NEW PEOPLES BANKSHARES INC
Form 10-Q
November 13, 2012
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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, 2012

¨ **Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from to

Commission file number: 000-33411

NEW PEOPLES BANKSHARES, INC.

(Exact name of registrant as specified in its charter)

Virginia	**31-1804543**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
67 Commerce Drive	
Honaker, Virginia	**24260**
(Address of principal executive offices)	**(Zip Code)**

(Registrant s telephone number, including area code) (276) 873-7000

n/a

(Former name, former address and former fiscal year, if changed 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 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 (§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 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	x

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

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

Class	**Outstanding at November 9, 2012**
Common Stock, $2.00 par value	13,824,697

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Part I Financial Information
Item 1 Financial Statements

NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

(IN THOUSANDS EXCEPT SHARE AND PER SHARE DATA)

(UNAUDITED)

	2012	2011
INTEREST AND DIVIDEND INCOME		
Loans including fees	$ 24,784	$ 31,357
Federal funds sold	2	9
Interest-earning deposits with banks	131	128
Investments	653	149
Dividends on equity securities (restricted)	83	74
Total Interest and Dividend Income	25,653	31,717
INTEREST EXPENSE		
Deposits		
Demand	81	126
Savings	177	399
Time deposits below $100,000	2,364	3,762
Time deposits above $100,000	1,589	2,295
FHLB Advances	403	669
Other borrowings	128	150
Trust Preferred Securities	370	315
Total Interest Expense	5,112	7,716
NET INTEREST INCOME	20,541	24,001
PROVISION FOR LOAN LOSSES	4,093	6,258
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	16,448	17,743
NONINTEREST INCOME		
Service charges	1,834	1,816
Fees, commissions and other income	1,742	1,515
Insurance and investment fees	260	325
Net realized gains on sale of investment securities	385	
Life insurance investment income	235	253
Total Noninterest Income	4,456	3,909
NONINTEREST EXPENSES		
Salaries and employee benefits	10,496	11,723

Occupancy and equipment expense	3,231	3,276
Advertising and public relations	325	304
Data processing and telecommunications	1,323	1,218
FDIC insurance premiums	1,244	1,571
Other real estate owned and repossessed vehicles, net	4,387	4,476
Other operating expenses	4,071	3,775
Total Noninterest Expenses	25,077	26,343
LOSS BEFORE INCOME TAXES	(4,173)	(4,691)
INCOME TAX EXPENSE (BENEFIT)	2,363	(1,733)
NET LOSS	$ (6,536)	$ (2,958)
Loss Per Share		
Basic	$ (0.64)	$ (0.30)
Fully Diluted	$ (0.64)	$ (0.30)
Average Weighted Shares of Common Stock		
Basic	10,177,237	10,010,178
Fully Diluted	10,177,237	10,010,178

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

(IN THOUSANDS EXCEPT SHARE AND PER SHARE DATA)

(UNAUDITED)

	2012	2011
INTEREST AND DIVIDEND INCOME		
Loans including fees	$ 7,989	$ 9,955
Federal funds sold	1	
Interest-earning deposits with banks	36	48
Investments	212	65
Dividends on equity securities (restricted)	28	24
Total Interest and Dividend Income	8,266	10,092
INTEREST EXPENSE		
Deposits		
Demand	27	37
Savings	57	75
Time deposits below $100,000	707	1,132
Time deposits above $100,000	477	721
FHLB Advances	72	225
Other borrowings	40	45
Trust Preferred Securities	123	115
Total Interest Expense	1,503	2,350
NET INTEREST INCOME	6,763	7,742
PROVISION FOR LOAN LOSSES	967	2,801
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	5,796	4,941
NONINTEREST INCOME		
Service charges	635	657
Fees, commissions and other income	554	496
Insurance and investment fees	28	134
Net realized gains on sale of investment securities	48	
Life insurance investment income	90	77
Total Noninterest Income	1,355	1,364
NONINTEREST EXPENSES		
Salaries and employee benefits	3,389	3,864
Occupancy and equipment expense	1,047	1,132
Advertising and public relations	114	121

Data processing and telecommunications	434	420
FDIC insurance premiums	399	475
Other real estate owned and repossessed vehicles, net	1,140	1,986
Other operating expenses	1,315	1,115
Total Noninterest Expenses	7,838	9,113
LOSS BEFORE INCOME TAXES	(687)	(2,808)
INCOME TAX EXPENSE (BENEFIT)	776	(976)
NET LOSS	$ (1,463)	$ (1,832)
Loss Per Share		
Basic	$ (0.14)	$ (0.18)
Fully Diluted	$ (0.14)	$ (0.18)
Average Weighted Shares of Common Stock		
Basic	10,507,724	10,010,178
Fully Diluted	10,507,724	10,010,178

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

(IN THOUSANDS)

(UNAUDITED)

