MIDSOUTH BANCORP INC
Form 10-Q
November 09, 2011

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

FORM 10-Q

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

For the quarterly period ended September 30, 2011

OR

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

For the transition period from _____ to _____

COMMISSION FILE NUMBER 1-11826
MIDSOUTH BANCORP, INC.
(Exact name of registrant as specified in its charter)

Louisiana	72 –1020809
(State of other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

102 Versailles Boulevard, Lafayette, Louisiana 70501
(Address of principal executive offices, including zip code)
(337) 237-8343
(Registrant’s telephone number, including area code)

Indicate by checkmark 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 x 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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
YES x NO ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a small reporting company.
Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨ Small reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.)
YES ¨ NO x

As of November 4, 2011, there were 9,730,506 shares of the registrant’s Common Stock, par value $0.10 per share, outstanding.

Table of Contents

Part I – Financial Information

Item 1. Financial Statements.
MidSouth Bancorp, Inc. and Subsidiaries
Consolidated Balance Sheets
(dollars in thousands, except share data)

	September 30, 2011 (unaudited)	December 31, 2010* (audited)
Assets		
Cash and due from banks, including required reserves of $5,803 and $3,487, respectively	$ 22,100	$ 20,758
Interest-bearing deposits in banks	73,575	69,452
Federal funds sold	2,127	1,697
Time deposits held in banks	-	5,164
Securities available-for-sale, at fair value (cost of $313,054 at September 30, 2011 and $257,472 at December 31, 2010)	325,736	263,809
Securities held-to-maturity (fair value of $44,114 at September 30, 2011 and $1,608 at December 31, 2010)	43,736	1,588
Other investments	5,057	5,062
Loans	673,426	580,812
Allowance for loan losses	(7,329)	(8,813)
Loans, net	666,097	571,999
Bank premises and equipment, net	40,752	36,592
Accrued interest receivable	5,270	4,628
Goodwill	16,997	9,271
Intangibles	2,710	115
Cash surrender value of life insurance	4,813	4,698
Other real estate	7,278	1,206
Other assets	5,703	6,300
Total assets	$ 1,221,951	$ 1,002,339
Liabilities and Shareholders' Equity		
Liabilities:		
Deposits:		
Non-interest-bearing	$ 222,937	$ 199,460
Interest bearing	766,073	601,312
Total deposits	989,010	800,772
Securities sold under agreements to repurchase	55,078	43,826
Junior subordinated debentures	15,465	15,465
Other liabilities	9,031	5,623
Total liabilities	1,068,584	865,686
Commitments and contingencies	-	-
Shareholders' equity:		
Series A Preferred stock, no par value; 5,000,000 shares authorized, no shares issued and outstanding at September 30, 2011 and 20,000 shares issued and outstanding at December 31, 2010	-	19,408
Series B Preferred stock, no par value; 5,000,000 shares authorized, 32,000 shares issued and outstanding at September 30, 2011 and no shares issued and outstanding at	32,000	-

December 31, 2010		
Common stock, $0.10 par value; 30,000,000 shares authorized, 9,880,743 issued and 9,730,266 outstanding at September 30, 2011 and December 31, 2010	988	988
Additional paid-in capital	89,991	89,893
Unearned ESOP shares	(17)	(104)
Accumulated other comprehensive income	8,370	4,182
Treasury stock – 150,477 shares at September 30, 2011 and December 31, 2010, at cost	(3,286)	(3,286)
Retained earnings	25,321	25,572
Total shareholders' equity	153,367	136,653
Total liabilities and shareholders' equity	$ 1,221,951	$ 1,002,339

See notes to unaudited consolidated financial statements.
* Derived from audited financial statements

Table of Contents

MidSouth Bancorp, Inc. and Subsidiaries
Consolidated Statements of Earnings (unaudited)
(in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Interest income:				
Loans, including fees	$10,803	$10,104	$30,015	$29,832
Securities and other investments:				
Taxable	1,407	925	3,538	2,816
Nontaxable	816	986	2,597	3,009
Federal funds sold	2	3	7	4
Time and interest bearing deposits in other banks	49	59	170	214
Other investments	43	43	116	113
Total interest income	13,120	12,120	36,443	35,988
Interest expense:				
Deposits	1,013	1,325	2,985	4,316
Securities sold under agreements to repurchase	207	249	602	713
Federal funds purchased	-	-	-	2
Other borrowed money	-	-	-	3
Junior subordinated debentures	242	247	726	731
Total interest expense	1,462	1,821	4,313	5,765
Net interest income	11,658	10,299	32,130	30,223
Provision for loan losses	650	1,500	3,150	4,150
Net interest income after provision for loan losses	11,008	8,799	28,980	26,073
Non-interest income:				
Service charges on deposits	1,781	2,427	5,066	7,485
Gain on securities, net	-	-	99	-
ATM and debit card income	964	859	2,797	2,489
Other charges and fees	653	450	1,679	1,427
Total non-interest income	3,398	3,736	9,641	11,401
Non-interest expenses:				
Salaries and employee benefits	5,778	5,118	15,980	15,306
Occupancy expense	2,474	2,177	6,718	6,709
FDIC insurance	188	334	711	986
Other	4,735	3,488	11,726	10,019
Total non-interest expenses	13,175	11,117	35,135	33,020
Income before income taxes	1,231	1,418	3,486	4,454
Income tax expense	131	179	292	530
Net earnings	1,100	1,239	3,194	3,924
Dividends on preferred stock and accretion of warrants	804	300	1,402	898
Net earnings available to common shareholders	$296	$939	$1,792	$3,026

Earnings per share:				
Basic	$0.03	$0.09	$0.18	$0.31
Diluted	$0.03	$0.09	$0.18	$0.31

See notes to unaudited consolidated financial statements.

