FIRST COMMUNITY CORP /SC/
Form 10-K
March 29, 2011

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

(Mark One)

ý **Annual Report under Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the fiscal year ended December 31, 2010

Or

o **Transition Report under Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the transition period from to
Commission file number: 000-28344

First Community Corporation

(Exact name of registrant as specified in its charter)

South Carolina (State or other jurisdiction of incorporation or organization)	**57-1010751** (I.R.S. Employer Identification No.)
5455 Sunset Blvd., Lexington, South Carolina (Address of principal executive offices)	**29072** (Zip Code)

803-951-2265
Registrant's telephone number, including area code

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	**Name of each exchange on which registered**
Common stock, $1.00 par value per share	The NASDAQ Capital Market

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No ý

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes o No ý

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 past 90 days. Yes ý No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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 o No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. Yes o No ý

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.

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

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

As of June 30, 2010, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was $16,946,376 based on the closing sale price of $5.80 on June 30, 2010, as reported on The NASDAQ Capital Market. 3,273,533 shares of the issuer's common stock were issued and outstanding as of March 29, 2011.

Documents Incorporated by Reference

Proxy Statement for the Annual Meeting of Shareholders to be held on May 18, 2011.	Part III (Portions of Items 10-14)

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This report, including information included or incorporated by reference in this document, contains statements which constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements may relate to, among other matters, the financial condition, results of operations, plans, objectives, future performance, and business of our Company. Forward-looking statements are based on many assumptions and estimates and are not guarantees of future performance. Our actual results may differ materially from those anticipated in any forward-looking statements, as they will depend on many factors about which we are unsure, including many factors which are beyond our control. The words "may," "would," "could," "should," "will," "expect," "anticipate," "predict," "project," "potential," "continue," "assume," "believe," "intend," "plan," "forecast," "goal," and "estimate," as well as similar expressions, are meant to identify such forward-looking statements. Potential risks and uncertainties that could cause our actual results to differ materially from those anticipated in our forward-looking statements include, without limitation, those described under the heading "Risk Factors" in this Annual Report on Form 10-K for the year ended December 31, 2010 as filed with the Securities and Exchange Commission (the "SEC") and the following:

- reduced earnings due to higher credit losses generally and specifically because losses in the sectors of our loan portfolio secured by real estate are greater than expected due to economic factors, including, but not limited to, declining real estate values, increasing interest rates, increasing unemployment, or changes in payment behavior or other factors;
- reduced earnings due to higher other-than-temporary impairment charges resulting from additional decline in the value of our private label mortgage backed securities portfolio, specifically as a result of increasing default rates, and loss severities on the underlying real estate collateral.
- the amount of our loan portfolio collateralized by real estate and weaknesses in the real estate market;
- our ability to comply with our formal written agreement with our primary bank regulator and potential regulatory actions if we fail to comply;
- restrictions or conditions imposed by our regulators on our operations may make it more difficult for us to achieve our goals;
- the adequacy of the level of our allowance for loan losses and the amount of loan loss provisions required in future periods;
- significant increases in competitive pressure in the banking and financial services industries;
- changes in the interest rate environment which could reduce anticipated or actual margins;
- changes in political conditions or the legislative or regulatory environment, including the effect of recent financial reform legislation on the banking and financial services industries;
- general economic conditions, either nationally or regionally and especially in our primary service area, being less favorable than expected resulting in, among other things, a deterioration in credit quality;
- changes occurring in business conditions and inflation;

increased funding costs due to market illiquidity, increased competition for funding, and/or increased regulatory requirements with regard to funding;

changes in deposit flows;

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- changes in technology;
- changes in monetary and tax policies;
- changes in monetary and tax policies, including confirmation of the income tax refund claims received by the Internal Revenue Service ("IRS");
- changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board and the Financial Accounting Standards Board;
- the rate of delinquencies and amounts of loans charged-off;
- the rate of loan growth in recent years and the lack of seasoning of a portion of our loan portfolio;
- our ability to maintain appropriate levels of capital and to comply with our higher individual minimum capital ratios;
- our ability to attract and retain key personnel;
- our ability to retain our existing customers, including our deposit relationships;
- adverse changes in asset quality and resulting credit risk-related losses and expenses;
- loss of consumer confidence and economic disruptions resulting from terrorist activities; and
- other risks and uncertainties detailed in Part I, Item 1A of this Annual Report on Form 10-K and from time to time in our filings with the SEC.

These risks are exacerbated by the developments over the last three years in national and international financial markets, and we are unable to predict what effect these uncertain market conditions will continue to have on our Company. Beginning in 2008 and continuing throughout 2010, the capital and credit markets experienced unprecedented levels of extended volatility and disruption. There can be no assurance that these unprecedented developments will not continue to materially and adversely affect our business, financial condition and results of operations.

All forward-looking statements in this report are based on information available to us as of the date of this report. Although we believe that the expectations reflected in our forward-looking statements are reasonable, we cannot guarantee you that these expectations will be achieved. We undertake no obligation to publicly update or otherwise revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

PART I

Item 1. Business.

General

First Community Corporation, a bank holding company registered under the Bank Holding Company Act of 1956, as amended, was incorporated under the laws of South Carolina in 1994 primarily to own and control all of the capital stock of First Community Bank, N.A., which commenced operations in August 1995. On October 1, 2004, we completed our acquisition of DutchFork Bancshares, Inc. and its wholly-owned subsidiary, Newberry Federal Savings Bank. During the second quarter of 2006, we completed our acquisition of DeKalb Bankshares, Inc., the holding company for The Bank of Camden. On September 15, 2008, we completed the acquisition of two financial planning and investment advisory firms, EAH Financial Group and Pooled Resources, LLC. We engage in a commercial banking business from our main office in Lexington, South Carolina and our 11 full-service offices located in Lexington (two), Forest Acres, Irmo, Cayce-West Columbia, Gilbert, Chapin,

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Northeast Columbia, Prosperity, Newberry and Camden. We offer a wide-range of traditional banking products and services for professionals and small-to medium-sized businesses, including consumer and commercial, mortgage, brokerage and investment, and insurance services. We also offer online banking to our customers. Our stock trades on The NASDAQ Capital Market under the symbol "FCCO".

Location and Service Area

The bank is engaged in a general commercial and retail banking business, emphasizing the needs of small-to-medium sized businesses, professional concerns and individuals, primarily in Richland, Lexington, Kershaw and Newberry Counties of South Carolina and the surrounding areas.

Richland County, Lexington County, Kershaw County and Newberry County are located in the geographic center of the state of South Carolina. Columbia, the capital of South Carolina, is located within and divided between Richland and Lexington counties. Columbia can be reached via three interstate highways: I-20, I-26, and I-77. Columbia is served by several airlines as well as by passenger and freight rail service. According to the U. S. Census Bureau, Richland, Lexington, Kershaw and Newberry Counties, which include the primary service areas for the existing eleven sites of the bank, had estimated populations in 2009 of 372,023, 255,607, 60,042 and 38,763, respectively. The principal components of the economy within our market area are service industries, government, and wholesale and retail trade. The largest employers in the area, each of which employs in excess of 3,000 people, include Fort Jackson Army Base, the University of South Carolina, Palmetto Health Alliance, Blue Cross Blue Shield and SCANA Corporation. The area has experienced steady growth over the past 10 years and we expect that the area, as well as the service industry needed to support it, will to continue to grow. For 2009, Richland, Lexington, Kershaw and Newberry Counties had estimated median household incomes of $45,643, $52,062, $45,268 and $37,263, respectively, compared to $42,580 for South Carolina as a whole. Markets in the United States, including our market areas, have experienced extreme volatility and disruption for more than 30 months. Our operations have been significantly impacted by prevailing economic conditions, competition, and the monetary, fiscal, and regulatory policies of governmental agencies.

Banking Services

We offer a full range of deposit services that are typically available in most banks and thrift institutions, including checking accounts, NOW accounts, savings accounts and other time deposits of various types, ranging from daily money market accounts to longer-term certificates of deposit. The transaction accounts and time certificates are tailored to our principal market area at rates competitive to those offered in the area. In addition, we offer certain retirement account services, such as Individual Retirement Accounts ("IRAs"). All deposit accounts are insured by the Federal Deposit Insurance Corporation ("FDIC") up to the maximum amount allowed by law (currently, $250,000, subject to aggregation rules).

We also offer a full range of commercial and personal loans. Commercial loans include both secured and unsecured loans for working capital (including inventory and receivables), business expansion (including acquisition of real estate and improvements), and the purchase of equipment and machinery. Consumer loans include secured and unsecured loans for financing automobiles, home improvements, education, and personal investments. We also make real estate construction and acquisition loans. We originate fixed and variable rate mortgage loans substantially all of which are closed in the name of a third party, which are sold into the secondary market. Our lending activities are subject to a variety of lending limits imposed by federal law. While differing limits apply in certain circumstances based on the type of loan or the nature of the borrower (including the borrower's relationship to the bank), in general, we are subject to a loans-to-one-borrower limit of an amount equal to 15% of the bank's unimpaired capital and surplus, or 25% of the unimpaired capital and surplus if the excess over 15% is approved by the board of directors of the bank and is fully secured by readily marketable collateral. As a result, our lending limit will increase or decrease in response to increases or decreases in the bank's level of capital. Based upon the capitalization of the bank at December 31, 2010, the maximum amount we could lend to one borrower is $8.5 million. In addition, we may not make any loans to any director, officer, employee, or 10% shareholder of the company or the bank unless the loan is approved by our board of directors and is made on terms not more favorable to such person than would be available to a person not affiliated with the bank.

Other bank services include internet banking, cash management services, safe deposit boxes, travelers checks, direct deposit of payroll and social security checks, and automatic drafts for various accounts. We offer non-deposit investment products and other investment brokerage services through a registered representative with an affiliation through LPL Financial. We are associated with Jeannie, Star, and Plus networks of automated teller machines and Mastermoney debit cards that may be used by our customers throughout South Carolina and other regions. We also offer VISA and MasterCard credit card services through a correspondent bank as our agent.

We currently do not exercise trust powers, but we can begin to do so with the prior approval of our primary banking regulator, the Office of the Comptroller of the Currency ("OCC").

Competition

The banking business is highly competitive. We compete as a financial intermediary with other commercial banks, savings and loan associations, credit unions and money market mutual funds operating in Richland, Lexington, Kershaw and Newberry Counties and elsewhere. As of June 30, 2010, there were 26 financial institutions operating approximately 202 offices in Lexington, Richland, Kershaw and Newberry Counties. The competition among the various financial institutions is based upon a variety of factors, including interest rates offered on deposit accounts, interest rates charged on loans, credit and service charges, the quality of services rendered the convenience of banking facilities and, in the case of loans to large commercial borrowers, relative lending limits. Size gives larger banks certain advantages in competing for business from large corporations. These advantages include higher lending limits and the ability to offer services in other areas of South Carolina. As a result, we do not generally attempt to compete for the banking relationships of large corporations, but concentrate our efforts on small-to-medium sized businesses and individuals. We believe we have competed effectively in this market by offering quality and personal service.

Market Share

As of June 30, 2010, the most recent date for which market data is available, total deposits in the bank's primary service area, Lexington, Richland, Kershaw and Newberry Counties, were over $13.8 billion. At June 30, 2010, our deposits represented 3.3% of the market.

Employees

As of December 31, 2010, we had 147 full-time employees. We believe that our relations with our employees are good.