	For the three months ended September 30,		For the nine months ended September 30,	
	2012	**2011**	**2012**	**2011**
Net Loss	$ (1,463)	$ (1,832)	$ (6,536)	$ (2,958)
Other comprehensive income (loss):				
Investment Securities Activity				
Unrealized gains arising during the period	261	58	475	184
Tax related to unrealized gains	(89)	(20)	(162)	(63)
Reclassification of realized gains during the period	(48)		(385)	
Tax related to realized gains	17		131	
Total other comprehensive income	141	38	59	121
Total comprehensive loss	$ (1,322)	$ (1,794)	$ (6,477)	$ (2,837)

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED BALANCE SHEETS

(IN THOUSANDS EXCEPT PER SHARE AND SHARE DATA)

	September 30, 2012 (Unaudited)	December 31, 2011 (Audited)
ASSETS		
Cash and due from banks	$ 16,976	$ 18,306
Interest-bearing deposits with banks	50,679	72,170
Federal funds sold	2	77
Total Cash and Cash Equivalents	67,657	90,553
Investment securities		
Available-for-sale	48,559	32,434
Loans receivable	538,992	597,816
Allowance for loan losses	(17,588)	(18,380)
Net Loans	521,404	579,436
Bank premises and equipment, net	32,290	33,141
Equity securities (restricted)	2,818	3,573
Other real estate owned	11,368	15,092
Accrued interest receivable	2,516	3,067
Life insurance investments	11,890	11,351
Goodwill and other intangibles	67	123
Deferred taxes	4,789	7,220
Other assets	4,859	4,394
Total Assets	$ 708,217	$ 780,384
LIABILITIES		
Deposits:		
Demand deposits:		
Noninterest bearing	$ 109,057	$ 109,629
Interest-bearing	61,261	58,459
Savings deposits	95,359	94,569
Time deposits	387,540	445,658
Total Deposits	653,217	708,315
Federal Home Loan Bank advances	6,858	17,983
Accrued interest payable	1,793	1,796
Accrued expenses and other liabilities	1,735	1,471
Other borrowings		5,450
Trust preferred securities	16,496	16,496
Total Liabilities	680,099	751,511

Commitments and contingencies				
STOCKHOLDERS EQUITY				
Common stock - $2.00 par value; 50,000,000 shares authorized; 13,824,697 and 10,010,178 shares issued and outstanding at September 30, 2012 and December 31, 2011, respectively		27,649		20,020
Common stock warrants		663		
Additional paid-in-capital		19,119		21,689
Retained earnings (deficit)		(19,621)		(13,085)
Accumulated other comprehensive income		308		249
Total Stockholders Equity		28,118		28,873
Total Liabilities and Stockholders Equity	$	708,217	$	780,384

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

(IN THOUSANDS INCLUDING SHARE DATA)

(UNAUDITED)

	Shares of Common Stock	Common Stock	Common Stock Warrants	Additional Paid in Capital	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income (Loss)	Total Shareholders Equity
Balance, December 31, 2010	10,010	$ 20,020	$	$ 21,689	$ (4,175)	$ (11)	$ 37,523
Net loss					(2,958)		(2,958)
Unrealized gain on available-for-sale securities, net of $63 tax						121	121
Balance, September 30, 2011	10,010	$ 20,020	$	$ 21,689	$ (7,133)	$ 110	$ 34,686
Balance, December 31, 2011	10,010	$ 20,020	$	21,689	$ (13,085)	$ 249	$ 28,873
Net loss					(6,536)		(6,536)
Conversion of Director Notes plus accrued interest	3,815	7,629	663	(2,570)			5,722
Realized gains on available-for-sale securities, net of $131 tax						(254)	(254)
Unrealized gain on available-for-sale securities, net of $162 tax						313	313
Balance, September 30, 2012	13,825	$ 27,649	$ 663	19,119	$ (19,621)	$ 308	$ 28,118

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

(IN THOUSANDS)

(UNAUDITED)

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$ (6,536)	$ (2,958)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation	1,899	1,903
Provision for loan losses	4,093	6,258
Income (less expenses) on life insurance	(539)	(253)
Gain on sale of securities available-for-sale	(385)	
(Gain) loss on sale of fixed assets	(5)	146
Loss (gain) on sale of foreclosed real estate	383	(17)
Adjustment of carrying value of foreclosed real estate	2,983	3,508
Accretion of bond premiums/discounts	397	16
Deferred tax expense	2,401	(305)
Amortization of core deposit intangible	56	79
Net change in:		
Interest receivable	551	532
Other assets	(465)	(2,080)
Accrued interest payable	269	176
Accrued expenses and other liabilities	264	80
Net Cash Provided by Operating Activities	5,366	7,085
CASH FLOWS FROM INVESTING ACTIVITIES		
Net decrease in loans	47,066	58,201
Purchase of securities available-for-sale	(33,203)	(16,765)
Proceeds from sale and maturities of securities available-for-sale	17,155	3,925
Sale of Federal Home Loan Bank stock	755	221
Payments for the purchase of premises and equipment	(1,065)	(1,593)
Proceeds from sales of premises and equipment	22	185
Proceeds from sales of other real estate owned	7,231	4,182
Net Cash Provided by Investing Activities	37,961	48,356
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayment of line of credit borrowings		(4,900)
Net increase in other borrowings		5,200
Repayments to Federal Home Loan Bank	(11,125)	(5,900)
Net change in:		
Demand deposits	2,230	17,849
Savings deposits	790	(10,617)
Time deposits	(58,118)	(41,323)
Net Cash Used in Financing Activities	(66,223)	(39,691)