MidSouth Bancorp, Inc. and Subsidiaries
Consolidated Statement of Shareholders' Equity (unaudited)
For the Nine Months Ended September 30, 2011
(in thousands, except share and per share data)

	Preferred Stock Series A		Preferred Stock Series B		Common Stock		Additional Paid-in Capital	Unearned ESOP Shares	Accumulated Other Comprehensive Income	Treasury Stock	Retained Earnings	Total
	Shares	Amt	Shares	Amt	Shares	Amt						
ance-cember 31, 0	20,000	$19,408	-	$-	9,880,743	$988	$89,893	$(104)	$4,182	$(3,286)	$25,572	$136,653
earnings	-	-	-	-	-	-	-	-	-	-	3,194	3,194
realized ding gains on urities ilable-for-sale ing during the iod, net of ome tax ense of $2,191	-	-	-	-	-	-	-	-	4,253	-	-	4,253
classification ustment for n on securities ilable-for-sale, of income tax ense of $34	-	-	-	-	-	-	-	-	(65)	-	-	(65)
mprehensive ome												7,382
idends on ies A Preferred ck and retion of nmon stock rants	-	592	-	-	-	-	-	-	-	-	(1,242)	(650)
payment of ies A Preferred ck	(20,000)	(20,000)			-	-	-	-	-	-		(20,000)
uance of Series referred Stock			32,000	32,000	-	-	-	-	-	-		32,000
idends on ies B Preferred ck	-	-	-	-	-	-	-	-	-	-	(160)	(160)
idends on nmon stock, 21 per share	-	-	-	-	-	-	-	-	-	-	(2,043)	(2,043)
OP npensation ense	-	-	-	-	-	-	32	87	-	-	-	119

ck option and ricted stock npensation ense	-	-	-	-	-	-	66	-	-	-	-	66
ance- tember 30, 1	-	$-	32,000	$32,000	9,880,743	$988	$89,991	$(17)	$8,370	$(3,286)	$25,321	$153,367

MidSouth Bancorp, Inc. and Subsidiaries
Consolidated Statements of Cash Flows (unaudited)
(in thousands)

	For the Nine Months Ended September 30,	
	2011	2010
Cash flows from operating activities:		
Net earnings	$3,194	$3,924
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	2,504	2,623
Provision for loan losses	3,150	4,150
Provision for deferred tax expense	(189)	(838)
Amortization of premiums on securities, net	679	909
Amortization of other investments	10	-
Stock compensation expense	14	5
Restricted stock expense	52	23
Net gain on sale of investment securities	(99)	-
Net loss on sale of other real estate	66	146
Net loss on sale of premises and equipment	15	62
Change in accrued interest receivable	(447)	(181)
Change in accrued interest payable	(275)	(300)
Change in other assets & other liabilities, net	2,050	2,322
Write down of other real estate owned	434	241
Net cash provided by operating activities	11,158	13,086
Cash flows from investing activities net of effect of purchase acquisition in 2011:		
Net decrease in time deposits in other banks	5,164	21,062
Proceeds from maturities and calls of securities available-for-sale	58,990	26,278
Proceeds from maturities and calls of securities held-to-maturity	900	1,456
Proceeds from sale of securities available-for-sale	3,895	-
Purchases of securities available-for-sale	(118,517)	(26,107)
Purchases of securities held-to-maturity	(43,403)	-
Purchases of other investments	(5)	(173)
Net change in loans	(46,652)	(18,067)
Purchases of premises and equipment	(2,947)	(689)
Proceeds from sale of premises and equipment	6	3
Net cash associated with Jefferson Bank acquisition	93,800	-
Proceeds from sale of other real estate	613	766
Purchase of other real estate	-	(450)
Net cash (used in) provided by investing activities	(48,156)	4,079
Cash flows from financing activities net of effect of purchase acquisition in 2011:		
Change in deposits	22,465	6,320
Change in securities sold under agreements to repurchase	11,252	6,032
Change in federal funds purchased	-	(1,700)
Issuance of Series B preferred stock	32,000	-
Redemption of Series A preferred stock	(20,000)	-
Issuance of common stock and treasury stock, net of offering expenses	-	4,769
Payment of dividends on preferred stock	(778)	(750)

Payment of dividends on common stock	(2,046)	(1,825)
Proceeds from exercise of stock options	-	17
Net cash provided by financing activities	42,893	12,863
Net increase in cash and cash equivalents	5,895	30,028
Cash and cash equivalents, beginning of period	91,907	23,351
Cash and cash equivalents, end of period	$97,802	$53,379
Supplemental information- Noncash items		
Accretion of warrants	$592	$148
Transfer of loans to other real estate	7,185	1,183
Net change in loan to ESOP	(87)	(84)

See Note 2 – Acquisition Activity for all noncash items related to the acquisition.
See notes to unaudited consolidated financial statements.

MidSouth Bancorp, Inc. and Subsidiaries
Notes to Interim Consolidated Financial Statements
September 30, 2011
(Unaudited)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements and notes thereto contain all adjustments, consisting only of normal recurring adjustments, necessary to present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of MidSouth Bancorp, Inc. (the "Company") and its subsidiaries as of September 30, 2011 and the results of their operations and their cash flows for the periods presented. The interim financial information should be read in conjunction with the annual consolidated financial statements and the notes thereto included in the Company's 2010 Annual Report on Form 10-K.

The results of operations for the nine month period ended September 30, 2011 are not necessarily indicative of the results to be expected for the entire year.

Use of Estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

Summary of Significant Accounting Policies — The accounting and reporting policies of the Company conform with accounting principles generally accepted in the United States of America and general practices within the banking industry. There have been no material changes or developments in the application of accounting principles or in our evaluation of the accounting estimates and the underlying assumptions or methodologies that we believe to be Critical Accounting Policies and Estimates as disclosed in our 2010 Annual Report on Form 10-K.

Recently Adopted Accounting Pronouncements — In December 2010, the FASB issued Accounting Standards Update No. 2010-29, Disclosure of Supplementary Pro Forma Information for Business Combinations ("ASU No. 2010-29"). ASU No. 2010-29 specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. ASU No. 2010-29 is effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The required ASU No. 2010-29 disclosures were not required in conjunction with the Bank's purchase of five former Jefferson Bank branches from the First Bank & Trust Company of Lubbock, Texas in Note 2 – Acquisition Activity due to the immateriality of assets acquired and liabilities assumed to the Company's consolidated balance sheet.