SUPERVISION AND REGULATION

Both the company and the bank are subject to extensive state and federal banking laws and regulations that impose specific requirements or restrictions on and provide for general regulatory oversight of virtually all aspects of our operations. These laws and regulations are generally intended to protect depositors, not shareholders. The following summary is qualified by reference to the statutory and regulatory provisions discussed. Changes in applicable laws or regulations may have a material effect on our business and prospects. Our operations may be affected by legislative changes and the policies of various regulatory authorities. We cannot predict the effect that fiscal or monetary policies, economic control, or new federal or state legislation may have on our business and earnings in the future.

On April 6, 2010, the bank entered into a formal written agreement (the "Formal Agreement") with the OCC, our primary bank regulator. The Formal Agreement is based on the findings of the OCC during a 2009 on-site examination of the bank. As reflected in the Formal Agreement, the OCC's primary concern with the bank is driven by the rating agencies downgrades of non-agency mortgage backed securities (MBS) in its investment portfolio. These securities, purchased in 2004 through 2008, were all rated AAA by the rating agencies at the time of purchase; however, they have been impacted by the economic recession and the stress on the residential housing sector. These ratings do not reflect the discounted purchase price paid by the bank. They only reflect their analysis of the performance of the security overall, and therefore, a downgrade does not capture the risk of loss to the bank. The Formal Agreement did not require any adjustment to the bank's balance sheet or income statement; nor did it change the Bank's "well capitalized" status. The OCC has, however, separately established the following individual minimum capital ratios for the bank: a Tier 1 leverage capital ratio of at least 8.00%, a Tier 1 risk-based capital ratio of at least 10.00%, and a Total risk-based capital ratio of at least 12.00%. As of December 31, 2010, the bank exceeds each of these ratios and remains "well capitalized."

The Board of Directors has appointed an independent compliance committee made up of directors to monitor and report on compliance with the terms of the Formal Agreement. The bank intends to take all actions necessary to enable it to comply with the requirements of the Formal Agreement, and as of the date hereof management has submitted all documentation required as of this date to the OCC. There can be no assurance that the bank will be able to comply fully with the provisions of the Formal Agreement, and the determination of our compliance will be made by the OCC. However, management believes the bank is currently in compliance with all provisions of the Formal Agreement. Failure to meet the requirements of the Formal Agreement could result in additional regulatory requirements, which could result in regulators taking additional enforcement actions against the bank.

The following discussion is not intended to be a complete list of all the activities regulated by the banking laws or of the impact of such laws and regulations on our operations. It is intended only to briefly summarize some material provisions.

First Community Corporation

We own 100% of the outstanding capital stock of the bank, and therefore we are considered to be a bank holding company under the federal Bank Holding Company Act of 1956, as amended (the "Bank Holding Company Act"). As a result, we are primarily subject to the supervision, examination and reporting requirements of the Board of Governors of the Federal Reserve (the "Federal Reserve") under the Bank Holding Company Act and its regulations promulgated there under. Moreover, as a bank holding company of a bank located in South Carolina, we also are subject to the South Carolina Banking and Branching Efficiency Act.

Permitted Activities. Under the Bank Holding Company Act, a bank holding company is generally permitted to engage in, or acquire direct or indirect control of more than 5% of the voting shares of any company engaged in, the following activities:

- banking or managing or controlling banks;
- furnishing services to or performing services for our subsidiaries; and
- any activity that the Federal Reserve determines to be so closely related to banking as to be a proper incident to the business of banking.

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Activities that the Federal Reserve has found to be so closely related to banking as to be a proper incident to the business of banking include:

- factoring accounts receivable;
- making, acquiring, brokering or servicing loans and usual related activities;
- leasing personal or real property;
- operating a non-bank depository institution, such as a savings association;
- trust company functions;
- financial and investment advisory activities;
- conducting discount securities brokerage activities;
- underwriting and dealing in government obligations and money market instruments;
- providing specified management consulting and counseling activities;
- performing selected data processing services and support services;
- acting as agent or broker in selling credit life insurance and other types of insurance in connection with credit transactions; and
- performing selected insurance underwriting activities.

As a bank holding company, we also can elect to be treated as a "financial holding company," which would allow us to engage in a broader array of activities. In sum, a financial holding company can engage in activities that are financial in nature or incidental or complimentary to financial activities, including insurance underwriting, sales and brokerage activities, providing financial and investment advisory services, underwriting services and limited merchant banking activities. We have not sought financial holding company status, but may elect such status in the future as our business matures. If we were to elect in writing for financial holding company status, each insured depository institution we control would have to be well capitalized, well managed and have at least a satisfactory rating under the Community Reinvestment Act ("CRA") (discussed below).

The Federal Reserve has the authority to order a bank holding company or its subsidiaries to terminate any of these activities or to terminate its ownership or control of any subsidiary when it has reasonable cause to believe that the bank holding company's continued ownership, activity or control constitutes a serious risk to the financial safety, soundness or stability of it or any of its bank subsidiaries.

Change in Control. In addition, and subject to certain exceptions, the Bank Holding Company Act and the Change in Bank Control Act, together with regulations promulgated there under, require Federal Reserve approval prior to any person or company acquiring "control" of a bank holding company. Control is conclusively presumed to exist if an individual or company acquires 25% or more of any class of voting securities of a bank holding company. Following the relaxing of these restrictions by the Federal Reserve in September 2008, control will be rebuttably presumed to exist if a person acquires more than 33% of the total equity of a bank or bank holding company, of which it may own, control or have the power to vote not more than 15% of any class of voting securities.

Source of Strength. In accordance with Federal Reserve Board policy, we are expected to act as a source of financial strength to the bank and to commit resources to support the bank in circumstances in which we might not otherwise do so. If the bank were to become "under-capitalized" (see below under "First Community Bank, N.A. Prompt Corrective Action"), we would be required to provide a guarantee of the bank's plan to return to capital adequacy. Additionally, under the Bank Holding Company Act, the Federal Reserve Board may require a bank holding company to terminate any activity or relinquish control of a non-bank subsidiary, other than a non-bank subsidiary of a bank, upon the Federal Reserve's determination that such activity or control constitutes a serious risk to the financial soundness or stability of any depository institution subsidiary of a bank holding company. Federal bank regulatory authorities have additional discretion to require a bank holding company to divest itself of any bank or non-bank subsidiaries if the agency determines that divestiture may aid the depository institution's financial condition. Further, any loans by a bank holding company to a subsidiary bank are subordinate in right of payment to deposits and certain other indebtedness of the subsidiary bank. In the event of a bank holding company's bankruptcy, any commitment by the bank holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank at a certain level would be assumed by the bankruptcy trustee and entitled to priority payment.

Capital Requirements. The Federal Reserve Board imposes certain capital requirements on the bank holding company under the Bank Holding Company Act, including a minimum leverage ratio and a minimum ratio of "qualifying" capital to risk-weighted assets. These requirements are essentially the same as those that apply to the bank and are described below under "First Community Bank, N.A. Capital Regulations." Subject to our capital requirements and certain other restrictions, we are able to borrow money to make a capital contribution to the bank, and these loans may be repaid from dividends paid from the bank to the company. Our ability to pay dividends depends on, among other things, the bank's ability to pay dividends to us, which is subject to regulatory restrictions as described below in "First Community Bank, N.A. Dividends." We are also able to raise capital for contribution to the bank by issuing securities without having to receive regulatory approval, subject to compliance with federal and state securities laws.

South Carolina State Regulation. As a South Carolina bank holding company under the South Carolina Banking and Branching Efficiency Act, we are subject to limitations on sale or merger and to regulation by the South Carolina Board of Financial Institutions (the "S.C. Board"). We are not required to obtain the approval of the S.C. Board prior to acquiring the capital stock of a national bank, but we must notify them at least 15 days prior to doing so. We must receive the Board's approval prior to engaging in the acquisition of a South Carolina state chartered bank or another South Carolina bank holding company.

First Community Bank, N.A.

The bank operates as a national banking association incorporated under the laws of the United States and subject to examination by the OCC. Deposits in the bank are insured by the FDIC up to a maximum amount of $250,000, pursuant to the provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") signed into law by the U.S. President on July 21, 2010. The FDIC insurance coverage limit applies per depositor, per insured depository institution for each account ownership category. In addition, the FDIC provides unlimited deposit insurance coverage for noninterest-bearing transaction accounts (typically business checking accounts) and certain funds swept into noninterest-bearing savings accounts. We elected to voluntarily participate in the FDIC's Temporary Liquidity Guarantee Program ("TLGP") (discussed below in greater detail) through December 31, 2010. Throughout 2010, participating institutions paid fees of 15 to 25 basis points (annualized), depending on the Risk Category assigned to the institution, on the balance of each covered account in excess of $250 thousand. Coverage under the program was in addition to and separate from the basic coverage available under the FDIC's general deposit insurance rules. We believe participation in the program enhanced our ability to retain customer deposits. As a result of the Dodd-Frank Act, the voluntary TAGP program will end on December 31, 2010, and all institutions will be required to provide full deposit insurance on noninterest-bearing transaction accounts until December 31, 2012.

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The OCC and the FDIC regulate or monitor virtually all areas of the bank's operations, including:

- security devices and procedures;
- adequacy of capitalization and loss reserves;
- loans;
- investments;
- borrowings;
- deposits;
- mergers;
- issuances of securities;
- payment of dividends;
- interest rates payable on deposits;
- interest rates or fees chargeable on loans;
- establishment of branches;
- corporate reorganizations;
- maintenance of books and records; and
- adequacy of staff training to carry on safe lending and deposit gathering practices.

The OCC requires that the bank maintain specified capital ratios of capital to assets and imposes limitations on the bank's aggregate investment in real estate, bank premises, and furniture and fixtures. Two categories of regulatory capital are used in calculating these ratios Tier 1 capital and total capital. Tier 1 capital generally includes common equity, retained earnings, a limited amount of qualifying preferred stock, and qualifying minority interests in consolidated subsidiaries, reduced by goodwill and certain other intangible assets, such as core deposit intangibles, and certain other assets. Total capital generally consists of Tier 1 capital plus Tier 2 capital, which includes the allowance for loan losses, preferred stock that did not qualify as Tier 1 capital, certain types of subordinated debt and a limited amount of other items.

The bank is required to calculate three ratios: the ratio of Tier 1 capital to risk-weighted assets, the ratio of total capital to risk-weighted assets, and the "leverage ratio," which is the ratio of Tier 1 capital to assets on a non-risk-adjusted basis. For the two ratios of capital to risk-weighted assets, certain assets, such as cash and U.S. Treasury securities, have a zero risk weighting. Others, such as commercial and consumer loans, have a 100% risk weighting. Some assets, notably purchase- money loans secured by first-liens on residential real property, are risk-weighted at 50%. Assets also include amounts that represent the potential funding of off-balance sheet obligations such as loan commitments and letters of credit. These potential assets are assigned to risk categories in the same manner as funded assets. The total assets in each category are multiplied by the appropriate risk weighting to determine risk-adjusted assets for the capital calculations.

The minimum capital ratios for both the company and the bank are generally 8% for total capital, 4% for Tier 1 capital and 4% for leverage. To be eligible to be classified as "well capitalized," the bank must generally maintain a total capital ratio of 10% or more, a Tier 1 capital ratio of 6% or more, and a leverage ratio of 5% or more. Certain implications of the regulatory capital classification system is discussed in greater detail below. In addition to the Formal Agreement discussed above, the OCC has separately established the following individual minimum capital ratios for the bank: a Tier 1 leverage capital ratio of at least 8.00%, a Tier 1 risk-based capital ratio of at least 10.00%, and a Total risk-based capital ratio of at least 12.00%. As of December 31, 2010, the bank exceeds each of these ratios and remains "well capitalized."