Net (decrease) increase in cash and cash equivalents	(22,896)	15,750
Cash and Cash Equivalents, Beginning of Period	90,553	82,529
Cash and Cash Equivalents, End of Period	$ 67,657	$ 98,279
Supplemental Disclosure of Cash Paid During the Period for:		
Interest	$ 5,115	$ 7,892
Taxes	$	$
Supplemental Disclosure of Non Cash Transactions:		
Other real estate acquired in settlement of foreclosed loans	$ 6,873	$ 6,108
Conversion of Director Notes in other borrowings to common stock	$ (5,450)	$
Conversion of accrued interest payable on Director Notes to common stock	$ (272)	$
Common stock issued as a result of the conversion of Director Notes	$ 5,722	$

The accompanying notes are an integral part of this statement.

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NEW PEOPLES BANKSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 NATURE OF OPERATIONS:

New Peoples Bankshares, Inc. (The Company) is a bank holding company whose principal activity is the ownership and management of a community bank. New Peoples Bank, Inc. (Bank) was organized and incorporated under the laws of the Commonwealth of Virginia on December 9, 1997. The Bank commenced operations on October 28, 1998, after receiving regulatory approval. As a state chartered member bank, the Bank is subject to regulation by the Virginia Bureau of Financial Institutions, the Federal Deposit Insurance Corporation and the Federal Reserve Bank. The Bank provides general banking services to individuals, small and medium size businesses and the professional community of southwestern Virginia, southern West Virginia, and eastern Tennessee. On June 9, 2003, the Company formed two wholly owned subsidiaries, NPB Financial Services, Inc. and NPB Web Services, Inc. On July 7, 2004 the Company established NPB Capital Trust I for the purpose of issuing trust preferred securities. On September 27, 2006, the Company established NPB Capital Trust 2 for the purpose of issuing additional trust preferred securities. NPB Financial Services, Inc. was a subsidiary of the Company until January 1, 2009 when it became a subsidiary of the Bank. In June 2012 the name of NPB Financial Services, Inc. was changed to NPB Insurance Services, Inc.

NOTE 2 ACCOUNTING PRINCIPLES:

The financial statements conform to U. S. generally accepted accounting principles and to general industry practices. In the opinion of management, the accompanying unaudited financial statements contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly the financial position at September 30, 2012, and the results of operations for the three month and nine month periods ended September 30, 2012 and 2011. The notes included herein should be read in conjunction with the notes to financial statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2011. The results of operations for the three month and nine month periods ended September 30, 2012 and 2011 are not necessarily indicative of the results to be expected for the full year.

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

NOTE 3 FORMAL WRITTEN AGREEMENT:

Effective July 29, 2010, the Company and the Bank entered into a written agreement with the Federal Reserve Bank of Richmond (Reserve Bank) and the Virginia State Corporation Commission Bureau of Financial Institutions (the Bureau) called (the Written Agreement). At September 30, 2012, we believe we have not yet achieved full compliance with the Written Agreement but we have made progress in our compliance efforts under the Written Agreement and all of the written plans required to date, as discussed in the following paragraphs, have been submitted on a timely basis.

Under the terms of the Written Agreement, the Bank has agreed to develop and submit for approval within specified time periods written plans to: (a) strengthen board oversight of management and the Bank s operation; (b) if appropriate after review, to strengthen the Bank s management and board governance; (c) strengthen credit risk management policies; (d) enhance lending and credit administration; (e) enhance the Bank s management of commercial real estate concentrations; (f) conduct ongoing review and grading of the Bank s loan portfolio; (g) improve the Bank s position with respect to loans, relationships, or other assets in excess of $1 million which are now or in the future become past due more than 90 days, which are on the Bank s problem loan list, or which are adversely classified in any report of examination of the Bank; (h) review and revise, as appropriate, current policy and maintain sound processes for maintaining an adequate allowance for loan and lease losses; (i) enhance management of the Bank s liquidity position and funds management practices; (j) revise its contingency funding plan; (k) revise its strategic plan; and (l) enhance the Bank s anti-money laundering and related activities.

In addition, the Bank has agreed that it will: (a) not extend, renew, or restructure any credit that has been criticized by the Reserve Bank or the Bureau absent prior board of directors approval in accordance with the restrictions in the Written Agreement; (b) eliminate all assets or portions of assets classified as loss and thereafter charge off all assets classified as loss in a federal or state report of examination, unless otherwise approved by the Reserve Bank.

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Under the terms of the Written Agreement, both the Company and the Bank have agreed to submit capital plans to maintain sufficient capital at the Company, on a consolidated basis, and the Bank, on a stand-alone basis, and to refrain from declaring or paying dividends without prior regulatory approval. The Company has agreed that it will not take any other form of payment representing a reduction in the Bank s capital or make any distributions of interest, principal, or other sums on subordinated debentures or trust preferred securities without prior regulatory approval. The Company may not incur, increase or guarantee any debt without prior regulatory approval and has agreed not to purchase or redeem any shares of its stock without prior regulatory approval.