In April 2011, the FASB issued ASU No. 2011-02, A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring, which amends guidance for evaluating whether the restructuring of a receivable by a creditor is a troubled debt restructuring ("TDR"). The ASU responds to concerns that creditors are inconsistently applying existing guidance for identifying TDRs. The main provision of this Update requires a creditor to separately conclude whether the restructuring constitutes a concession and whether the debtor is experiencing financial difficulties, in order to determine if a restructuring constitutes a TDR. Guidance is also provided to assist the creditor in evaluating these two criteria. Furthermore, the amendments clarify that a creditor is precluded from using the effective interest rate test, as described in the debtors guidance on restructuring payables, when evaluating whether a restructuring constitutes a TDR. The Company adopted ASU No. 2011-02 for the interim period beginning July 1,

2011. Adoption of ASU No. 2011-02 did not have a material impact on the Company's results of operations, financial position or disclosures.

In September 2011, the FASB issued ASU 2011-08, Intangibles- Goodwill and Other (Topic 350): Testing Goodwill for Impairment. The amendments in this Update gives an entity the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. However, if an entity concludes otherwise, then it is required to perform the first step of the two-step impairment test by calculating the fair value of the reporting unit and comparing the fair value with the carrying amount of the reporting unit, as described in ASC 350-20-35-4. If the carrying amount of a reporting unit exceeds its fair value, then the entity is required to perform the second step of the goodwill impairment test to measure the amount of the impairment loss, if any, as described in ASC 350-20-35-9. Under the amendments in this Update, an entity has the option to bypass the qualitative assessment for any reporting unit in any period and proceed directly to performing the first step of the two-step goodwill impairment test. An entity may resume performing the qualitative assessment in any subsequent period. The amendments in this Update are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued. The Company has elected to adopt ASU 2011-08 effective for the year ended December 31, 2011.

Table of Contents

Recently Issued Accounting Pronouncements —In April 2011, the FASB issued ASU No. 2011-03, Transfers and Servicing (Topic 860): Reconsideration of Effective Control for Repurchase Agreements. The amendments in this Update remove from the assessment of effective control (1) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee, and (2) the collateral maintenance implementation guidance related to that criterion. Other criteria applicable to the assessment of effective control are not changed by the amendments in this Update. The guidance in this Update is effective for the first interim or annual period beginning on or after December 15, 2011. The guidance should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted. ASU No. 2011-03 is not expected to have a material impact on the Company's results of operations, financial position or disclosures.

In May 2011, the FASB issued ASU 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. The amendments in this Update result in common fair value measurement and disclosure requirements in U.S. GAAP and IFRSs. Consequently, the amendments change the wording used to describe many of the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. For many of the requirements, the Board does not intend for the amendments in this Update to result in a change in the application of the requirements in Topic 820. The Update also reflects the FASB's consideration of the different characteristics of public and non-public entities and the needs of users of their financial statements. Non-public entities will be exempt from a number of the new disclosure requirements. The amendments in this Update are to be applied prospectively. For public entities, the amendments are effective during interim and annual periods beginning after December 15, 2011. Early application by public entities is not permitted.

In June 2011, the FASB issued ASU 2011-05, Comprehensive Income (Topic 220): Presentation of Comprehensive Income. The amendments in this Update allows an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. This Update eliminates the option to present the components of other comprehensive income as part of the statement of changes in shareholders' equity. The amendments in this Update do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. The amendments in this Update should be applied retrospectively. For public entities, the amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted, because compliance with the amendments is already permitted. The amendments do not require any transition disclosures.

Reclassifications—Certain reclassifications have been made to the prior years' financial statements in order to conform to the classifications adopted for reporting in 2011. The reclassifications had no impact on shareholders' equity or net income.

Table of Contents

2. Acquisition Activity

On July 29, 2011, the Company's subsidiary, MidSouth Bank, N.A. ("the Bank"), consummated the purchase of all five former Jefferson Bank locations in the Dallas-Fort Worth, Texas area. The Bank acquired the branch network from First Bank and Trust Company, which purchased Jefferson Bank's assets in connection with the bankruptcy of Jefferson Bank's parent company. The Bank acquired at fair value approximately $57.7 million in performing loans and assumed approximately $165.8 million in Jefferson Bank deposits for a purchase price of approximately $10.6 million.

The Jefferson Bank transaction was accounted for using the acquisition method of accounting and accordingly, assets acquired, liabilities assumed and consideration exchanged were recorded at their estimated fair values on the acquisition date. Fair values are preliminary and subject to refinement for up to one year after the closing date of the acquisition as additional information relative to fair values become available. Assets acquired totaled $166.1 million, including $57.7 million in loans, $93.8 million in cash, $0.2 million of investment securities, $3.6 million of fixed assets and $10.4 million of intangibles. Liabilities assumed were $166.1 million, including $165.8 million of deposits.

Preliminary goodwill of $7.7 million is calculated as the purchase premium after adjusting for the fair value of net assets acquired and represents the value expected from the synergies created from combining the businesses as well as the economies of scale expected from combining the operations of the acquired branches with those of the Bank.

The following table provides the assets purchased and the liabilities assumed and the adjustments to fair value (in thousands):

Assets	As Recorded By Jefferson	Fair Value Adjustments	Fair Value
Cash	$93,800	$ -	$93,800
Investment securities	175	-	175
Loans receivable	59,818	(2,124)	57,694
Fixed assets	2,240	1,392	3,632
Core deposit intangible	-	2,702	2,702
Other assets	327	-	327
Total assets acquired	$156,360	$ 1,970	$158,330
Liabilities			
Deposits	$164,368	$ 1,405	$165,773
Other liabilities	283	-	283
Total liabilities assumed	164,651	1,405	166,056
Excess of liabilities assumed over assets acquired	$8,291		
Aggregate fair value adjustments		$ 565	
Goodwill			$7,726

The discount on loans receivable will be accreted to interest income over the 3 year estimated average life of the loans using the level yield method. The core deposit intangible asset is being amortized over a 10 year life on an accelerated basis. The deposit premium will be amortized over the 2.4 year average life of the related deposits as a reduction of interest expense.