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Prompt Corrective Action. The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") established a "prompt corrective action" program in which every bank is placed in one of five regulatory categories, depending primarily on its regulatory capital levels. The OCC and the other federal banking regulators are permitted to take increasingly severe action as a bank's capital position or financial condition declines below the "Adequately Capitalized" level described below. Regulators are also empowered to place in receivership or require the sale of a bank to another depository institution when a bank's leverage ratio reaches two percent. Better capitalized institutions are generally subject to less onerous regulation and supervision than banks with lesser amounts of capital. The OCC's regulations set forth five capital categories, each with specific regulatory consequences. The categories are:

Well Capitalized The institution exceeds the required minimum level for each relevant capital measure. A well capitalized institution is one (i) having a total capital ratio of 10% or greater, (ii) having a Tier 1 capital ratio of 6% or greater, (iii) having a leverage capital ratio of 5% or greater and (iv) that is not subject to any order or written directive to meet and maintain a specific capital level for any capital measure.

Adequately Capitalized The institution meets the required minimum level for each relevant capital measure. No capital distribution may be made that would result in the institution becoming undercapitalized. An adequately capitalized institution is one (i) having a total capital ratio of 8% or greater, (ii) having a Tier 1 capital ratio of 4% or greater and (iii) having a leverage capital ratio of 4% or greater or a leverage capital ratio of 3% or greater if the institution is rated composite 1 under the CAMELS (Capital, Assets, Management, Earnings, Liquidity and Sensitivity to market risk) rating system.

Undercapitalized The institution fails to meet the required minimum level for any relevant capital measure. An undercapitalized institution is one (i) having a total capital ratio of less than 8% or (ii) having a Tier 1 capital ratio of less than 4% or (iii) having a leverage capital ratio of less than 4%, or if the institution is rated a composite 1 under the CAMEL rating system, a leverage capital ratio of less than 3%.

Significantly Undercapitalized The institution is significantly below the required minimum level for any relevant capital measure. A significantly undercapitalized institution is one (i) having a total capital ratio of less than 6% or (ii) having a Tier 1 capital ratio of less than 3% or (iii) having a leverage capital ratio of less than 3%.

Critically Undercapitalized The institution fails to meet a critical capital level set by the appropriate federal banking agency. A critically undercapitalized institution is one having a ratio of tangible equity to total assets that is equal to or less than 2%.

If the OCC determines, after notice and an opportunity for hearing, that the bank is in an unsafe or unsound condition, the regulator is authorized to reclassify the bank to the next lower capital category (other than critically undercapitalized) and require the submission of a plan to correct the unsafe or unsound condition.

Usually, if the bank is not well capitalized, it cannot accept brokered deposits without prior FDIC approval and, if approval is granted, cannot offer an effective yield in excess of 75 basis points on interests paid on deposits of comparable size and maturity in such institution's normal market area for deposits accepted from within its normal market area, or national rate paid on deposits of comparable size and maturity for deposits accepted outside the bank's normal market area. Moreover, if the bank becomes less than adequately capitalized, it must adopt a capital restoration plan acceptable to the OCC that is subject to a limited performance guarantee by the corporation. The bank also would become subject to increased regulatory oversight, and is increasingly restricted in the scope of its permissible activities. Each company having control over an undercapitalized institution also must provide a limited guarantee that the institution will comply with its capital restoration plan. Except under limited circumstances consistent with an accepted capital restoration plan, an undercapitalized institution may not grow. An undercapitalized institution may not acquire another institution, establish additional branch offices or engage in any new line of business unless determined by the appropriate federal banking agency to be consistent with an accepted capital restoration plan, or unless the FDIC determines that the proposed action will further the purpose of prompt corrective action. The appropriate federal banking agency may take any action authorized for a significantly undercapitalized institution if an undercapitalized institution fails to submit an acceptable capital restoration plan or fails in any material respect to implement a plan accepted by the agency. A critically undercapitalized institution is subject to having a receiver or conservator appointed to manage its affairs and for loss of its charter to conduct banking activities.

An insured depository institution may not pay a management fee to a bank holding company controlling that institution or any other person having control of the institution if, after making the payment, the institution, would be undercapitalized. In addition, an institution cannot make a capital distribution, such as a dividend or other distribution that is in substance a distribution of capital to the owners of the institution if following such a distribution the institution would be undercapitalized. Thus, if payment of such a management fee or the making of such would cause the bank to become undercapitalized, it could not pay a management fee or dividend to us.

In addition to the Formal Agreement discussed above, the OCC has separately established the following individual minimum capital ratios for the bank: a Tier 1 leverage capital ratio of at least 8.00%, a Tier 1 risk-based capital ratio of at least 10.00%, and a Total risk-based capital ratio of at least 12.00%. As of December 31, 2010, the bank exceeds each of these ratios and remains "well capitalized."

Standards for Safety and Soundness. The Federal Deposit Insurance Act also requires the federal banking regulatory agencies to prescribe, by regulation or guideline, operational and managerial standards for all insured depository institutions relating to: (i) internal controls, information systems and internal audit systems; (ii) loan documentation; (iii) credit underwriting; (iv) interest rate risk exposure; and (v) asset growth. The agencies also must prescribe standards for asset quality, earnings, and stock valuation, as well as standards for compensation, fees and benefits. The federal banking agencies have adopted regulations and Interagency Guidelines Prescribing Standards for Safety and Soundness to implement these required standards. These guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. Under the regulations, if the OCC determines that the bank fails to meet any standards prescribed by the guidelines, the agency may require the bank to submit to the agency an acceptable plan to achieve compliance with the standard, as required by the OCC. The final regulations establish deadlines for the submission and review of such safety and soundness compliance plans.

Regulatory Examination. The OCC also requires the bank to prepare annual reports on the bank's financial condition and to conduct an annual audit of its financial affairs in compliance with its minimum standards and procedures.

All insured institutions must undergo regular on-site examinations by their appropriate banking agency. The cost of examinations of insured depository institutions and any affiliates may be assessed by the appropriate federal banking agency against each institution or affiliate as it deems necessary or appropriate. Insured institutions are required to submit annual reports to the FDIC, their federal regulatory agency, and state supervisor when applicable. The FDIC has developed a method for insured depository institutions to provide supplemental disclosure of the estimated fair market value of assets and liabilities, to the extent feasible and practicable, in any balance sheet, financial statement, report of condition or any other report of any insured depository institution. The federal banking regulatory agencies prescribe, by regulation, standards for all insured depository institutions and depository institution holding companies relating, among other things, to the following:

- internal controls;
- information systems and audit systems;
- loan documentation;
- credit underwriting;
- interest rate risk exposure; and
- asset quality.

Transactions with Affiliates and Insiders. The company is a legal entity separate and distinct from the bank and its other subsidiaries. Various legal limitations restrict the bank from lending or otherwise supplying funds to the company or its non-bank subsidiaries. The company and the bank are subject to Sections 23A and 23B of the Federal Reserve Act and Federal Reserve Regulation W. Section 23A of the Federal Reserve Act places limits on the amount of loans or extensions of credit to, or investments in, or certain other transactions with, affiliates and on the amount of advances to third parties collateralized by the securities or obligations of affiliates. The aggregate of all covered transactions is limited in amount, as to any one affiliate, to 10% of the bank's capital and surplus and, as to all affiliates combined, to 20% of the bank's capital and surplus. Furthermore, within the foregoing limitations as to amount, each covered transaction must meet specified collateral requirements. The bank is forbidden to purchase low quality assets from an affiliate.

Section 23B of the Federal Reserve Act, among other things, prohibits an institution from engaging in certain transactions with certain affiliates unless the transactions are on terms substantially the same, or at least as favorable to such institution or its subsidiaries, as those prevailing at the time for comparable transactions with nonaffiliated companies.

Regulation W generally excludes all non-bank and non-savings association subsidiaries of banks from treatment as affiliates, except to the extent that the Federal Reserve Board decides to treat these subsidiaries as affiliates. The regulation also limits the amount of loans that can be purchased by a bank from an affiliate to not more than 100% of the bank's capital and surplus.

The bank is also subject to certain restrictions on extensions of credit to executive officers, directors, certain principal shareholders, and their related interests. Such extensions of credit (i) must be made on substantially the same terms, including interest rates, and collateral, as those prevailing at the time for comparable transactions with third parties and (ii) must not involve more than the normal risk of repayment or present other unfavorable features.

Dividends. The company's principal source of cash flow, including cash flow to pay dividends to its shareholders, is dividends it receives from the bank. Statutory and regulatory limitations apply to the bank's payment of dividends to the company. As a general rule, the amount of a dividend may not exceed, without prior regulatory approval, the sum of net income in the calendar year to date and the retained net earnings of the immediately preceding two calendar years. A depository institution may not pay any dividend if payment would cause the institution to become undercapitalized or if it already is undercapitalized. The OCC may prevent the payment of a dividend if it determines that the payment would be an unsafe and unsound banking practice. The OCC also has advised that a national bank should generally pay dividends only out of current operating earnings.

Pursuant to the terms of the Formal Agreement between the bank and the OCC, the bank is currently restricted from paying cash dividends to the company without the prior approval of the OCC. In addition, the company must currently obtain preapproval of the Federal Reserve Board before paying dividends.

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Branching. National banks are required by the National Bank Act to adhere to branch office banking laws applicable to state banks in the states in which they are located. Under current South Carolina law, the bank may open branch offices throughout South Carolina with the prior approval of the OCC. In addition, with prior regulatory approval, the bank is able to acquire existing banking operations in South Carolina. Furthermore, federal legislation permits interstate branching, including out-of-state acquisitions by bank holding companies, interstate branching by banks, and interstate merging by banks. The Dodd-Frank Act removes previous state law restrictions on de novo interstate branching in states such as South Carolina. This change permits out-of-state banks to open de novo branches in states where the laws of the state where the de novo branch to be opened would permit a bank chartered by that state to open a de novo branch.

Anti-Tying Restrictions. Under amendments to the Bank Holding Company Act and Federal Reserve regulations, a bank is prohibited from engaging in certain tying or reciprocity arrangements with its customers. In general, a bank may not extend credit, lease, sell property, or furnish any services or fix or vary the consideration for these on the condition that (i) the customer obtain or provide some additional credit, property, or services from or to the bank, the bank holding company or subsidiaries thereof or (ii) the customer may not obtain some other credit, property, or services from a competitor, except to the extent reasonable conditions are imposed to assure the soundness of the credit extended. Certain arrangements are permissible: a bank may offer combined-balance products and may otherwise offer more favorable terms if a customer obtains two or more traditional bank products; and certain foreign transactions are exempt from the general rule. A bank holding company or any bank affiliate also is subject to anti-tying requirements in connection with electronic benefit transfer services.

Community Reinvestment Act. The CRA requires that the OCC evaluate the record of the bank in meeting the credit needs of its local community, including low and moderate income neighborhoods. These factors are also considered in evaluating mergers, acquisitions, and applications to open a branch or facility. Failure to adequately meet these criteria could impose additional requirements and limitations on our bank.