Under the terms of the Written Agreement, the Company and the Bank have appointed a committee to monitor compliance with the Written Agreement. The directors of the Company and the Bank have recognized and unanimously agree with the common goal of financial soundness represented by the Written Agreement and have confirmed the intent of the directors and executive management to diligently seek to comply with all requirements of the Written Agreement.

NOTE 4 CAPITAL:

Capital Requirements and Ratios

The Company and the Bank are subject to various capital requirements administered by federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and, possibly, additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company s and the Bank s financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier 1 capital (as defined) to risk-weighted assets (as defined) and of Tier 1 capital (as defined) to average assets (as defined). Management believes that, as of September 30, 2012, the Company and the Bank meet all capital adequacy requirements to which they are subject.

As of September 30, 2012 the Bank was well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following tables. There are no conditions or events since the notification that management believes have changed the Company s and Bank s category.

The Company s and the Bank s actual capital amounts and ratios are presented in the table as of September 30, 2012 and December 31, 2011, respectively.

	Actual		Minimum Capital Requirement		Minimum to Be Well Capitalized Under Prompt Corrective Action Provisions	
(Dollars are in thousands)	Amount	Ratio	Amount	Ratio	Amount	Ratio
September 30, 2012:						
Total Capital to Risk Weighted Assets						
The Company	$ 46,159	10.36%	35,650	8%	$ N/A	N/A
The Bank	48,007	10.75%	35,713	8%	44,641	10%
Tier 1 Capital Risk Weighted Assets:						
The Company	33,688	7.56%	17,825	4%	N/A	N/A
The Bank	42,279	9.47%	17,857	4%	26,785	6%
Tier 1 Capital to Average Assets:						
The Company	33,688	4.74%	28,454	4%	N/A	N/A
The Bank	42,279	5.94%	28,485	4%	35,607	5%
December 31, 2011:						
Total Capital to Risk Weighted Assets						
The Company	$ 45,856	9.15%	40,104	8%	$ N/A	N/A
The Bank	53,070	10.56%	40,189	8%	50,236	10%

Tier 1 Capital Risk Weighted Assets:						
The Company	32,941	6.57%	20,052	4%	N/A	N/A
The Bank	46,641	9.28%	20,095	4%	30,142	6%
Tier 1 Capital to Average Assets:						
The Company	33,461	4.23%	31,658	4%	N/A	N/A
The Bank	46,641	5.99%	31,160	4%	38,950	5%

Conversion of Notes to Common Stock and Warrants

In December, 2010, the Company borrowed $250,000 from Director Scott White for one year. The note bore interest at the variable rate of interest equal to the Wall Street Journal prime rate payable at maturity or conversion, was unsecured and was convertible into the Company s common stock under certain conditions. In January, 2011, the Company received an additional $250,000 loan from Director Lynn Keene on identical terms. The purpose of these borrowings was to provide cash for operating expenses of the Company. On March 16, 2011 Directors Keene and White loaned the Company an additional $4.95 million which, after receiving regulatory approval, the Company used to retire its indebtedness to the FDIC as receiver for Silverton Bank. The loans had a stated maturity of December 31, 2011 with the same terms as the previous notes. In each case, the Company was obligated to convert the debt into the Company s common stock if, before the stated maturity, the Company conducted an offering of its common stock at the price per share at which it was offered. If the Company did not conduct an offering prior to the stated maturity, the Company had the option, but not the obligation, to convert the debt into shares of its common stock within 30 days of the stated maturity at a price per share to be established by the Company s Board of Directors. On December 21, 2011, with regulatory approval the Company consolidated the earlier loans into a loan in the principal amount of $2.8 million from Director White and $2.65 million from Director Keene on the same terms as the previous loans except that the maturity date of the borrowings was extended to June 30, 2012. Prior to their maturity, the maturity of the loans was extended to December 31, 2012 on the same terms. The Company believes this indebtedness was on more favorable terms to the Company than could be obtained from unrelated parties.

On September 19, 2012, in conjunction with the public offering of its common stock, the Company converted both notes to common stock and Mr. White received 1,959,889 shares and Mr. Keene received 1,854,630 shares. Each director also obtained warrants that are immediately exercisable to purchase common stock over the next five years at a price of $1.75 per share. Mr. White received 391,977 warrants and Mr. Keene received 370,926 warrants. These conversions were made on the same terms as the public offering as required by the notes. These transactions resulted in Director Keene beneficially owning 16.04% and Director White beneficially owning 19.28% of the Company s common stock.

As a result of this noncash transaction, the Company recorded a $5.7 million increase to stockholders equity and reduced other borrowings by $5.45 million and accrued interest payable by $272 thousand. The $5.7 million increase to stockholders equity was allocated by an increase of $7.6 million to common stock, $663 thousand allocated to the commons stock warrants, and a decrease of $2.6 million to additional paid in capital. The value of the common stock warrants was calculated using the Black-Scholes Option Pricing Model.