The following table provides a reconciliation of goodwill:

Balance, December 31, 2010	$9,271
Addition: Jefferson Bank	7,726
Balance, September 30, 2011	$16,997

Table of Contents

The operating results of the Company for the period ended September 30, 2011 include the operating results of the acquired assets and assumed liabilities for the 63 days subsequent to the acquisition date of July 29, 2011. The operations of the former Jefferson Bank branches provided $359,000 in revenue, net of interest expense, and resulted in a $137,000 net loss before taxes after operating costs of $497,000 for the period from the acquisition date. The net loss is exclusive of interest income earned on net cash received from the acquisition and is included in the consolidated financial statements. Jefferson Bank's results of operations prior to the acquisition are not included in the Company's consolidated statement of income.

Acquisition related charges of $876,000 for the quarter and $998,000 for the nine month period ended September 30, 2011 are recorded in the consolidated statements of earnings and include incremental costs to execute the transaction and to integrate the operations of the Company and the former Jefferson Bank branches. Such expenses were primarily for professional services, data processing costs and other fees associated with the conversion of systems and integration of operations; costs related to branch and office consolidations, costs related to termination of existing contractual arrangements for various services, marketing and promotion expenses, retention and severance and incentive compensation costs, travel costs, and printing, supplies and other costs.

In many cases, determining the fair value of the acquired assets and assumed liabilities required that the Company estimate cash flows expected to result from those assets and liabilities and to discount those cash flows at appropriate rates of interest. The most significant of those determinations related to the fair valuation of acquired loans. For such loans, the excess of cash flows expected at acquisition over the estimated fair value is recognized as interest income over the remaining lives of the loans. Management determined that the acquired loans were performing and that there was no evidence of credit quality deterioration. Therefore, these loans are accounted for under ASC 310-20 and accordingly, contractual cash flows equal the expected cash flows. The loans are categorized into different loan pools per loan types. The Company determined expected cash flows on the acquired loans based on the best available information at the date of acquisition. In accordance with GAAP, there was no carry-over of Jefferson Bank's previously established allowance for loan losses.

Loans at the acquisition date of July 29, 2011 are presented in the following table (in thousands).

Residential	$6,327
Residential construction	2,190
Commercial and industrial	10,957
Commercial real estate	27,300
Land	9,950
Agriculture	312
Home equity lines of credit	183
Installment	475
	$57,694

3. Investment Securities

At September 30, 2011, the investment portfolio included approximately $33.9 million of GNMA collateralized mortgage obligations ("CMOs") backed by commercial mortgages, compared with approximately $3.1 million at December 31, 2010. As a result of the increase in this type of investment, the CMO category has been subdivided into residential and commercial as of September 30, 2011 and December 31, 2010. With the exception of three private-label CMOs with a combined balance remaining of $148,000 at September 30, 2011, all of the Company's CMOs are government-sponsored enterprise ("GSE") securities.

9

Table of Contents

The portfolio of securities consisted of the following (in thousands):

	September 30, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
U.S. Government sponsored enterprises	$81,133	$843	$-	$81,976
Obligations of state and political subdivisions	91,987	5,984	-	97,971
GSE mortgage-backed securities	75,063	4,456	-	79,519
Collateralized mortgage obligations: residential	39,209	711	5	39,915
Collateralized mortgage obligations: commercial	25,662	693	-	26,355
	$313,054	$12,687	$5	$325,736

	December 31, 2010			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
U.S. Government sponsored enterprises	$116,560	$1,138	$-	$117,698
Obligations of state and political subdivisions	105,376	3,593	117	108,852
GSE mortgage-backed securities	10,642	830	-	11,472
Collateralized mortgage obligations: residential	21,849	882	43	22,688
Collateralized mortgage obligations: commercial	3,045	54	-	3,099
	$257,472	$6,497	$160	$263,809

	September 30, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Held-to-maturity:				
Obligations of state and political subdivisions	$340	$3	$-	$343
GSE mortgage-backed securities	35,821	375	-	36,196
Collateralized mortgage obligations: commercial	7,575	-	-	7,575
	$43,736	$378	$-	$44,114

	December 31, 2010			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Held-to-maturity:				
Obligations of state and political subdivisions	$1,588	$20	$-	$1,608

Table of Contents

The amortized cost and fair value of debt securities at September 30, 2011 by contractual maturity are shown in the following table (in thousands) with the exception of mortgage-backed securities and collateralized mortgage obligations. Expected maturities may differ from contractual maturities for mortgage-backed securities and collateralized mortgage obligations because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Available-for-sale:		
Due in one year or less	$56,427	$56,892
Due after one year through five years	73,917	76,940
Due after five years through ten years	36,150	39,132
Due after ten years	6,626	6,983
Mortgage-backed securities and collateralized mortgage obligations:		
Residential	114,272	119,434
Commercial	25,662	26,355
	$313,054	$325,736

	Amortized Cost	Fair Value
Held-to-maturity:		
Due in one year or less	$140	$142
Due after one year through five years	200	201
Mortgage-backed securities and collateralized mortgage obligations:		
Residential	35,821	36,196
Commercial	7,575	7,575
	$43,736	$44,114

Details concerning investment securities with unrealized losses are as follows (in thousands):

	September 30, 2011					
	Securities with losses under 12 months		Securities with losses over 12 months		Total	
Available-for-sale:	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
Collateralized mortgage obligations: residential	$-	$-	$148	$5	$148	$5
	$-	$-	$148	$5	$148	$5

	December 31, 2010					
	Securities with losses under 12 months		Securities with losses over 12 months		Total	
Available-for-sale:	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
Obligations of state and political subdivisions	$6,919	$117	$-	$-	$6,919	$117

Collateralized mortgage obligations: residential	4,689	36	227	7	4,916	43
	$11,608	$153	$227	$7	$11,835	$160

Table of Contents

Management evaluates each quarter whether unrealized losses on securities represent impairment that is other than temporary. For debt securities, the Company considers its intent to sell the securities or if it is more likely than not the Company will be required to sell the securities. If such impairment is identified, based upon the intent to sell or the more likely than not threshold, the carrying amount of the security is reduced to fair value with a charge to earnings. Upon the result of the aforementioned review, management then reviews for potential other than temporary impairment based upon other qualitative factors. In making this evaluation, management considers changes in market rates relative to those available when the security was acquired, changes in market expectations about the timing of cash flows from securities that can be prepaid, performance of the debt security, and changes in the market's perception of the issuer's financial health and the security's credit quality. If determined that a debt security has incurred other than temporary impairment, then the amount of the credit related impairment is determined. If a credit loss is evident, the amount of the credit loss is charged to earnings and the non-credit related impairment is recognized through other comprehensive income.