Finance Subsidiaries. Under the Gramm-Leach-Bliley Act (the "GLBA"), subject to certain conditions imposed by their respective banking regulators, national and state-chartered banks are permitted to form "financial subsidiaries" that may conduct financial or incidental activities, thereby permitting bank subsidiaries to engage in certain activities that previously were impermissible. The GLBA imposes several safeguards and restrictions on financial subsidiaries, including that the parent bank's equity investment in the financial subsidiary be deducted from the bank's assets and tangible equity for purposes of calculating the bank's capital adequacy. In addition, the GLBA imposes new restrictions on transactions between a bank and its financial subsidiaries similar to restrictions applicable to transactions between banks and non-bank affiliates.

Consumer Protection Regulations. Activities of the bank are subject to a variety of statutes and regulations designed to protect consumers. Interest and other charges collected or contracted for by the bank are subject to state usury laws and federal laws concerning interest rates. The bank's loan operations are also subject to federal laws applicable to credit transactions, such as:

- the federal Truth-In-Lending Act, governing disclosures of credit terms to consumer borrowers;
- the Home Mortgage Disclosure Act of 1975, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;
- the Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, creed or other prohibited factors in extending credit;

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- the Fair Credit Reporting Act of 1978, governing the use and provision of information to credit reporting agencies;
- the Fair Debt Collection Act, governing the manner in which consumer debts may be collected by collection agencies; and
- the rules and regulations of the various federal agencies charged with the responsibility of implementing such federal laws.

The deposit operations of the bank also are subject to:

- the Right to Financial Privacy Act, which imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records; and
- the Electronic Funds Transfer Act and Regulation E issued by the Federal Reserve Board to implement that Act, which governs automatic deposits to and withdrawals from deposit accounts and customers' rights and liabilities arising from the use of automated teller machines and other electronic banking services.

Enforcement Powers. The bank and its "institution-affiliated parties," including its management, employee's agent's independent contractors and consultants such as attorneys and accountants and others who participate in the conduct of the financial institution's affairs, are subject to potential civil and criminal penalties for violations of law, regulations or written orders of a government agency. These practices can include the failure of an institution to timely file required reports or the filing of false or misleading information or the submission of inaccurate reports. Civil penalties may be as high as $1,000,000 a day for such violations. Criminal penalties for some financial institution crimes have been increased to twenty years. In addition, regulators are provided with greater flexibility to commence enforcement actions against institutions and institution-affiliated parties. Possible enforcement actions include the termination of deposit insurance. Furthermore, banking agencies' power to issue cease-and-desist orders were expanded. Such orders may, among other things, require affirmative action to correct any harm resulting from a violation or practice, including restitution, reimbursement, indemnifications or guarantees against loss. A financial institution may also be ordered to restrict its growth, dispose of certain assets, rescind agreements or contracts, or take other actions as determined by the ordering agency to be appropriate.

Anti-Money Laundering. Financial institutions must maintain anti-money laundering programs that include established internal policies, procedures, and controls; a designated compliance officer; an ongoing employee training program; and testing of the program by an independent audit function. The company and the bank are also prohibited from entering into specified financial transactions and account relationships and must meet enhanced standards for due diligence and "knowing your customer" in their dealings with foreign financial institutions and foreign customers. Financial institutions must take reasonable steps to conduct enhanced scrutiny of account relationships to guard against money laundering and to report any suspicious transactions, and recent laws provide law enforcement authorities with increased access to financial information maintained by banks. Anti-money laundering obligations have been substantially strengthened as a result of the USA Patriot Act, enacted in 2001 and renewed in 2006. Bank regulators routinely examine institutions for compliance with these obligations and are required to consider compliance in connection with the regulatory review of applications. The regulatory authorities have been active in imposing "cease and desist" orders and money penalty sanctions against institutions found to be violating these obligations.

USA PATRIOT Act/Bank Secrecy Act. Financial institutions must maintain anti-money laundering programs that include established internal policies, procedures, and controls; a designated compliance officer; an ongoing employee training program; and testing of the program by an independent audit function. The USA PATRIOT Act, amended, in part, the Bank Secrecy Act and provides for the facilitation of information sharing among governmental entities and financial institutions for the purpose of combating terrorism and money laundering by enhancing anti-money laundering and financial transparency laws, as well as enhanced information collection tools and enforcement mechanics for the U.S. government, including: (i) requiring standards for verifying customer identification at account opening; (ii) rules to promote cooperation among financial institutions, regulators, and law enforcement entities in identifying parties that may be involved in terrorism or money laundering; (iii) reports by nonfinancial trades and businesses filed with the U.S. Treasury Department's Financial Crimes Enforcement Network for transactions exceeding $10,000; and (iv) filing suspicious activities reports if a bank believes a customer may be violating U.S. laws and regulations and requires enhanced due diligence requirements for financial institutions that administer, maintain, or manage private bank accounts or correspondent accounts for non-U.S. persons. Bank regulators routinely examine institutions for compliance with these obligations and are required to consider compliance in connection with the regulatory review of applications.

Under the USA PATRIOT Act, the Federal Bureau of Investigation ("FBI") can send to the banking regulatory agencies lists of the names of persons suspected of involvement in terrorist activities. The bank can be requested, to search its records for any relationships or transactions with persons on those lists. If the bank finds any relationships or transactions, it must file a suspicious activity report and contact the FBI.

The Office of Foreign Assets Control ("OFAC"), which is a division of the U.S. Department of the Treasury (the "Treasury"), is responsible for helping to insure that United States entities do not engage in transactions with "enemies" of the United States, as defined by various Executive Orders and Acts of Congress. OFAC has sent, and will send, our banking regulatory agencies lists of names of persons and organizations suspected of aiding, harboring or engaging in terrorist acts. If the bank finds a name on any transaction, account or wire transfer that is on an OFAC list, it must freeze such account, file a suspicious activity report and notify the FBI. The bank has appointed an OFAC compliance officer to oversee the inspection of its accounts and the filing of any notifications. The bank actively checks high-risk OFAC areas such as new accounts, wire transfers and customer files. The bank performs these checks utilizing software, which is updated each time a modification is made to the lists provided by OFAC and other agencies of Specially Designated Nationals and Blocked Persons.

Privacy and Credit Reporting. Financial institutions are required to disclose their policies for collecting and protecting confidential information. Customers generally may prevent financial institutions from sharing nonpublic personal financial information with nonaffiliated third parties except under narrow circumstances, such as the processing of transactions requested by the consumer. Additionally, financial institutions generally may not disclose consumer account numbers to any nonaffiliated third party for use in telemarketing, direct mail marketing or other marketing to consumers. It is the bank's policy not to disclose any personal information unless required by law. The OCC and the federal banking agencies have prescribed standards for maintaining the security and confidentiality of consumer information. The bank is subject to such standards, as well as standards for notifying consumers in the event of a security breach.

Like other lending institutions, the bank utilizes credit bureau data in its underwriting activities. Use of such data is regulated under the Federal Credit Reporting Act on a uniform, nationwide basis, including credit reporting, prescreening, sharing of information between affiliates, and the use of credit data. The Fair and Accurate Credit Transactions Act of 2003 (the "FACT Act") permits states to enact identity theft laws that are not inconsistent with the conduct required by the provisions of the FACT Act.

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Check 21. The Check Clearing for the 21st Century Act gives "substitute checks," such as a digital image of a check and copies made from that image, the same legal standing as the original paper check. Some of the major provisions include:

- allowing check truncation without making it mandatory;
- demanding that every financial institution communicate to accountholders in writing a description of its substitute check processing program and their rights under the law;
- legalizing substitutions for and replacements of paper checks without agreement from consumers;
- retaining in place the previously mandated electronic collection and return of checks between financial institutions only when individual agreements are in place;
- requiring that when accountholders request verification, financial institutions produce the original check (or a copy that accurately represents the original) and demonstrate that the account debit was accurate and valid; and
- requiring the re-crediting of funds to an individual's account on the next business day after a consumer proves that the financial institution has erred.

Effect of Governmental Monetary Policies. Our earnings are affected by domestic economic conditions and the monetary and fiscal policies of the United States government and its agencies. The Federal Reserve Bank's monetary policies have had, and are likely to continue to have, an important impact on the operating results of commercial banks through its power to implement national monetary policy in order, among other things, to curb inflation or combat a recession. The monetary policies of the Federal Reserve Board have major effects upon the levels of bank loans, investments and deposits through its open market operations in United States government securities and through its regulation of the discount rate on borrowings of member banks and the reserve requirements against member bank deposits. It is not possible to predict the nature or impact of future changes in monetary and fiscal policies.

Insurance of Accounts and Regulation by the FDIC. The deposits at our bank are insured up to applicable limits by the Deposit Insurance Fund of the FDIC. The Deposit Insurance Fund is the successor to the Bank Insurance Fund and the Savings Association Insurance Fund, which were merged effective March 31, 2006. As insurer, the FDIC imposes deposit insurance premiums and is authorized to conduct examinations of and to require reporting by FDIC insured institutions. It also may prohibit any FDIC insured institution from engaging in any activity the FDIC determines by regulation or order to pose a serious risk to the insurance fund. The FDIC also has the authority to initiate enforcement actions against savings institutions, after giving the Office of Thrift Supervision an opportunity to take such action, and may terminate the deposit insurance if it determines that the institution has engaged in unsafe or unsound practices or is in an unsafe or unsound condition.

Under regulations effective January 1, 2007, the FDIC adopted a new risk-based premium system that provides for quarterly assessments based on an insured institution's ranking in one of four risk categories based upon supervisory and capital evaluations. For deposits held as of March 31, 2009, institutions are assessed at annual rates ranging from 12 to 50 basis points, depending on each institution's risk of default as measured by regulatory capital ratios and other supervisory measures. Effective April 1, 2009, assessments will take into account each institution's reliance on secured liabilities and brokered deposits. This resulted in assessments ranging from 7 to 77.5 basis points. In May 2009, the FDIC issued a final rule which levied a special assessment applicable to all insured depository institutions totaling 5 basis points of each institution's total assets less Tier 1 capital as of June 30, 2009, not to exceed 10 basis points of domestic deposits. This special assessment was part of the FDIC's efforts to rebuild the Deposit Insurance Fund. We paid this one time special assessment in the amount of $300 thousand to the FDIC at the end of the third quarter 2009.

In November 2009, the FDIC issued a rule that required all insured depository institutions, with limited exceptions, to prepay their estimated quarterly risk-based assessments for the fourth quarter of 2009 and for all of 2010, 2011 and 2012. The FDIC also adopted a uniform three-basis point increase in assessment rates effective on January 1, 2011. In December 2009, we paid $2.9 million in prepaid risk-based assessments, which included $184 thousand related to the fourth quarter of 2009 that would have been otherwise payable in the first quarter of 2010. This amount is included in deposit insurance expense for 2009. The remaining $2.7 million in prepaid deposit insurance is included in accrued interest receivable and other assets in the accompanying balance sheet as of December 31, 2009. As a result, we incurred increased insurance costs during 2009 and 2010 than in previous periods.

FDIC insured institutions are required to pay a Financing Corporation assessment to fund the interest on bonds issued to resolve thrift failures in the 1980s. The Financing Corporation quarterly assessment for the fourth quarter of 2010 equaled 5.765 basis points for each $100 in domestic deposits at our institution. These assessments, which may be revised based upon the level of deposits, will continue until the bonds mature in the years 2017 through 2019.