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NOTE 5 INVESTMENT SECURITIES:

The amortized cost and estimated fair value of securities (all available-for-sale) are as follows:

(Dollars are in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Value
September 30, 2012				
U.S. Government Agencies	$ 25,602	$ 258	$ 21	$ 25,839
Taxable municipals	853	2	5	850
Tax-exempt municipals				
Mortgage backed securities	21,638	233	1	21,870
Total Securities AFS	$ 48,093	$ 493	$ 27	$ 48,559
December 31, 2011				
U.S. Government Agencies	$ 21,405	$ 238	$ 10	$ 21,633
Taxable municipals	1,465	89	2	1,552
Tax-exempt municipals	1,043	11		1,054
Mortgage backed securities	8,144	67	16	8,195
Total Securities AFS	$ 32,057	$ 405	$ 28	$ 32,434

The following table details unrealized losses and related fair values in the available-for-sale portfolio. This information is aggregated by the length of time that individual securities have been in a continuous unrealized loss position as of September 30, 2012 and December 31, 2011.

	Less than 12 Months		12 Months or More		Total	
(Dollars are in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
September 30, 2012						
U.S. Government Agencies	$ 2,911	$ 21	$	$	$ 2,911	$ 21
Taxable municipals	280	5			280	5
Mtg. backed securities	743	1			743	1
Total Securities AFS	$ 3,934	$ 27	$	$	$ 3,934	$ 27
December 31, 2011						
U.S. Government Agencies	$ 5,592	$ 10	$	$	$ 5,592	$ 10
Taxable municipals	572	2			572	2
Mtg. backed securities	4,055	16			4,055	16
Total Securities AFS	$ 10,219	$ 28	$	$	$ 10,219	$ 28

At September 30, 2012, the available-for-sale portfolio included five investments for which the fair market value was less than amortized cost. At December 31, 2011, the available-for-sale portfolio included eleven investments for which the fair market value was less than amortized cost. Management evaluates securities for other than temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial conditions and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. No securities had an other than temporary impairment.

The amortized cost and fair value of investment securities at September 30, 2012, by contractual maturity, are shown in the following schedule. 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.

(Dollars are in thousands) Securities Available for Sale	Amortized Cost	Fair Value	Weighted Average Yield
Due in one year or less	$	$	%
Due after one year through five years	1,503	1,510	1.01%
Due after five years through fifteen years	12,274	12,403	1.73%
Due after fifteen years	34,316	34,646	2.15%
Total	$ 48,093	$ 48,559	2.01%

Investment securities with a carrying value of $18.9 million and $15.7 million at September 30, 2012 and December 31, 2011, were pledged to secure public deposits, overnight payment processing and for other purposes required by law.

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The Bank, as a member of the Federal Reserve Bank and the Federal Home Loan Bank, is required to hold stock in each. These equity securities are restricted from trading and are recorded at a cost of $2.8 million and $3.6 million as of September 30, 2012 and December 31, 2011, respectively.

NOTE 6 LOANS:

Loans receivable outstanding are summarized as follows:

(Dollars are in thousands)	September 30, 2012	December 31, 2011
Real estate secured:		
Commercial	$ 155,255	$ 170,789
Construction and land development	25,212	32,389
Residential 1-4 family	243,938	255,998
Multifamily	12,636	14,320
Farmland	35,179	40,106
Total real estate loans	472,220	513,602
Commercial	30,420	39,327
Agriculture	4,965	6,147
Consumer installment loans	31,200	38,522
All other loans	187	218
Total loans	$ 538,992	$ 597,816

Loans receivable on nonaccrual status are summarized as follows:

(Dollars are in thousands)	September 30, 2012	December 31, 2011
Real estate secured:		
Commercial	$ 19,735	$ 19,169
Construction and land development	2,997	5,583
Residential 1-4 family	4,974	4,829
Multifamily	2,076	2,101
Farmland	7,198	5,257
Total real estate loans	36,980	36,939
Commercial	2,556	4,522
Agriculture	494	854
Consumer installment loans	127	1
All other loans		
Total loans receivable on nonaccrual status	$ 40,157	$ 42,316

Total interest income not recognized on nonaccrual loans for nine months ended September 30, 2012 and 2011 was $1.1 million and $1.3 million, respectively.

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The following table presents information concerning the Company s investment in loans considered impaired as of September 30, 2012 and December 31, 2011:

As of September 30, 2012 (Dollars are in thousands)	Average Recorded Investment	Interest Income Recognized	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:					
Real estate secured:					
Commercial	$ 28,230	$ 628	$ 21,704	$ 24,215	$
Construction and land development	5,009	84	4,017	8,934	
Residential 1-4 family	8,203	243	7,548	7,810	
Multifamily	1,045	48	1,196	1,196	
Farmland	8,592	(44)	9,068	9,407	
Commercial	2,846	35	2,034	2,389	
Agriculture	551	8	467	467	
Consumer installment loans	79	9	112	112	
All other loans					
With an allowance recorded:					
Real estate secured:					
Commercial	15,089	241	16,139	16,510	4,225
Construction and land development	1,962	(157)	1,575	5,636	346
Residential 1-4 family	5,884	165	4,714	5,257	793
Multifamily	1,479	26	2,314	2,550	621
Farmland	4,790	66	2,185	2,306	385
Commercial	1,641	17	1,395	1,663	207
Agriculture	378				
Consumer installment loans	79	3	37	37	15
All other loans					
Total	$ 85,857	$ 1,372	$ 74,505	$ 88,489	$ 6,592

