs and CDs. These accounts generally earn interest at rates the Company establishes based on market factors and the anticipated amount and timing of funding needs. The establishment or continuity of a core deposit relationship can be a factor in loan pricing decisions. While the Company's primary focus is on establishing customer relationships to attract core deposits, at times, the Company uses brokered deposits and other wholesale deposits to supplement its funding sources. As of June 30, 2017, brokered deposits represented approximately 13.0 percent of total deposits.

Over the last couple years the overall mix of average deposits has shifted to a higher percentage of noninterest-bearing and money market and savings deposits, with reductions in the percentage of deposits held in interest-bearing demand accounts. The Company believes its deposit product offerings are properly structured to attract and retain core low-cost deposit relationships. The average cost of interest-bearing deposits for the three and six months ended June 30, 2017 was 0.65 percent and 0.63 percent, compared to 0.56 percent and 0.55 percent for the same period in 2016. The increase in the costs were due to changes in deposit mix and higher rates on interest-bearing deposit accounts.

Total deposits as of June 30, 2017 were \$981.6 million, which was an increase of \$74.6 million from December 31, 2016. As of June 30, 2017 the Company had outstanding time deposits under \$100,000 with balances of \$139.0 million, time deposits over \$100,000 with balances of \$178.9 million, and a fair value premium for time deposits of approximately \$204 thousand.

The following table summarizes the maturities of time deposits \$100,000 or more as of June 30, 2017.

Remaining maturity: (Dollars in thousands)	June 30, 2017
Three months or less	\$ 43,740
Three to six months	79,490
Six to twelve months	41,070
More than twelve months	14,628
Total	<u>\$ 178,928</u>

Borrowings

The Company uses short-term borrowings and long-term debt to provide both funding and, to a lesser extent, regulatory capital using debt at the Company level which can be downstreamed as Tier 1 capital to the Bank. There were zero short-term borrowings at June 30, 2017. Short-term borrowings totaled \$18.5 million at December 31, 2016 comprised of \$5 million in FHLB advances maturing within twelve months and the remainder consisted of Federal Funds purchased. There was no long-term debt outstanding at June 30, 2017.

Capital Resources

The Company uses leverage analysis to examine the potential of the institution to increase assets and liabilities using the current capital base. The key measurements included in this analysis are the Bank's Common Equity Tier 1 capital, Tier 1 capital, leverage and total capital ratios. At June 30, 2017 and December 31, 2016, our capital ratios, including our Bank's capital ratios, exceeded regulatory minimum capital requirements. From time to time we may be required to support the capital needs of our bank subsidiary. We believe we have various capital raising techniques available to us to provide for the capital needs of our bank, if necessary.

Liquidity and Off-Balance Sheet Arrangements

At June 30, 2017, we had \$154.1 million of pre-approved but unused lines of credit and \$2.8 million of standby letters of credit. These commitments generally have fixed expiration dates and many will expire without being drawn upon. The total commitment level does not necessarily represent future cash requirements. If needed to fund these outstanding commitments, the Bank has the ability to liquidate Federal funds sold or securities available-for-sale, or on a short-term basis to borrow and purchase Federal funds from other financial institutions.

Market Risk and Liquidity Risk Management

The Bank's Asset Liability Management Committee ("ALCO") is responsible for making decisions regarding liquidity and funding solutions based upon approved liquidity, loan, capital and investment policies. The ALCO must consider interest rate sensitivity and liquidity risk management when rendering a decision on funding solutions and loan pricing. To assist in this process the Bank has contracted with an independent third party to prepare quarterly reports that summarize several key asset-liability measurements. In addition, the third party will also provide recommendations to the Bank's ALCO regarding future balance sheet structure, earnings and liquidity strategies. Two critical areas of focus for ALCO are interest rate sensitivity and liquidity risk management. We do not believe there have been any material changes to the Company's interest rate sensitivity or liquidity risk from December 31, 2016 to the period ended June 30, 2017 .

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

This Item is not applicable to smaller reporting companies.