The FDIC may terminate the deposit insurance of any insured depository institution, including the bank, if it determines after a hearing that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC or the OCC. It also may suspend deposit insurance temporarily during the hearing process for the permanent termination of insurance, if the institution has no tangible capital. If insurance of accounts is terminated, the accounts at the institution at the time of the termination, less subsequent withdrawals, shall continue to be insured for a period of six months to two years, as determined by the FDIC. Management of the bank is not aware of any practice, condition or violation that might lead to termination of the bank's deposit insurance.

Incentive Compensation. In June 2010, the Federal Reserve, the FDIC and the OCC issued a comprehensive final guidance on incentive compensation policies intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. The guidance, which covers all employees that have the ability to materially affect the risk profile of an organization, either individually or as part of a group, is based upon the key principles that a banking organization's incentive compensation arrangements should (i) provide incentives that do not encourage risk-taking beyond the organization's ability to effectively identify and manage risks, (ii) be compatible with effective internal controls and risk management, and (iii) be supported by strong corporate governance, including active and effective oversight by the organization's board of directors.

The Federal Reserve will review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as the company, that are not "large, complex banking organizations." These reviews will be tailored to each organization based on the scope and complexity of the organization's activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the organization's supervisory ratings, which can affect the organization's ability to make acquisitions and take other actions. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the organization's safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies.

Recent Legislative and Regulatory Initiatives to Address Financial and Economic Crises. The Congress, Treasury and the federal banking regulators, including the FDIC, have taken broad action since early September 2008 to address volatility in the U.S. banking system.

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In October 2008, the Emergency Economic Stabilization Act of 2008 ("EESA") was enacted. The EESA authorizes the Treasury Department to purchase from financial institutions and their holding companies up to $700 billion in mortgage loans, mortgage-related securities and certain other financial instruments, including debt and equity securities issued by financial institutions and their holding companies in a troubled asset relief program ("TARP"). The purpose of TARP is to restore confidence and stability to the U.S. banking system and to encourage financial institutions to increase their lending to customers and to each other. The Treasury has allocated $250 billion towards the TARP Capital Purchase Program ("CPP"). Under the CPP, the Treasury Department purchased debt or equity securities from participating institutions. TARP also includes direct purchases or guarantees of troubled assets of financial institutions. Participants in the CPP are subject to executive compensation limits and are encouraged to expand their lending and mortgage loan modifications.

On November 21, 2008 as part of the TARP CPP, the company entered into a Letter Agreement and Securities Purchase Agreement (collectively, the "CPP Purchase Agreement") with the Treasury, pursuant to which the company sold (i) 11,350 shares of its Fixed Rate Cumulative Perpetual Preferred Stock, Series T (the "Series T Preferred Stock") and (ii) a warrant (the "CPP Warrant") to purchase 195,915 shares of the company's common stock for an aggregate purchase price of $11,350,000 in cash.

The Series T Preferred Stock will qualify as Tier 1 capital and will be entitled to cumulative dividends at a rate of 5% per annum for the first five years, and 9% per annum thereafter. The company must consult with the OCC before it may redeem the Series T Preferred Stock but, contrary to the original restrictions in the EESA, will not necessarily be required to raise additional equity capital in order to redeem this stock. The CPP Warrant has a 10-year term and is immediately exercisable upon its issuance, with an exercise price, subject to anti-dilution adjustments, equal to $8.69 per share of the common stock. Please see the Form 8-K we filed with the SEC on November 25, 2008, for additional information about the Series T Preferred Stock and the CPP Warrant.

Following a systemic risk determination, the FDIC established its Temporary Liquidity Guarantee Program ("TLGP") in October 2008. Under the interim rule for the TLGP, there are two parts to the program: the Debt Guarantee Program ("DGP") and the Transaction Account Guarantee Program ("TAGP"). Eligible entities generally are participants unless they exercised an opt-out right in timely fashion. Under the DGP, the FDIC guarantees certain senior unsecured debt issued by participating entities. Under the TAGP, the FDIC guarantees all funds held in qualifying noninterest-bearing transaction accounts at participating insured depository institutions.

The DGP initially permitted participating entities to issue FDIC-guaranteed senior unsecured debt until June 30, 2009, with the FDIC's guarantee for such debt to expire on the earlier of the maturity of the debt (or the conversion date, for mandatory convertible debt) or June 30, 2012. To reduce the potential for market disruptions at the conclusion of the DGP and to begin the orderly phase-out of the program, on May 29, 2009 the FDIC issued a final rule that extended for four months the period during which certain participating entities could issue FDIC-guaranteed debt. All insured depository institutions and those other participating entities that had issued FDIC-guaranteed debt on or before April 1, 2009 were permitted to participate in the extended DGP without application to the FDIC. Other participating entities that received approval from the FDIC also were permitted to participate in the extended DGP. The expiration of the guarantee period was also extended from June 30, 2012 to December 31, 2012. As a result, all such participating entities were permitted to issue FDIC-guaranteed debt through and including October 31, 2009, with the FDIC's guarantee expiring on the earliest of the debt's mandatory conversion date (for mandatory convertible debt), the stated maturity date, or December 31, 2012. The company opted out of the DGP.

For the TAGP, eligible entities are all FDIC-insured institutions. Under the TAGP, the FDIC provides unlimited deposit insurance coverage for noninterest-bearing transaction accounts (typically business checking accounts) and certain funds swept into noninterest-bearing savings accounts. We elected to voluntarily participate in the TAGP through December 31, 2010. Throughout 2010, participating institutions paid fees of 15 to 25 basis points (annualized), depending on the Risk Category assigned to the institution, on the balance of each covered account in excess of $250 thousand. Coverage under the TAGP was in addition to and separate from the basic coverage available under the FDIC's general deposit insurance rules. As a result of the Dodd-Frank Act that was signed into law on July 21, 2010, the voluntary TAGP program will end on December 31, 2010, and all institutions will be required to provide full deposit insurance on noninterest-bearing transaction accounts until December 31, 2012. There will not be a separate assessment for this as there was for institutions participating in the TAGP program.

The EESA has been followed by numerous actions by the Federal Reserve, Congress, U.S. Treasury, the SEC and others to address the liquidity and credit crisis that followed the recession that commenced in 2007. These measures include homeowner relief that encourages loan restructuring and modification; the establishment of significant liquidity and credit facilities for financial institutions and banks; the lowering of the federal funds rate; action against short-term selling practices, the temporary guaranty program for money market funds; the establishment of a commercial paper funding facility to provide back-stop liquidity to commercial paper issuers; and coordinated international efforts to address illiquidity and other weaknesses in the banking sector.

On July 21, 2010, the U.S. President signed into law the Dodd-Frank Act, a comprehensive regulatory framework that will likely result in dramatic changes across the financial regulatory system, some of which became effective immediately and some of which will not become effective until various future dates. Implementation of the Dodd-Frank Act will require many new rules to be made by various federal regulatory agencies over the next several years. Uncertainty remains as to the ultimate impact of the Dodd-Frank Act until final rulemaking is complete, which could have a material adverse impact either on the financial services industry as a whole or on our business, financial condition, results of operations, and cash flows. Provisions in the legislation that affect consumer financial protection regulations, deposit insurance assessments, payment of interest on demand deposits, and interchange fees could increase the costs associated with deposits and place limitations on certain revenues those deposits may generate. The Dodd-Frank Act includes provisions that, among other things, will:

- Centralize responsibility for consumer financial protection by creating a new agency, the Bureau of Consumer Financial Protection, responsible for implementing, examining, and enforcing compliance with federal consumer financial laws;

- Create the Financial Stability Oversight Council that will recommend to the Federal Reserve increasingly strict rules for capital, leverage, liquidity, risk management and other requirements as companies grow in size and complexity;

- Provide mortgage reform provisions regarding a customer's ability to repay, restricting variable-rate lending by requiring that the ability to repay variable-rate loans be determined by using the maximum rate that will apply during the first five years of a variable-rate loan term, and making more loans subject to provisions for higher cost loans, new disclosures, and certain other revisions;

- Change the assessment base for federal deposit insurance from the amount of insured deposits to consolidated assets less tangible capital, eliminate the ceiling on the size of the Deposit Insurance Fund ("DIF"), and increase the floor on the size of the DIF, which generally will require an increase in the level of assessments for institutions with assets in excess of $10 billion;

- Make permanent the $250,000 limit for federal deposit insurance and provide unlimited federal deposit insurance until December 31, 2012 for noninterest-bearing demand transaction accounts at all insured depository institutions;

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- Implement corporate governance revisions, including with regard to executive compensation and proxy access by shareholders, which apply to all public companies, not just financial institutions;

- Repeal the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transactions and other accounts;

- Amend the Electronic Fund Transfer Act ("EFTA") to, among other things, give the Federal Reserve the authority to establish rules regarding interchange fees charged for electronic debit transactions by payment card issuers having assets over $10 billion and to enforce a new statutory requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer;

- Eliminate the Office of Thrift Supervision ("OTS") one year from the date of the new law's enactment. The OCC, which is currently the primary federal regulator for national banks such as our bank, will become the primary federal regulator for federal thrifts. In addition, the Federal Reserve will supervise and regulate all savings and loan holding companies that were formerly regulated by the OTS.

On September 27, 2010, the U.S. President signed into law the Small Business Jobs Act of 2010 (the "Act"). The Small Business Lending Fund (the "SBLF"), which was enacted as part of the Act, is a $30 billion fund that encourages lending to small businesses by providing Tier 1 capital to qualified community banks with assets of less than $10 billion. On December 21, 2010, the U.S. Treasury published the application form, term sheet and other guidance for participation in the SBLF. Under the terms of the SBLF, the Treasury will purchase shares of senior preferred stock from banks, bank holding companies, and other financial institutions that will qualify as Tier 1 capital for regulatory purposes and rank senior to a participating institution's common stock. The application deadline for participating in the SBLF is March 31, 2011.

Internationally, both the Basel Committee on Banking Supervision (the "Basel Committee") and the Financial Stability Board (established in April 2009 by the Group of Twenty ("G-20") Finance Ministers and Central Bank Governors to take action to strengthen regulation and supervision of the financial system with greater international consistency, cooperation, and transparency) have committed to raise capital standards and liquidity buffers within the banking system ("Basel III"). On September 12, 2010, the Group of Governors and Heads of Supervision agreed to the calibration and phase-in of the Basel III minimum capital requirements (raising the minimum Tier 1 common equity ratio to 4.5% and minimum Tier 1 equity ratio to 6.0%, with full implementation by January 2015) and introducing a capital conservation buffer of common equity of an additional 2.5% with full implementation by January 2019. The U.S. federal banking agencies support this agreement. In December 2010, the Basel Committee issued the Basel III rules text, outlining the details and time-lines of global regulatory standards on bank capital adequacy and liquidity. According to the Basel Committee, the Framework sets out higher and better-quality capital, better risk coverage, the introduction of a leverage ratio as a backstop to the risk-based requirement, measures to promote the build-up of capital that can be drawn down in periods of stress, and the introduction of two global liquidity standards.

In November 2010, the Federal Reserve's monetary policymaking committee, the Federal Open Market Committee ("FOMC"), decided that further support to the economy was needed. With short-term interest rates already nearing 0%, the FOMC agreed to deliver that support by committing to purchase additional longer-term securities, as it did in 2008 and 2009. The FOMC intends to buy an additional $600 billion of longer-term U.S. Treasury securities by mid-2011 and will continue to reinvest repayments of principal on its holdings of securities, as it has been doing since August 2010.