As of December 31, 2011 (Dollars are in thousands)	Average Recorded Investment	Interest Income Recognized	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:					
Real estate secured:					
Commercial	$ 32,370	$ 1,356	$ 31,633	$ 33,175	$
Construction and land development	14,288	125	6,954	12,838	
Residential 1-4 family	6,406	315	8,221	8,296	
Multifamily	619	31	613	613	
Farmland	13,005	435	10,364	10,554	
Commercial	2,958	60	3,529	4,070	
Agriculture	396	1	521	817	
Consumer installment loans	4	1	9	9	
All other loans					
With an allowance recorded:					
Real estate secured:					
Commercial	9,887	691	14,482	14,973	2,794
Construction and land development	2,917	87	2,289	2,310	474
Residential 1-4 family	5,111	277	6,473	6,764	1,052
Multifamily					
Farmland	2,354	119	4,192	4,192	605

Commercial	1,982	75	1,857	1,857	649
Agriculture	758	28	641	641	448
Consumer installment loans	41	3	43	43	24
All other loans					
Total	$ 93,096	$ 3,604	$ 91,821	$ 101,152	$ 6,046

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An age analysis of past due loans receivable was as follows:

As of September 30, 2012 (Dollars are in thousands)	Loans 30-59 Days Past Due	Loans 60-89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or More Days Past Due
Real estate secured:							
Commercial	$ 4,118	$ 884	$ 9,586	$ 14,588	$ 140,667	$ 155,255	$
Construction and land development	2,106	84	912	3,102	22,110	25,212	
Residential 1-4 family	7,586	1,858	3,692	13,136	230,802	243,938	1,074
Multifamily		331	2,076	2,407	10,229	12,636	
Farmland	704	192	5,299	6,195	28,984	35,179	
Total real estate loans	14,514	3,349	21,565	39,428	432,792	472,220	1,074
Commercial	30	382	1,831	2,243	28,177	30,420	3
Agriculture	59		343	402	4,563	4,965	
Consumer installment Loans	660	56	187	903	30,297	31,200	72
All other loans	66	14	7	87	100	187	7
Total loans	$ 15,329	$ 3,801	$ 23,933	$ 43,063	$ 495,929	$ 538,992	$ 1,156

As of December 31, 2011 (Dollars are in thousands)	Loans 30-59 Days Past Due	Loans 60-89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or More Days Past Due
Real estate secured:							
Commercial	$ 9,754	$ 2,294	$ 7,771	$ 19,819	$ 150,970	$ 170,789	$
Construction and land development	595	238	5,280	6,113	26,276	32,389	
Residential 1-4 family	9,471	1,412	4,101	14,984	241,014	255,998	1,129
Multifamily		1,777	218	1,995	12,325	14,320	
Farmland	2,841	624	3,800	7,265	32,841	40,106	
Total real estate loans	22,661	6,345	21,170	50,176	463,426	513,602	1,129
Commercial	551	34	2,938	3,523	35,804	39,327	117
Agriculture	268	88	458	814	5,333	6,147	3
Consumer installment Loans	822	133	221	1,176	37,346	38,522	222
All other loans	26	9	33	68	150	218	33
Total loans	$ 24,328	$ 6,609	$ 24,820	$ 55,757	$ 542,059	$ 597,816	$ 1,504

The Company categorizes loans receivable into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans and leases individually by classifying the loans receivable as to credit risk. The Company uses the following definitions for risk ratings:

Pass - Loans in this category are considered to have a low likelihood of loss based on relevant information analyzed about the ability of the borrowers to service their debt and other factors.

Special Mention - Loans in this category are currently protected but are potentially weak, including adverse trends in borrower s operations, credit quality or financial strength. Those loans constitute an undue and unwarranted credit risk but not to the point of justifying a substandard classification. The credit risk may be relatively minor yet constitute an unwarranted risk in light of the circumstances. Special mention loans have potential weaknesses which may, if not checked or corrected, weaken the loan or inadequately protect the Company s credit position at some future date.

Substandard - A substandard loan is inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified as substandard must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt; they are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

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Doubtful - Loans classified Doubtful have all the weaknesses inherent in loans classified Substandard, plus the added characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions, and values highly questionable and improbable.