The unrealized losses on debt securities at September 30, 2011 resulted from changing market interest rates over the yields available at the time the underlying securities were purchased. Two of the 22 collateralized mortgage obligations contained unrealized losses at September 30, 2011. Management identified no impairment related to credit quality. At September 30, 2011, management had the intent and ability to hold impaired securities and no impairment was evaluated as other than temporary. As a result, no other than temporary impairment losses were recognized during the three months ended September 30, 2011.

During the nine months ended September 30, 2011, the Company sold five securities classified as available-for-sale and one security classified as held-to-maturity. Of the available-for-sale securities, four securities were sold with gains totaling $94,000 and one security was sold at a loss of $4,000 for a net gain of $90,000. The securities were sold as a result of an external review performed on the municipal securities portfolio. The decision to sell the one held to maturity security, which was sold at a gain of $9,000, was based on the inability to obtain current financial information on the municipality. The sale was consistent with action taken on other securities with a similar deficiency, as identified in the external review. The Company did not sell any investment securities during the nine month period ending September 30, 2010.

Securities with an aggregate carrying value of approximately $148.0 million and $150.6 million at September 30, 2011 and December 31, 2010, respectively, were pledged to secure public funds on deposit and for other purposes required or permitted by law.

4. Other Investments

The Company is required to own stock in the Federal Reserve Bank of Atlanta ("FRB-Atlanta") and as a member of the Federal Home Loan Bank system, owns stock in the Federal Home Loan Bank of Dallas ("FHLB-Dallas"). The Company accounts for FRB-Atlanta and FHLB-Dallas stock as other investments along with stock ownership in two correspondent banks and a Community Reinvestment Act ("CRA") investment in a Senior Housing Crime Prevention program in Louisiana. The CRA investment consisted of three government-sponsored agency mortgage-backed securities purchased by the Company and held by the Senior Housing Crime Prevention program. The majority of the interest earned on the securities provides income to the program.

For impairment analysis, the Company reviews financial statements and regulatory capital ratios for each of the banks in which the Company owns stock to verify financial stability and regulatory compliance with capital requirements. As of September 30, 2011 and December 31, 2010, based upon quarterly reviews, management determined that there was no impairment in the bank stocks held as other investments.

The aggregate carrying amount of other investments consisted of the following (in thousands):

	September 30, 2011	December 31, 2010
FRB-Atlanta	$ 1,628	$ 1,624
FHLB-Dallas	586	584
Other bank stocks	713	713
CRA investment	2,130	2,141
	$ 5,057	$ 5,062

Table of Contents

5. Credit Quality of Loans and Allowance for Loan Losses

A summary of the activity in the allowance for loan losses is as follows (in thousands):

	Three Months Ended September 30, 2011	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2011	Nine Months Ended September 30, 2010
Balance, beginning of period	$7,313	$8,471	$8,813	$7,995
Provision for loan losses	650	1,500	3,150	4,150
Recoveries	48	58	256	209
Loans charged-off	(682)	(1,583)	(4,890)	(3,908)
Balance, end of period	$7,329	$8,446	$7,329	$8,446

The Company's loans individually evaluated for impairment were approximately $12.2 million at September 30, 2011 and $25.2 million at December 31, 2010. Specific reserves totaling $605,000 were established for $3.0 million of impaired loans reported at September 30, 2011. At December 31, 2010, specific reserves totaling $3.1 million were established for $11.9 million of impaired loans. Interest recognized on impaired loans totaled $357,000 at September 30, 2011. Loans classified as TDRs totaled $461,000 and $653,000 at September 30, 2011 and December 31, 2010, respectively. Four commercial loans were classified as TDRs due to a reduction in monthly payments granted to the borrowers and one small consumer loan was classified as a TDR due to a credit exception granted to the borrower. As of September 30, 2011, there have been no commitments to lend additional funds to debtors owing receivables whose terms have been modified in TDRs.

To provide greater transparency on non-performing assets, additional disclosures required by ASU 2010-20 have been included below. Allowance for loan losses is reported by portfolio segment and further detail of credit quality indicators are provided by class of loans.

Modifications by Class of Loans
(in thousands)

	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled debt restructuring as of September 30, 2011:			
Commercial, financial, and agricultural	4	$ 449	$ 449
Consumer - other	1	12	12
		$ 461	$ 461

	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled debt restructuring as of December 31, 2010:			
Commercial, financial, and agricultural	1	$ 194	$ 194
Commercial real estate - other	1	446	446
Consumer - other	1	13	13
		$ 653	$ 653

13

Table of Contents

Allowance for Loan Losses and Recorded Investment in Loans
For the Nine Months Ended September 30, 2011 (in thousands)