In November 2010, the FDIC approved two proposals that amend the deposit insurance assessment regulations. The first proposal implements a provision in the Dodd-Frank Act that changes the assessment base from one based on domestic deposits (as it has been since 1935) to one based on assets. The assessment base changes from adjusted domestic deposits to average consolidated total assets minus average tangible equity.

The second proposal changes the deposit insurance assessment system for large institutions in conjunction with the guidance given in the Dodd-Frank Act. Since the new base would be much larger than the current base, the FDIC will lower assessment rates, which achieves the FDIC's goal of not significantly altering the total amount of revenue collected from the industry. Risk categories and debt ratings will be eliminated from the assessment calculation for large banks which will instead use scorecards. The scorecards will include financial measures that are predictive of long-term performance. A large financial institution will continue to be defined as an insured depository institution with at least $10 billion in assets. Both changes in the assessment system will be effective as of April 1, 2011 and will be payable at the end of September.

In December 2010, the FDIC voted to increase the required amount of reserves for the designated reserve ratio ("DRR") to 2.0%. The ratio is higher than the 1.35% set by the Dodd-Frank Act in July 2010 and is an integral part of the FDIC's comprehensive, long-range management plan for the DIF. On December 16, 2010, the Federal Reserve issued a proposal to implement a provision in the Dodd-Frank Act that requires the Federal Reserve to set debit card interchange fees. The proposed rule, if implemented in its current form, would result in a significant reduction in debit-card interchange revenue. Though the rule technically does not apply to institutions with less than $10 billion in assets, there is concern that the price controls may harm community banks, which could be pressured by the marketplace to lower their own interchange rates.

On December 29, 2010, the Dodd-Frank Act was amended to include full FDIC insurance on Interest on Lawyers Trust Accounts ("IOLTAs"). IOLTAs will receive unlimited insurance coverage as noninterest-bearing transaction accounts for two years ending December 31, 2012.

In February 2011, the FDIC approved the final rules that, as noted above, change the assessment base from domestic deposits to average assets minus average tangible equity, adopt a new scorecard-based assessment system for financial institutions with more than $10 billion in assets, and finalize the DRR target size at 2.0% of insured deposits.

As a result of the enhancements to deposit insurance protection and the expectation that there will be demands on the FDIC's deposit insurance fund, our deposit insurance costs increased significantly in 2009 and remained elevated in 2010. Regardless of our lack of participation, governmental intervention and new regulations under these programs could materially and adversely affect our business, financial condition and results of operation.

With respect to any other potential future government assistance programs, we will evaluate the merits of the programs, including the terms of the financing, the company's capital position, the cost to the company of alternative capital, and the company's strategy for the use of additional capital, to determine whether it is prudent to participate.

Proposed Legislation and Regulatory Action. From time to time, various legislative and regulatory initiatives are introduced in Congress and state legislatures, as well as by regulatory agencies. Such initiatives may include proposals to expand or contract the powers of bank holding companies and depository institutions or proposals to substantially change the financial institution regulatory system. Such legislation could change banking statutes and the operating environment of the company in substantial and unpredictable ways. If enacted, such legislation could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance among banks, savings associations, credit unions, and other financial institutions. We cannot predict whether any such legislation will be enacted, and, if enacted, the effect that it, or any implementing regulations, would have on the financial condition or results of operations of the Company. A change in statutes, regulations or regulatory policies applicable to the company or the bank could have a material effect on the business of the company.

Item 1A. Risk Factors.

Our business, financial condition, and results of operations could be harmed by any of the following risks, or other risks that have not been identified or which we believe are immaterial or unlikely. Shareholders should carefully consider the risks described below in conjunction with the other information in this Form 10-K and the information incorporated by reference in this Form 10-K, including our consolidated financial statements and related notes.

We have become subject to a Formal Agreement that will require us to take certain actions.

On April 6, 2010, the bank entered into the Formal Agreement with the OCC, our primary bank regulator. The Formal Agreement is based on the findings of the OCC during a 2009 on-site examination of the bank. As reflected in the Formal Agreement, the OCC's primary concern with the bank is driven by the rating agencies downgrades of non-agency mortgage backed securities (MBS) in its investment portfolio. These securities, purchased in 2004 through 2008, were all rated AAA by the rating agencies at the time of purchase; however, they have been impacted by the economic recession and the stress on the residential housing sector.

The Board of Directors has appointed an independent compliance committee made up of directors to monitor and report on compliance with the terms of the Formal Agreement. The bank intends to take all actions necessary to enable it to comply with the requirements of the Formal Agreement, and as of the date hereof management has submitted all documentation required as of this date to the OCC. There can be no assurance that the bank will be able to comply fully with the provisions of the Formal Agreement, and the determination of our compliance will be made by the OCC. However, management believes the bank is currently in compliance with all provisions of the Formal Agreement. Failure to meet the requirements of the Formal Agreement could result in additional regulatory requirements, which could result in regulators taking additional enforcement actions against the bank.

Changes in the financial markets could impair the value of our investment portfolio.

The investment securities portfolio is a significant component of our total earning assets. Total securities averaged $194.4 million in 2010, as compared to $219.9 million in 2009. This represents 31.9% and 38.1% of the average earning assets for the year ended December 31, 2010 and 2009, respectively. At December 31, 2010, the portfolio was 33.4% of earning assets. Turmoil in the financial markets could impair the market value of our investment portfolio, which could adversely affect our net income and possibly our capital.

During the last half of 2007 and throughout 2008 through 2010 the bond markets and many institutional holders of bonds came under a great deal of stress partially as a result of the ongoing recessionary economic conditions. At December 31, 2010, we had mortgage-backed securities (MBSs) including collateralized mortgage obligations ("CMOs") with a fair value of $121.3 million. Of these, approximately $72.8 million were issued by government sponsored enterprises ("GSEs") and $48.5 million by private label issuers. The result has been that the market for these investments has become less liquid and the spread as compared to alternative investments has widened dramatically. To a lesser extent MBSs issued by GSEs such as the Federal Home Loan Mortgage Corporation ("FHLMC" or "Freddie Mac") and the Federal National Mortgage Association ("FNMA" or "Fannie Mae") have been impacted and spreads have increased on these investments. These entities have also experienced increasing delinquencies in the underlying loans that make up the MBSs and CMOs. In 2008 and 2009, many of the privately issued MBSs incurred rating agency downgrades. At December 31, 2010, 20 of our private label CMO's have been downgraded below investment grade.

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Delinquencies on the underlying mortgages on all mortgage securities have increased dramatically. We monitor these investments on a monthly basis. Increasing delinquencies and defaults in the underlying mortgages have resulted in recognizing OTTI during 2009 and 2010 (see Note 5 to the financial statements). In evaluating these securities for OTTI, we use assumptions relative to continued defaults rates, loss severities on the underlying collateral and prepayment speeds. Differences in actual experience and the assumptions used could result in a loss of earnings as a result of further OTTI charges, all of which could have a material adverse effect on our financial condition and results of operations.

Our other investments include municipal and corporate debt securities. As of December 31, 2010, we had municipal securities with an approximate fair value of $19.1 million and corporate debt and other securities with an approximate fair value of $3.8 million. Two corporate debt securities with a fair value of $1.1 million have been downgraded below investment grade (see Note 5 to the financial statements). Based on our evaluation we recognized OTTI on one of these securities in 2010 of $1.1 million (see Note 5 to the financial statements). There is a risk that further deterioration in the underlying issuer's financial condition or the underlying collateral could result in OTTI charges in future periods.

On September 7, 2008, the Treasury, the Federal Reserve and the Federal Housing Finance Agency ("FHFA") announced that FHFA was placing the FHLMC under conservatorship. Due to these actions, we took an OTTI charge of $8.1 million in the third quarter of 2008 relating to the Freddie Mac preferred stock that we held. This charge, along with our second quarter of 2008 charge of $6.1 million related to our investment in preferred stock issued by Freddie Mac, eliminated any further direct material exposure in our investment portfolio to Freddie Mac equity securities.

As of December 31, 2010 and 2009, for securities that were either classified as "Held to Maturity" or "Available for Sale" the unrealized losses on these investments were not considered to be "other than temporary" and we believe it is more likely than not we will be able to hold these until they mature or recover our current book value. We currently maintain substantial liquidity which supports our intent and ability to hold these investments until they mature, or until there is a market price recovery. However, if we were to cease to have the ability and intent to hold these investments until maturity or a market price recovery, or were to sell these securities at a loss, it could adversely affect our net income and possibly our capital.

Recent negative developments in the financial industry and the domestic and international credit markets may adversely affect our operations and results.

Negative developments in the latter half of 2007 and during 2008 through 2010 in the global credit and securitization markets have resulted in uncertainty in the financial markets in general with the expectation of the general economic downturn continuing into 2011. As a result, commercial as well as consumer loan portfolio performances have deteriorated at many institutions and the competition for deposits and quality loans has increased significantly. In addition, the values of real estate collateral supporting many commercial loans and home mortgages have declined and may continue to decline. Global securities markets and bank holding company stock prices in particular, have been negatively affected, as has the ability of banks and bank holding companies to raise capital or borrow in the debt markets. As a result, significant new federal laws and regulations relating to financial institutions, including, without limitation, the EESA and the Treasury's CPP, have been adopted. Furthermore, the potential exists for additional federal or state laws and regulations regarding, among other matters, lending and funding practices and liquidity standards, and bank regulatory agencies are expected to be active in responding to concerns and trends identified in examinations, including the expected issuance of many formal enforcement orders. Negative developments in the financial industry and the domestic and international credit markets, and the impact of new legislation in response to those developments, may negatively impact our operations by restricting our business operations, including our ability to

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originate or sell loans, and adversely impact our financial performance. We can provide no assurance regarding the manner in which any new laws and regulations will affect us.

There can be no assurance that recently enacted legislation will help stabilize the U.S. financial system.

As described above under Part I, Item 1, "Supervision and Regulation", in response to the challenges facing the financial services sector, a number of regulatory and governmental actions have been enacted or announced. There can be no assurance that these government actions will achieve their purpose. The failure of the financial markets to stabilize, or a continuation or worsening of the current financial market conditions, could have a material adverse affect on our business, our financial condition, the financial condition of our customers, our common stock trading price, as well as our ability to access credit. It could also result in declines in our investment portfolio which could be "other-than-temporary impairments."

Our focus on lending to small to mid-sized community-based businesses may increase our credit risk.

Most of our commercial business and commercial real estate loans are made to small business or middle market customers. These businesses generally have fewer financial resources in terms of capital or borrowing capacity than larger entities and have a heightened vulnerability to economic conditions. If general economic conditions in the markets in which we operate negatively impact this important customer sector, our results of operations and financial condition and the value of our common stock and Series A Preferred Stock may be adversely affected. Moreover, a portion of these loans have been made by us in recent years and the borrowers may not have experienced a complete business or economic cycle. Furthermore, the deterioration of our borrowers' businesses may hinder their ability to repay their loans with us, which could have a material adverse effect on our financial condition and results of operations.

Our decisions regarding credit risk and reserves for loan losses may materially and adversely affect our business.

Making loans and other extensions of credit is an essential element of our business. Although we seek to mitigate risks inherent in lending by adhering to specific underwriting practices, our loans and other extensions of credit may not be repaid. The risk of nonpayment is affected by a number of factors, including:

- the duration of the credit;
- credit risks of a particular customer;
- changes in economic and industry conditions; and
- in the case of a collateralized loan, risks resulting from uncertainties about the future value of the collateral.