Based on the most recent analysis performed, the risk category of loans receivable was as follows:

As of September 30, 2012

(Dollars are in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Real estate secured:					
Commercial	$ 109,113	$ 11,913	$ 34,084	$ 145	$ 155,255
Construction and land development	18,148	1,260	5,804		25,212
Residential 1-4 family	198,672	16,245	27,834	1,187	243,938
Multifamily	9,220	179	3,237		12,636
Farmland	21,904	2,405	10,870		35,179
Total real estate loans	357,057	32,002	81,829	1,332	472,220
Commercial	23,013	3,748	3,618	41	30,420
Agriculture	4,191	229	543	2	4,965
Consumer installment loans	29,622	501	1,027	50	31,200
All other loans	187				187
Total	$ 414,070	$ 36,480	$ 87,017	$ 1,425	$ 538,992

As of December 31, 2011

(Dollars are in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Real estate secured:					
Commercial	$ 112,694	$ 18,377	$ 39,573	$ 145	$ 170,789
Construction and land development	23,203	1,224	7,962		32,389
Residential 1-4 family	209,863	17,137	27,730	1,268	255,998
Multifamily	11,727	1,909	684		14,320
Farmland	21,715	4,957	13,022	412	40,106
Total real estate loans	379,202	43,604	88,971	1,825	513,602
Commercial	32,018	2,045	4,227	1,037	39,327
Agriculture	4,743	678	726		6,147
Consumer installment loans	36,107	900	1,484	31	38,522
All other loans	218				218
Total	$ 452,288	$ 47,227	$ 95,408	$ 2,893	$ 597,816

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NOTE 7 ALLOWANCE FOR LOAN LOSSES:

The following table details activity in the allowance for loan losses by portfolio segment for the period ended September 30, 2012. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

As of September 30, 2012

(Dollars are in thousands)	Beginning Balance	Charge Offs	Recoveries	Advances	Provisions	Ending Balance
Real estate secured:						
Commercial	$ 5,671	$ (1,989)	$ 38	$	$ 3,852	$ 7,572
Construction and land development	3,848	(339)	71		(1,240)	2,340
Residential 1-4 family	3,759	(1,289)	84		726	3,280
Multifamily	148				541	689
Farmland	951	(577)			483	857
Total real estate loans	14,377	(4,194)	193		4,362	14,738
Commercial	1,883	(736)	67		311	1,525
Agriculture	486	(2)	11		(171)	324
Consumer installment loans	781	(267)	43		(128)	429
All other loans	2				(1)	1
Unallocated	851				(280)	571
Total	$ 18,380	$ (5,199)	$ 314	$	$ 4,093	$ 17,588

As of September 30, 2012	Allowance for Loan Losses			Recorded Investment in Loans		
(Dollars are in thousands)	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Real estate secured:						
Commercial	$ 4,225	$ 3,347	$ 7,572	$ 37,843	$ 117,412	$ 155,255
Construction and land development	346	1,994	2,340	5,592	19,620	25,212
Residential 1-4 family	793	2,487	3,280	12,262	231,676	243,938
Multifamily	621	68	689	3,510	9,126	12,636
Farmland	385	472	857	11,253	23,926	35,179
Total real estate loans	6,370	8,368	14,738	70,460	401,760	472,220
Commercial	207	1,318	1,525	3,429	26,991	30,420
Agriculture		324	324	467	4,498	4,965
Consumer installment loans	15	414	429	149	31,051	31,200
All other loans		1	1		187	187
Unallocated		571	571			
Total	$ 6,592	$ 10,996	$ 17,588	$ 74,505	$ 464,487	$ 538,992

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The following table details activity in the allowance for loan losses by portfolio segment for the period ended December 31, 2011. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

As of December 31, 2011

(Dollars are in thousands)	Beginning Balance	Charge Offs	Recoveries	Advances	Provisions	Ending Balance
Real estate secured:						
Commercial	$ 5,141	$ (4,147)	$ 877	$	$ 3,800	$ 5,671
Construction and land development	4,913	(7,245)	1,296	153	4,731	3,848
Residential 1-4 family	1,699	(1,299)	141		3,218	3,759
Multifamily	42				106	148
Farmland	922	(511)	66		474	951
Total real estate loans	12,717	(13,202)	2,380	153	12,329	14,377
Commercial	3,281	(2,480)	140		942	1,883
Agriculture	1,120	(1,031)	18		379	486
Consumer installment loans	1,733	(694)	123		(381)	781
All other loans					2	2
Unallocated	6,163				(5,312)	851
Total	$ 25,014	$ (17,407)	$ 2,661	$ 153	$ 7,959	$ 18,380

As of December 31, 2011	Allowance for Loan Losses			Recorded Investment in Loans		
(Dollars are in thousands)	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
Real estate secured:						
Commercial	$ 2,794	$ 2,877	$ 5,671	$ 46,115	$ 124,674	$ 170,789
Construction and land development	474	3,374	3,848	9,243	23,146	32,389
Residential 1-4 family	1,052	2,707	3,759	14,694	241,304	255,998
Multifamily		148	148	613	13,707	14,320
Farmland	605	346	951	14,556	25,550	40,106
Total real estate loans	4,925	9,452	14,377	85,221	428,381	513,602
Commercial	649	1,234	1,883	5,386	33,941	39,327
Agriculture	448	38	486	1,162	4,985	6,147
Consumer installment loans	24	757	781	52	38,470	38,522
All other loans		2	2		218	218
Unallocated		851	851			
Total	$ 6,046	$ 12,334	$ 18,380	$ 91,821	$ 505,995	$ 597,816

In determining the amount of our allowance, we rely on an analysis of our loan portfolio, our experience and our evaluation of general economic conditions, as well as the requirements of the written agreement and other regulatory input. If our assumptions prove to be incorrect, our current allowance may not be sufficient to cover future loan losses and we may experience significant increases to our provision.