	Coml, Fin, and Agric	Real Estate Construction	Real Estate Commercial	Real Estate Residential	Consumer	Finance Leases Coml	Other	Total
Allowance for loan losses:								
Beginning balance	$1,664	$2,963	$ 2,565	$ 862	$ 730	$29	$-	$8,813
Charge-offs	(625)	(2,377)	(1,219)	(214)	(436)	(19)	-	(4,890)
Recoveries	128	13	1	4	110	-	-	256
Provision	870	1,029	636	222	385	8	-	3,150
Ending balance	$2,037	$1,628	$ 1,983	$ 874	$ 789	$18	$-	$7,329
Ending balance: individually evaluated for impairment	$369	$66	$ 41	$ 26	$ 103	$-	$-	$605
Loans:								
Ending balance	$212,233	$60,055	$ 262,983	$ 78,188	$ 54,779	$4,472	716	$673,426
Ending balance: individually evaluated for impairment	$4,744	$3,741	$ 2,072	$ 1,420	$ 254	$-	$-	$12,231

Allowance for Loan Losses and Recorded Investment in Loans
For the Year Ended December 31, 2010 (in thousands)

	Coml, Fin, and Agric	Real Estate Construction	Real Estate Commercial	Real Estate Residential	Consumer	Finance Leases Coml	Other	Total
Allowance for loan losses:								
Beginning balance	$2,105	$2,240	$ 1,683	$ 631	$ 1,315	$21	$-	$7,995
Charge-offs	(1,333)	(1,478)	(130)	(146)	(1,368)	(1)	-	(4,456)
Recoveries	50	1	1	60	141	1	-	254
Provision	842	2,200	1,011	317	642	8	-	5,020
Ending balance	$1,664	$2,963	$ 2,565	$ 862	$ 730	$29	$-	$8,813
Ending balance: individually evaluated for impairment	$27	$2,024	$ 827	$ 84	$ 91	$-	$-	$3,053
Loans:								
Ending balance	$177,598	$54,164	$ 208,764	$ 72,460	$ 62,272	$4,748	$806	$580,812
Ending balance: individually evaluated for	$3,549	$10,813	$ 8,780	$ 1,761	$ 275	$-	$-	$25,178

impairment

14

Table of Contents

Credit Quality Indicators by Class of Loans
As of September 30, 2011 (in thousands)

Commercial Credit Exposure
Credit Risk Profile by
Creditworthiness Category

	Commercial, Financial, and Agricultural	Commercial Real Estate Construction	Commercial Real Estate -Other	Commercial Total	% of Total Commercial
Pass	$ 202,560	$ 44,751	$ 248,757	$ 496,068	93.77 %
Special mention	1,994	3,458	6,119	11,571	2.19 %
Substandard	7,679	5,590	8,107	21,376	4.04 %
	$ 212,233	$ 53,799	$ 262,983	$ 529,015	100.00 %

Residential Credit Exposure
Credit Risk Profile by
Creditworthiness Category

	Residential - Construction	Residential - Prime	Residential - Subprime	Residential Total	% of Total Residential
Pass	$ 6,156	$ 73,213	$ -	$ 79,369	93.99 %
Special mention	-	2,237	-	2,237	2.65 %
Substandard	100	2,738	-	2,838	3.36 %
	$ 6,256	$ 78,188	$ -	$ 84,444	100.00 %

Consumer and Commercial Credit Exposure
Credit Risk Profile Based on Payment
Activity

	Consumer - Credit Card	Consumer - Other	Finance Leases Commercial	Other Loans	Consumer Total	% of Total Consumer
Performing	$4,882	$49,631	$ 4,472	$716	$59,701	99.56 %
Nonperforming	10	256	-	-	266	.44 %
	$4,892	$49,887	$ 4,472	$716	$59,967	100.00 %

15

Table of Contents

Credit Quality Indicators by Class of Loans
As of December 31, 2010 (in thousands)

Commercial Credit Exposure
Credit Risk Profile by Creditworthiness Category

	Commercial, Financial, and Agricultural	Commercial Real Estate Construction	Commercial Real Estate -Other	Commercial Total	% of Total Commercial
Pass	$ 165,581	$ 32,061	$ 191,089	$ 388,731	89.50 %
Special Mention	3,661	3,851	3,726	11,238	2.59 %
Substandard	8,356	12,077	13,949	34,382	7.91 %
	$ 177,598	$ 47,989	$ 208,764	$ 434,351	100.00 %

Residential Credit Exposure
Credit Risk Profile by Creditworthiness Category

	Residential - Construction	Residential - Prime	Residential - Subprime	Residential Total	% of Total Residential
Pass	$ 5,959	$ 66,867	$ -	$ 72,826	92.61 %
Special mention	-	2,501	-	2,501	3.18 %
Substandard	216	3,092	-	3,308	4.21 %
	$ 6,175	$ 72,460	$ -	$ 78,635	100.00 %

Consumer and Commercial Credit Exposure
Credit Risk Profile Based on Payment Activity

	Consumer - Credit Card	Consumer - Other	Finance Leases Commercial	Other Loans	Consumer Total	% of Total Consumer
Performing	$ 5,318	$ 56,905	$ 4,748	$ 806	$ 67,777	99.93 %
Nonperforming	-	49	-	-	49	0.07 %
	$ 5,318	$ 56,954	$ 4,748	$ 806	$ 67,826	100.00 %

Table of Contents

Age Analysis of Past Due Loans by Class of Loans
(in thousands)

As of September 30, 2011	30-59 Days Past Due (1)	60-89 Days Past Due (1)	Greater than 90 Days Past Due (1)	Total Past Due	Current	Total Loans	Recorded Investment > 90 days and Accruing
Commercial, financial, and agricultural	$419	$115	$3,091	$3,625	$208,608	$212,233	$47
Commercial real estate – construction	431	129	419	979	59,076	60,055	-
Commercial real estate - other	1,113	265	1,143	2,521	260,462	262,983	-
Consumer - credit card	60	17	10	87	4,805	4,892	10
Consumer - other	393	126	236	755	49,132	49,887	14
Residential - construction	-	-	-	-	-	-	-
Residential - prime	741	122	478	1,341	76,847	78,188	16
Residential - subprime	-	-	-	-	-	-	-
Other loans	84	-	-	84	632	716	-
Finance leases commercial	-	-	-	-	4,472	4,472	-
	$3,241	$774	$5,377	$9,392	$664,034	$673,426	$87