We attempt to maintain an appropriate allowance for loan losses to provide for potential losses in our loan portfolio. We periodically determine the amount of the allowance based on consideration of several factors, including:

- an ongoing review of the quality, mix, and size of our overall loan portfolio;
- our historical loan loss experience;
- evaluation of economic conditions;

regular reviews of loan delinquencies and loan portfolio quality; and

the amount and quality of collateral, including guarantees, securing the loans.

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There is no precise method of predicting credit losses; therefore, we face the risk that charge-offs in future periods will exceed our allowance for loan losses and that additional increases in the allowance for loan losses will be required. Additions to the allowance for loan losses would result in a decrease of our net income, and possibly our capital.

Federal and state regulators periodically review our allowance for loan losses and may require us to increase our provision for loan losses or recognize further loan charge-offs, based on judgments different than those of our management. Any increase in the amount of our provision or loans charged-off as required by these regulatory agencies could have a negative effect on our operating results.

We may have higher loan losses than we have allowed for in our allowance for loan losses.

Our loan losses could exceed our allowance for loan losses. Our average loan size continues to increase and reliance on our historic allowance for loan losses may not be adequate. Approximately 75.6% of our loan portfolio is composed of construction (3.2%), commercial mortgage (66.2%) and commercial loans (6.2%). Repayment of such loans is generally considered more subject to market risk than residential mortgage loans. Industry experience shows that a portion of loans will become delinquent and a portion of loans will require partial or entire charge-off. Regardless of the underwriting criteria utilized, losses may be experienced as a result of various factors beyond our control, including among other things, changes in market conditions affecting the value of loan collateral and problems affecting the credit of our borrowers.

Economic challenges, especially those affecting Lexington, Richland, Newberry, and Kershaw Counties and the surrounding areas, may reduce our customer base, our level of deposits, and demand for financial products such as loans.

Our success significantly depends upon the growth in population, income levels, deposits, and housing starts in our markets of Lexington, Richland, Newberry, and Kershaw Counties and the surrounding area. The current economic downturn has negatively affected the markets in which we operate and, in turn, the quality of our loan portfolio. If the communities in which we operate do not grow or if prevailing economic conditions locally or nationally remain unfavorable, our business may not succeed. A continuation of the economic downturn or prolonged recession would likely result in the continued deterioration of the quality of our loan portfolio and reduce our level of deposits, which in turn would hurt our business. Interest received on loans represented approximately 72.2% of our interest income for the year ended December 31, 2010. If the economic downturn continues or a prolonged economic recession occurs in the economy as a whole, borrowers will be less likely to repay their loans as scheduled. Moreover, in many cases the value of real estate or other collateral that secures our loans has been adversely affected by the economic conditions and could continue to be negatively affected. Unlike many larger institutions, we are not able to spread the risks of unfavorable local economic conditions across a large number of diversified economies. A continued economic downturn could, therefore, result in losses that materially and adversely affect our business.

We face strong competition for customers, which could prevent us from obtaining customers and may cause us to pay higher interest rates to attract customers.

The banking business is highly competitive, and we experience competition in our market from many other financial institutions. We compete with commercial banks, credit unions, savings and loan associations, mortgage banking firms, consumer finance companies, securities brokerage firms, insurance companies, money market funds, and other mutual funds, as well as other super-regional, national, and international financial institutions that operate offices in our primary market areas and elsewhere. We compete with these institutions both in attracting deposits and in making loans. In addition, we have to attract our customer base from other existing financial institutions and from new residents. Many of our competitors are well-established, larger financial institutions. These institutions offer some services, such as extensive and established branch networks, that we do not provide. There is a risk that we will not be able to compete successfully with other financial institutions in our market, and that we may have to pay higher interest rates to attract deposits, resulting in reduced profitability. In addition, competitors that are not depository institutions are generally not subject to the extensive regulations that apply to us.

Our FDIC Deposit Insurance premiums have risen significantly in the recent past and may continue to increase in the future as a result of our risk assessment category and increased assessment rates imposed by the FDIC.

As a member institution of the FDIC, we are required to pay quarterly deposit insurance premium assessments to the FDIC. The company's deposit insurance assessments expense totaled $1.0 million for the year ended December 31, 2010. Due to the recent failure of several unaffiliated FDIC insurance depository institutions, and the FDIC's Temporary Liquidity Guarantee Program, the deposit insurance premium assessments paid by all banks has increased. In addition, the new FDIC requirements shift a greater share of any increase in such assessments onto institutions with higher risk profiles. In the fourth quarter of 2009, the FDIC collected prepaid insurance assessments for the three years ending December 31, 2012 in an effort to restore fund balances. We were required to pay approximately $3.0 million in prepaid insurance premiums which is included in other assets at December 31, 2009. At December 31, 2010, the remaining prepaid insurance premium was $1.7 million. Continued increases in this expense would have a material adverse effect on our financial condition.

We have a concentration of credit exposure in commercial real estate and a downturn in commercial real estate could adversely affect our business, financial condition, and results of operations.

As of December 31, 2010, we had approximately $218.3 million in loans outstanding to borrowers whereby the collateral securing the loan was commercial real estate, representing approximately 66.2% of our total loans outstanding as of that date. Approximately 29.2% of this real estate are owner-occupied properties. Commercial real estate loans are generally viewed as having more risk of default than residential real estate loans. They are also typically larger than residential real estate loans and consumer loans and depend on cash flows from the owner's business or the property to service the debt. Cash flows may be affected significantly by general economic conditions, and a downturn in the local economy or in occupancy rates in the local economy where the property is located could increase the likelihood of default. Because our loan portfolio contains a number of commercial real estate loans with relatively large balances, the deterioration of one or a few of these loans could cause a significant increase in our level of non-performing loans. An increase in non-performing loans could result in a loss of earnings from these loans, an increase in the related provision for loan losses and an increase in charge-offs, all of which could have a material adverse effect on our financial condition and results of operations.

Our commercial real estate loans have grown 1.9%, or $4.1 million, since December 31, 2009. The banking regulators are giving commercial real estate lending greater scrutiny, and may require banks with higher levels of commercial real estate loans to implement more stringent underwriting, internal controls, risk management policies and portfolio stress testing, as well as possibly higher levels of allowances for losses and capital levels as a result of commercial real estate lending growth and exposures.

A significant portion of our loan portfolio is secured by real estate, and events that negatively impact the real estate market could hurt our business.

A significant portion of our loan portfolio is secured by real estate. As of December 31, 2010, approximately 91.9% of our loans had real estate as a primary or secondary component of collateral.

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The real estate collateral in each case provides an alternate source of repayment in the event of default by the borrower and may deteriorate in value during the time the credit is extended. A further weakening of the real estate market in our primary market area could result in an increase in the number of borrowers who default on their loans and a reduction in the value of the collateral securing their loans, which in turn could have an adverse effect on our profitability and asset quality. If we are required to liquidate the collateral securing a loan to satisfy the debt during a period of reduced real estate values, our earnings and capital could be adversely affected. Acts of nature, including hurricanes, tornados, earthquakes, fires and floods, which could be exacerbated by potential climate change and may cause uninsured damage and other loss of value to real estate that secures these loans, may also negatively impact our financial condition.

Changes in prevailing interest rates may reduce our profitability.

Our results of operations depend in large part upon the level of our net interest income, which is the difference between interest income from interest- earning assets, such as loans and MBSs, and interest expense on interest-bearing liabilities, such as deposits and other borrowings. Depending on the terms and maturities of our assets and liabilities, we believe it is more likely than not a significant change in interest rates could have a material adverse effect on our profitability. Many factors cause changes in interest rates, including governmental monetary policies and domestic and international economic and political conditions. While we intend to manage the effects of changes in interest rates by adjusting the terms, maturities, and pricing of our assets and liabilities, our efforts may not be effective and our financial condition and results of operations could suffer.

We are dependent on key individuals, and the loss of one or more of these key individuals could curtail our growth and adversely affect our prospects.

Michael C. Crapps, our president and chief executive officer, has extensive and long-standing ties within our primary market area and substantial experience with our operations, and he has contributed significantly to our business. If we lose the services of Mr. Crapps, he would be difficult to replace and our business and development could be materially and adversely affected.

Our success also depends, in part, on our continued ability to attract and retain experienced loan originators, as well as other management personnel. Competition for personnel is intense, and we may not be successful in attracting or retaining qualified personnel. Our failure to compete for these personnel, or the loss of the services of several of such key personnel, could adversely affect our business strategy and seriously harm our business, results of operations, and financial condition.

Because of our participation in the Treasury's CPP, we are subject to several restrictions including restrictions on compensation paid to our executives.

Pursuant to the terms of the CPP Purchase Agreement between us and the Treasury, we adopted certain standards for executive compensation and corporate governance for the period during which the Treasury holds the equity issued pursuant to the CPP Purchase Agreement, including the common stock which may be issued pursuant to the CPP Warrant. These standards generally apply to our Chief Executive Officer, Chief Financial Officer and the three next most highly compensated senior executive officers. The standards include (1) ensuring that incentive compensation for senior executives does not encourage unnecessary and excessive risks that threaten the value of the financial institution; (2) required clawback of any bonus or incentive compensation paid to a senior executive based on statements of earnings, gains or other criteria that are later proven to be materially inaccurate; (3) prohibition on making golden parachute payments to senior executives; and (4) agreement not to deduct for tax purposes executive compensation in excess of $500,000 for each senior executive. In particular, the change to the deductibility limit on executive compensation will likely increase the overall cost of our compensation programs in future periods and may make it more difficult to attract suitable candidates to serve as executive officers.

The Recovery Act has imposed additional and broader compensation restrictions on CPP participants, which restrictions will be implemented by additional regulations. It will require significant time, effort, and resources on our part to ensure compliance, and the evolving regulations regarding compensation may restrict our ability to compete successfully for executive and management talent.

We are subject to extensive regulation that could limit or restrict our activities.

We operate in a highly regulated industry and are subject to examination, supervision, and comprehensive regulation by various regulatory agencies. Our compliance with these regulations is costly and restricts certain of our activities, including payment of dividends, mergers and acquisitions, investments, loans and interest rates charged, interest rates paid on deposits, and locations of offices. We are also subject to capitalization guidelines established by our regulators, which require us to maintain adequate capital to support our growth. In addition to the Formal Agreement, the OCC has separately established the following individual minimum capital ratios for the bank: a Tier 1 leverage capital ratio of at least 8.00%, a Tier 1 risk-based capital ratio of at least 10.00%, and a Total risk-based capital ratio of at least 12.00%. As of December 31, 2010, the bank exceeds each of these ratios and remains "well capitalized."

The laws and regulations applicable to the banking industry could change at any time, and we cannot predict the effects of these changes on our business and profitability. Because government regulation greatly affects the business and financial results of all commercial banks and bank holding companies, our cost of compliance could adversely affect our ability to operate profitably. See also "*Risk Factors Recent negative developments in the financial services industry and U.S. and global credit markets may adversely impact our operations and results.*"

The Sarbanes-Oxley Act of 2002, and the related rules and regulations promulgated by the Securities and Exchange Commission that are now applicable to us, have increased the scope, complexity, and cost of corporate governance, reporting, and disclosure practices. To comply with the Sarbanes-Oxley Act, we have previously hired an outside consultant to assist with our internal audit and internal control functions. We have experienced, and we expect to continue to experience, greater compliance costs, including costs related to internal controls, as a result of the Sarbanes-Oxley Act.