ITEM 4. CONTROLS AND PROCEDURES

Under the supervision and with the participation of management, including SmartFinancial's Chief Executive Officer and Chief Financial Officer, SmartFinancial has evaluated the effectiveness of its disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as of June 30, 2017 (the "Evaluation Date"). Based on such evaluation, such officers have concluded that, as of the Evaluation Date, SmartFinancial's disclosure controls and procedures were effective in alerting them on a timely basis to material information relating to SmartFinancial (including its consolidated subsidiaries) required to be included in SmartFinancial's periodic filings under the Exchange Act.

There were no changes in SmartFinancial's internal control over financial reporting during SmartFinancial's fiscal quarter ended June 30, 2017 that have materially affected, or are reasonably likely to materially affect, SmartFinancial's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

There are various claims and lawsuits in which SmartFinancial is periodically involved incidental to the Bank's business. In the opinion of management, no material loss is expected from any of such pending claims or lawsuits.

SmartFinancial and its wholly owned subsidiary, SmartBank, are periodically involved as a plaintiff or a defendant in various legal actions in the ordinary course of business. While the outcome of these matters is not currently determinable, neither SmartFinancial nor SmartBank is involved in any litigation that is expected to have a material impact on our financial position, results of operations, or cash flow. Management believes that any claims pending against SmartFinancial or SmartBank are without merit or that the ultimate liability, if any, resulting from such claims will not materially affect SmartBank's financial condition or SmartFinancial's consolidated financial position.

Item 1A. Risk Factors.

SmartFinancial, as a smaller reporting company, is not required to provide the information required by this Item.

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

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not Applicable.

Item 5. Other Information.

None.

Item 6. Exhibits

2.1	Agreement and Plan of Merger dated May 22, 2017, by and between SmartFinancial, Inc., SmartBank, Capstone Bancshares, Inc. and Capstone Bank (incorporated herein by reference to Exhibit 2.1 to the Company's Form 8-k filed on May 23, 2017)
31.1	Certification pursuant to Rule 13a-14(a)/15d-14(a)
31.2	Certification pursuant to Rule 13a-14(a)/15d-14(a)
32.1	Certification pursuant to 18 USC Section 1350 – Sarbanes-Oxley Act of 2002
32.2	Certification pursuant to 18 USC Section 1350 – Sarbanes-Oxley Act of 2002
101	Interactive Data Files

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SmartFinancial, Inc.

Date: August 14, 2017

/s/ William Y. Carroll, Jr.

William Y. Carroll, Jr.

President and Chief Executive Officer

(principal executive officer)

Date: August 14, 2017

/s/ Christopher Bryan Johnson

Christopher Bryan Johnson

Executive Vice President and Chief Financial Officer

(principal financial officer and accounting officer)

CERTIFICATION

I, William Y. Carroll, Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of SmartFinancial, Inc (the "Registrant");
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this period report;
4. The Registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
 - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervisions, to ensure that material information relating to the registrant, including its consolidated subsidiary, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of Issuer's board of directors:
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 14, 2017

/s/ William Y. Carroll, Jr.

William Y. Carroll, Jr.

President and Chief Executive Officer

CERTIFICATION

I, Christopher Bryan Johnson, certify that:

1. I have reviewed this quarterly report on Form 10-Q of SmartFinancial, Inc (the "Registrant");
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this period report;
4. The Registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
 - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervisions, to ensure that material information relating to the registrant, including its consolidated subsidiary, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of Issuer's board of directors:
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 14, 2017

/s/ Christopher Bryan Johnson

Christopher Bryan Johnson

Chief Financial Officer

**18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of SmartFinancial, Inc., (the "Company"), on Form 10-Q for the quarter ended June 30, 2017, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, William Y. Carroll, Jr., President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ William Y. Carroll, Jr.

William Y. Carroll, Jr.

President and Chief Executive Officer

August 14, 2017

**18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of SmartFinancial, Inc., (the "Company"), on Form 10-Q for the quarter ended June 30, 2017, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Christopher Bryan Johnson, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Christopher Bryan Johnson

Christopher Bryan Johnson

Chief Financial Officer

August 14, 2017