As of December 31, 2010	30-59 Days Past Due (1)	60-89 Days Past Due (1)	Greater than 90 Days Past Due (1)	Total Past Due	Current	Total Loans	Recorded Investment > 90 days and Accruing
Commercial, financial, and agricultural	$1,298	$114	$2,405	$3,817	$173,781	$177,598	$17
Commercial real estate - construction	3,334	-	3,324	6,658	41,331	47,989	-
Commercial real estate - other	642	6,579	1,234	8,455	200,309	208,764	-
	50	23	-	73	5,245	5,318	-

Consumer - credit card							
Consumer - other	407	79	280	766	56,188	56,954	49
Residential - construction	-	-	-	-	6,175	6,175	-
Residential - prime	1,023	22	1,155	2,200	70,260	72,460	-
Residential - subprime	-	-	-	-	-	-	-
Other loans	102	3	-	105	701	806	-
Finance leases commercial	-	-	-	-	4,748	4,748	-
	$6,856	$6,820	$8,398	$22,074	$558,738	$580,812	$66

(1) Past due amounts may include loans on nonaccrual status.

Table of Contents

Impaired Loans
(in thousands)

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
As of September 30, 2011					
With no related allowance recorded:					
Commercial, financial, and agricultural	$2,924	$3,042	$-	$2,187	$68
Commercial real estate – construction	3,419	3,419	-	4,131	155
Commercial real estate – other	1,744	1,744	-	1,894	38
Consumer – other	28	39	-	39	-
Residential – prime	1,113	1,113	-	1,244	32
Finance leases	-	-	-	9	-
Other	-	-	-	8	-
Subtotal:	$9,228	$9,357	$-	$9,512	$293
With an allowance recorded:					
Commercial	1,820	1,820	370	1,706	49
Commercial real estate – construction	322	322	66	1,500	9
Commercial real estate – other	328	328	41	254	-
Consumer – other	225	229	102	211	6
Residential – prime	308	308	26	274	-
Subtotal:	$3,003	$3,007	$605	$3,945	$64
Totals:					
Commercial	10,557	10,675	477	11,689	319
Consumer	253	268	102	250	6
Residential	1,421	1,421	26	1,518	32
Grand total:	$12,231	$12,364	$605	$13,457	$357

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
As of December 31, 2010					
With no related allowance recorded:					
Commercial, financial, and agricultural	$3,291	$3,538	$-	$4,036	$85
Commercial real estate – construction	5,918	9,175	-	5,584	179
Commercial real estate – other	2,407	2,487	-	1,941	114
Consumer – other	90	90	-	80	8
Residential – prime	1,549	1,549	-	1,166	77
Subtotal:	$13,255	$16,839	$-	$12,807	$463
With an allowance recorded:					
Commercial	258	258	27	1,671	6
Commercial real estate – construction	4,895	4,895	2,024	4,098	140
Commercial real estate – other	6,373	6,373	827	6,632	2
Consumer – other	185	185	91	262	3
Residential – prime	212	212	84	320	12
Subtotal:	$11,923	$11,923	$3,053	$12,983	$163
Totals:					
Commercial	23,142	26,726	2,878	23,962	526

Consumer	275	275	91	342	11
Residential	1,761	1,761	84	1,486	89
Grand total:	$25,178	$28,762	$3,053	$25,790	$ 626

Table of Contents

Loans on Nonaccrual Status
(in thousands)

	September 30, 2011	December 31, 2010
Commercial, financial, and agricultural	$ 4,295	$ 2,589
Commercial real estate - construction	988	8,220
Commercial real estate - other	1,566	7,378
Consumer - credit card	-	-
Consumer - other	242	261
Residential - construction	-	-
Residential - prime	848	1,155
Residential - subprime	-	-
Other loans	-	-
Finance leases commercial	-	-
	$ 7,939	$ 19,603

6. Stockholders' Equity

In August 2011, the Company repaid $20.0 million in Series A Preferred Stock issued to the Treasury under the Capital Purchase Plan ("CPP") with funds from the U.S. Treasury's Small Business Lending Fund ("SBLF") authorized by Congress under the Small Business Jobs Act of 2010. Repayment of the 20,000 shares of Series A Preferred Stock under the CPP resulted in accelerated accretion of discount on the preferred stock of approximately $444,000 in the third quarter of 2011. As a result of the repurchase of the Series A Preferred Stock, all of the TARP limitations affecting the Company were removed. In connection with the SBLF, the Company issued $32.0 million in Series B Preferred Stock to the Treasury. The dividend rate on the Series B Preferred Stock will be between 1% and 5% based on the level of qualified small business loans through the end of the ninth dividend period ending September 30, 2013. Beginning with the tenth dividend period and under certain conditions, the dividend rate could be as high as 9%.

7. Earnings Per Common Share

Following is a summary of the information used in the computation of earnings per common share (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Net earnings available to common shareholders	$296	$939	$1,792	$3,026
Weighted average number of common shares outstanding used in computation of basic earnings per common share	9,726	9,709	9,723	9,697
Effect of dilutive securities:				
Stock options	11	16	13	18
Restricted stock	3	-	4	-
Weighted average number of common shares outstanding plus effect of dilutive securities – used in computation of diluted earnings per share	9,740	9,725	9,740	9,715

Options to acquire 18,331 and 23,335 shares of common stock were not included in computing diluted earnings per share for the quarter and nine months ended September 30, 2011 and 2010, respectively, because the effect of these shares was anti-dilutive. For the quarter and nine months ended September 30, 2010, 21,366 shares of restricted stock were not included in computed diluted earnings because the effect of these shares was anti-dilutive. As a result of the completion of a qualified equity offering in December 2009, warrants issued to the U. S. Department of the Treasury (the "Treasury") to purchase 208,768 shares of our common stock were reduced to 104,384 shares. The remaining 104,384 shares subject to the warrants were anti-dilutive and not included in the computation of diluted earnings per share for the quarter and nine months ended September 30, 2011.