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NOTE 8 TROUBLED DEBT RESTRUCTURINGS:

The following table presents information related to loans modified as troubled debt restructurings during the nine and three months ended September 30, 2012 and 2011.

Troubled Debt Restructurings (Dollars are in thousands)	For the nine months ended September 30, 2012 # of Loans	Pre-Mod. Recorded Investment	Post-Mod. Recorded Investment	For the nine months ended September 30, 2011 # of Loans	Pre-Mod. Recorded Investment	Post-Mod. Recorded Investment
Real estate secured:						
Commercial	7	$ 991	$ 791	8	$ 6,956	$ 6,928
Construction and land Development				1	29	28
Residential 1-4 family	35	2,052	1,964	8	641	626
Multifamily				1	342	342
Farmland						
Total real estate loans	42	3,043	2,755	18	7,968	7,924
Commercial				6	1,111	1,096
Agriculture				2	390	390
Consumer installment loans	3	25	19	8	159	152
All other loans						
Total	45	$ 3,068	$ 2,774	34	$ 9,628	$ 9,562

Troubled Debt Restructurings (Dollars are in thousands)	For the three months ended September 30, 2012 # of Loans	Pre-Mod. Recorded Investment	Post-Mod. Recorded Investment	For the three months ended September 30, 2011 # of Loans	Pre-Mod. Recorded Investment	Post-Mod. Recorded Investment
Real estate secured:						
Commercial		$	$	4	$ 3,585	$ 3,577
Construction and land Development						
Residential 1-4 family				4	312	298
Multifamily				1	342	342
Farmland						
Total real estate loans				9	4,239	4,217
Commercial				5	1,074	1,063
Agriculture				1	90	90
Consumer installment loans				4	92	91
All other loans						
Total		$	$	19	$ 5,495	$ 5,461

During the nine months ended September 30, 2012, the Company modified 45 loans that were considered to be troubled debt restructurings. We extended the terms for 6 of these loans and the interest rate was lowered for 35 of these loans. During the nine months ended September 30, 2011, the Company modified 34 loans that were considered to be troubled debt restructurings. We extended the terms for 17 of these loans and the interest rate was lowered for 15 of these loans.

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The following table presents information related to loans to modified as a troubled debt restructurings that defaulted during the nine and three months ended September 30, 2012 and 2011, and within twelve months of their modification date. A troubled debt restructuring is considered to be in default once it becomes 90 days or more past due following a modification.

Troubled Debt Restructurings That Subsequently Defaulted During the Period	For the nine months ended September 30, 2012		For the nine months ended September 30, 2011	
(Dollars are in thousands)	# of Loans	Recorded Investment	# of Loans	Recorded Investment
Real estate secured:				
Commercial	4	$ 1,859		$
Construction and land development				
Residential 1-4 family	2	633		
Multifamily	1	163		
Farmland				
Total real estate loans	7	2,655		
Commercial				
Agriculture	1	300		
Consumer installment loans				
All other loans				
Total	8	$ 2,955		$

Troubled Debt Restructurings That Subsequently Defaulted During the Period	For the three months ended September 30, 2012		For the three months ended September 30, 2011	
(Dollars are in thousands)	# of Loans	Recorded Investment	# of Loans	Recorded Investment
Real estate secured:				
Commercial		$		$
Construction and land development				
Residential 1-4 family	1	522		
Multifamily	1	163		
Farmland				
Total real estate loans	2	685		
Commercial				
Agriculture				
Consumer installment loans				
All other loans				
Total	2	$ 685		$

In determination of the allowance for loan losses, management considers troubled debt restructurings and subsequent defaults in these restructurings in its estimate. The Company evaluates all troubled debt restructurings for possible further impairment. As a result, the allowance may be increased, adjustments may be made in the allocation of the allowance, or charge-offs may be taken to further writedown the carrying value of the loan. At September 30, 2012 there were $21.8 million in loans that are classified as troubled debt restructurings compared to $29.1 million at December 31, 2011.

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NOTE 9 EARNINGS PER SHARE:

Basic earnings per share computations are based on the weighted average number of shares outstanding during each year. Dilutive earnings per share reflect the additional common shares that would have been outstanding if dilutive potential common shares had been issued. Potential common shares that may be issued relate to outstanding options and are determined by the Treasury method. For the three and nine months ended September 30, 2012 and 2011, potential common shares were anti-dilutive and were not included in the calculation. Basic and diluted net loss per common share calculations follows:

(Amounts in Thousands, Except Share and Per Share Data)	For the three months ended September 30,		For the nine months ended September 30,	
	2012	2011	2012	2011
Net loss	$ (1,463)	$ (1,832)	$ (6,536)	$ (2,958)