Table of Contents

8. Declaration of Dividends

A first quarter dividend of $0.07 per share for holders of common stock of record on March 17, 2011 was declared on January 25, 2011 and was paid on April 1, 2011. On April 26, 2011, the Company declared a second quarter dividend of $0.07 per share for holders of common stock of record on June 16, 2011, and was paid on July 1, 2011. A third quarter dividend was declared on July 27, 2011 in the amount of $0.07 per share for holders of common stock of record on September 16, 2011 and paid on October 1, 2011. On October 25, 2011, the Company declared a fourth quarter dividend of $0.07 per share for holders of common stock of record December 15, 2011 to be paid on January 3, 2012.

9. Fair Value Measurement

The Company groups assets and liabilities 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. These levels are:

Level 1 – Valuation is based upon quoted prices for identical instruments traded in active markets.

Level 2 – Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 – Level 3 – Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques

Following is a description of valuation methodologies used for assets and liabilities which are either recorded or disclosed at fair value.

Cash and Cash Equivalents—The carrying value of cash and cash equivalents is a reasonable estimate of fair value.

Time Deposits Held in Banks—Fair values for fixed-rate time deposits are estimated using a discounted cash flow analysis that applies interest rates currently being offered on time deposits of similar terms of maturity.

Securities Available-for-Sale—Securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security’s credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange and U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter market funds. Securities are classified as Level 2 within the valuation hierarchy when the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the bond’s terms and conditions, among other things. Level 2 inputs are used to value U.S. Agency securities, mortgage-backed securities, municipal securities, single issue trust preferred securities, certain pooled trust preferred securities, and certain equity securities that are not actively traded.

Other Investments—The carrying value of other investments is a reasonable estimate of fair value.

Loans—For disclosure purposes, the fair value of fixed rate loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings. For variable rate loans, the carrying amount is a reasonable estimate of fair value. The Company does not record loans at fair value on a recurring basis. No adjustment to fair value is taken related to illiquidity discounts. However, from time to time, a loan is considered impaired and an allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management uses one of three methods to measure impairment, which, include collateral value, market value of similar debt, and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. Impaired loans where an allowance is established based on the fair value of collateral or where the loan balance has been charged down to fair value require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and adjusts the appraisal value by taking an additional discount for market conditions and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3.

Table of Contents

For non-performing loans, collateral valuations currently in file are reviewed for acceptability in terms of timeliness and applicability. Although each determination is made based on the facts and circumstances of each credit, generally valuations are no longer considered acceptable when there has been physical deterioration of the property from when it was last appraised, or there has been a significant change in the underlying assumptions of the appraisal. If the valuation is deemed to be unacceptable, a new appraisal is ordered. New appraisals are typically received within 4-6 weeks. While awaiting new appraisals, the valuation in the file is utilized, net of discounts. Discounts are derived from available relevant market data, selling costs, taxes, and insurance. Any perceived collateral deficiency utilizing the discounted value is specifically reserved (as required by ASC Topic 310) until the new appraisal is received or charged off. Thus, provisions or charge-offs are recognized in the period the credit is identified as non-performing.

The following sources are utilized to set appropriate discounts: market real estate agents, current local sales data, bank history for devaluation of similar property, Sheriff's valuations and buy/sell contracts. If a real estate agent is used to market and sell the property, values are discounted 10% for selling costs. Additional discounts may be applied if research from the above sources indicates a discount is appropriate given devaluation of similar property from the time of the initial valuation.

Other Real Estate—Other real estate properties are adjusted to fair value upon transfer of the loans to other real estate, and annually thereafter to insure other real estate assets are carried at the lower of carrying value or fair value. Exceptions to obtaining initial appraisals are properties where a buy/sell agreement exists for the loan value or greater, or where we have received a Sheriff's valuation for properties liquidated through a Sheriff sale. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the other real estate as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and adjusts the appraisal value by taking an additional discount for market conditions and there is no observable market prices, the Company records the other real estate asset as nonrecurring Level 3.

Cash Surrender Value of Life Insurance Policies—Fair value for life insurance cash surrender value is based on cash surrender values indicated by the insurance companies.

Deposits—The fair value of demand deposits, savings accounts, NOW accounts, and money market deposits is the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated by discounting the future cash flows using the rates currently offered for deposits of similar remaining maturities. The estimated fair value does not include customer related intangibles.

Securities Sold Under Agreements to Repurchase—The fair value approximates the carrying value of securities sold under agreements to repurchase due to their short-term nature.

Junior Subordinated Debentures—For junior subordinated debentures that bear interest on a floating basis, the carrying amount approximates fair value. For junior subordinated debentures that bear interest on a fixed rate basis, the fair value is estimated using a discounted cash flow analysis that applies interest rates currently being offered on similar types of borrowings.

Commitments to Extend Credit, Standby Letters of Credit and Credit Card Guarantees—Because commitments to extend credit and standby letters of credit are generally short-term and made using variable rates, the carrying value and estimated fair value associated with these instruments are immaterial.

Table of Contents

Assets Recorded at Fair Value

Below is a table that presents information about certain assets and liabilities measured at fair value on a recurring basis (in thousands):

Description	Assets / Liabilities Measured at Fair Value at September 30, 2011	Fair Value Measurements at September 30, 2011 using: Level 1	Level 2	Level 3
Available-for-sale securities:				
U.S. Government sponsored enterprises	$ 81,976	$-	$81,976	$-
Obligations of state and political subdivisions	97,971	-	97,971	-
GSE mortgage-backed securities	79,519	-	79,519	-
Collateralized mortgage obligations: residential	39,915	-	39,915	-
Collateralized mortgage obligations: commercial	26,355	-	26,355	-
	$ 325,736	$-	$325,736	$-

Description	Assets / Liabilities Measured at Fair Value at December 31, 2010	Fair Value Measurements at December 31, 2010 using: Level 1	Level 2	Level 3
Available-for-sale securities:				
U.S. Government sponsored enterprises	$ 117,698	$-	$117,698	$-
Obligations of state and political subdivisions	108,852	-	108,852	-
GSE mortgage-backed securities	11,472	-	11,472	-
Collateralized mortgage obligations: residential	22,688	-	22,688	