Proposals for further regulation of the financial services industry are continually being introduced in the Congress of the United States of America and the General Assembly of the State of South Carolina. The agencies regulating the financial services industry also periodically adopt changes to their regulations. See Part I, Item 1, "Supervision and Regulation" of this Form 10-K for a summary description of proposed regulations and legislative action that has been introduced and/or adopted over the past two years. It is possible that additional legislative proposals may be adopted or regulatory changes may be made that would have an adverse effect on our business.

We may need to raise additional capital in the future, but that capital may not be available when it is needed.

We are required by regulatory authorities to maintain adequate levels of capital to support our operations. To support our continued growth, we may need to raise additional capital. In addition, we intend to redeem the Series T Preferred Stock that we issued to the Treasury under the CPP before the dividends on the Series T Preferred Stock increase from 5% per annum to 9% per annum in 2014, and we may need to raise additional capital to do so. Our ability to raise additional capital, if needed, will depend in part on conditions in the capital markets at that time, which are outside our control. Accordingly, we cannot assure you of our ability to raise additional capital, if needed, on terms acceptable to us. If we cannot raise additional capital when needed, our ability to further expand our operations through internal growth and acquisitions could be materially impaired. In addition, if we decide to raise additional equity capital, your interest could be diluted.

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Our historical operating results may not be indicative of our future operating results.

We may not be able to sustain our historical rate of growth, and, consequently, our historical results of operations will not necessarily be indicative of our future operations. Various factors, such as economic conditions, regulatory and legislative considerations, and competition, may also impede our ability to expand our market presence. If we experience a significant decrease in our historical rate of growth, our results of operations and financial condition may be adversely affected because a high percentage of our operating costs are fixed expenses.

We may be adversely affected by the soundness of other financial institutions.

Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. We have exposure to many different industries and counterparties, and routinely execute transactions with counterparties in the financial services industry, including commercial banks, brokers and dealers, investment banks, and other institutional clients. Many of these transactions expose us to credit risk in the event of a default by a counterparty or client. In addition, our credit risk may be exacerbated when the collateral held by the bank cannot be realized upon or is liquidated at prices not sufficient to recover the full amount of the credit or derivative exposure due to the bank. Any such losses could have a material adverse affect on our financial condition and results

We will face risks with respect to expansion through acquisitions or mergers.

From time to time we may seek to acquire other financial institutions or parts of those institutions. We may also expand into new markets or lines of business or offer new products or services. These activities would involve a number of risks, including:

- the potential inaccuracy of the estimates and judgments used to evaluate credit, operations, management, and market risks with respect to a target institution;

- the time and costs of evaluating new markets, hiring or retaining experienced local management, and opening new offices and the time lags between these activities and the generation of sufficient assets and deposits to support the costs of the expansion;

- the incurrence and possible impairment of goodwill associated with an acquisition and possible adverse effects on our results of operations; and

- the risk of loss of key employees and customers.

Our underwriting decisions may materially and adversely affect our business.

While we generally underwrite the loans in our portfolio in accordance with our own internal underwriting guidelines and regulatory supervisory guidelines, in certain circumstances we have made loans which exceed either our internal underwriting guidelines, supervisory guidelines, or both. As of December 31, 2010, approximately $12.3 million of our loans, or 21.8% of our bank's regulatory capital, had loan-to-value ratios that exceeded regulatory supervisory guidelines, of which 6 loans totaling approximately $400 thousand had loan-to-value ratios of 100% or more. In addition, supervisory limits on commercial loan to value exceptions are set at 30% of our bank's capital. At December 31, 2010, $10.5 million of our commercial loans, or 18.6% of our bank's regulatory capital, exceeded the supervisory loan to value ratio. The number of loans in our portfolio with loan-to-value ratios in excess of supervisory guidelines, our internal guidelines, or both could increase the risk of delinquencies and defaults in our portfolio.

Our ability to pay cash dividends is limited, and we may be unable to pay future dividends even if we desire to do so.

Our ability to pay cash dividends may be limited by regulatory restrictions, by our bank's ability to pay cash dividends to our holding company and by our need to maintain sufficient capital to support our operations. The ability of our bank to pay cash dividends to our holding company is limited by its obligation to maintain sufficient capital and by other restrictions on its cash dividends that are applicable to national banks and banks that are regulated by the FDIC. If our bank is not permitted to pay cash dividends to our holding company, then we may be unable to pay cash dividends on our common stock. Pursuant to the terms of the Formal Agreement, our bank is currently not permitted to pay cash dividends to our company without the prior consent of the OCC. In addition, the company must currently obtain preapproval of the Federal Reserve Board before paying dividends.

As long as shares of our Series T Preferred Stock are outstanding, no dividends may be paid on our common stock unless all dividends on the Series T Preferred Stock have been paid in full. Additionally, prior to November 21, 2011, so long as the Treasury owns shares of the Series T Preferred Stock, we are not permitted to increase cash dividends on our common stock without the Treasury's consent. The dividends declared on shares of our Series T Preferred Stock will reduce the net income available to common shareholders and our earnings per common share. Additionally, the warrant to purchase our common stock issued to the Treasury, in conjunction with the issuance of the Series T Preferred Stock, may be dilutive to our earnings per share. These restrictions, together with the potentially dilutive impact of the warrant described in the next risk factor, could have a negative effect on the value of our common stock. Moreover, holders of our common stock are entitled to receive dividends only when, and if declared by our board of directors. Although we have historically paid cash dividends on our common stock, we are not required to do so and our board of directors could reduce or eliminate our common stock dividend in the future.

If we are unable to redeem the Series T Preferred Stock after five years, we will be required to make higher dividend payments on this stock, thereby substantially increasing our cost of capital.

If we are unable to redeem the Series T Preferred Stock issued to the Treasury pursuant to the CPP prior to February 15, 2014, the dividend rate will increase substantially on that date, from 5.0% per annum to 9.0% per annum. Depending on our financial condition at the time, this increase in the annual dividend rate on the Series T Preferred Stock could have a material negative effect on our liquidity, our net income available to common shareholders, and our earnings per share.

Legislation or regulatory changes could cause us to seek to repurchase the preferred stock and warrant that we sold to the Treasury pursuant to the CPP.

Legislation that was adopted after we closed on our sale of the Series T Preferred Stock and CPP Warrant on November 21, 2008, altered the terms of our CPP transaction in ways that create additional restrictions, complexity and compliance time and expense. Any legislation or regulations that may be implemented in the future may have a further material impact on the terms of our CPP transaction with the Treasury. We may seek to unwind, in whole or in part, the CPP transaction by repurchasing some or all of the preferred stock and warrant that we sold to the Treasury pursuant to the CPP. If we were to repurchase all or a portion of such preferred stock or warrant, then our capital levels could be materially reduced.

There can be no assurance whether or when the Series T Preferred Stock can be redeemed or whether or when the related Warrant can be repurchased.

Subject to approval of our regulators, we generally have the right to repurchase the shares of Series T Preferred Stock and the Warrant issued to the Treasury in the TARP Transaction. However,

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there can be no assurance as to when the Series T Preferred Stock and the Warrant will be repurchased, if at all. As a result, we will remain subject to the uncertainty of additional future changes to the CPP, which could put us at a competitive disadvantage. Until such time as the Series T Preferred Stock and the Warrant are repurchased, we will remain subject to the terms and conditions of those instruments, which, among other things, require us to obtain regulatory approval to repurchase or redeem our Common Stock or our other preferred stock or increase the annual aggregate dividends on our Common Stock over $0.32 per share, except in limited circumstances.

The Series T Preferred Stock impacts net income available to our common shareholders and earnings per common share, and the warrant we issued to the Treasury may be dilutive to holders of our common stock.

The dividends declared on our Series T Preferred Stock issued to the Treasury pursuant to the CPP will reduce the net income available to common shareholders and our earnings per common share. The Series T Preferred Stock will also receive preferential treatment in the event of liquidation, dissolution or winding up of First Community Corporation. Additionally, the ownership interest of the existing holders of our common stock will be diluted to the extent the warrant we issued to the Treasury in conjunction with the sale to the Treasury of the Series T Preferred Stock is exercised. The shares of common stock underlying the warrant represent approximately 5.7% of the shares of our common stock outstanding as of March 31, 2010 (including the shares issuable upon exercise of the warrant in total shares outstanding). Although the Treasury has agreed not to vote any of the shares of common stock it receives upon exercise of the warrant, a transferee of any portion of the warrant or of any shares of common stock acquired upon exercise of the warrant is not bound by this restriction.

Holders of the Series T Preferred Stock have rights that are senior to those of our common shareholders.

The Series T Preferred Stock that we issued to the Treasury on November 21, 2008 is senior to our shares of common stock and holders of the Series T Preferred Stock have certain rights and preferences that are senior to holders of our common stock. The Series T Preferred Stock ranks senior to our common stock and all other equity securities of ours designated as ranking junior to the Series T Preferred Stock. So long as any shares of the Series T Preferred Stock remain outstanding, unless all accrued and unpaid dividends for all prior dividend periods have been paid or are contemporaneously declared and paid in full, no dividend whatsoever shall be paid or declared on our common stock or other junior stock, other than a dividend payable solely in common stock. We and our subsidiary also generally may not purchase, redeem or otherwise acquire for consideration any shares of our common stock or other junior stock unless we have paid in full all accrued dividends on the Series T Preferred Stock for all prior dividend periods, other than in certain circumstances described more fully below. Furthermore, the Series T Preferred Stock is entitled to a liquidation preference over shares of our common stock in the event of our liquidation, dissolution or winding up.

Holders of the Series T Preferred Stock may, under certain circumstances, have the right to elect two directors to our board of directors.

In the event that we fail to pay dividends on the Series T Preferred Stock for an aggregate of six quarterly dividend periods or more (whether or not consecutive), the authorized number of directors then constituting our board of directors will be increased by two. Holders of the Series T Preferred Stock, together with the holders of any outstanding parity stock with like voting rights, referred to as voting parity stock, voting as a single class, will be entitled to elect the two additional members of our board of directors, referred to as the preferred stock directors, at the next annual meeting (or at a special meeting called for the purpose of electing the preferred stock directors prior to the next annual meeting) and at each subsequent annual meeting until all accrued and unpaid dividends for all past dividend periods have been paid in full.

Holders of the Series T Preferred Stock have limited voting rights.

Except as otherwise required by law and in connection with the election of directors to our board of directors in the event that we fail to pay dividends on the Series T Preferred Stock for an aggregate of at least six quarterly dividend periods (whether or not consecutive), holders of the Series T Preferred Stock have limited voting rights. So long as shares of the Series T Preferred Stock are outstanding, in addition to any other vote or consent of shareholders required by law or our amended and restated articles of incorporation, the vote or consent of holders owning at least $66^2/_3$% of the shares of Series T Preferred Stock outstanding is required for (1) any authorization or issuance of shares ranking senior to the Series T Preferred Stock; (2) any amendment to the rights of the Series T Preferred Stock so as to adversely affect the rights, preferences, privileges or voting power of the Series T Preferred Stock; or (3) consummation of any merger, share exchange or similar transaction unless the shares of Series T Preferred Stock remain outstanding, or if we are not the surviving entity in such transaction, are converted into or exchanged for preference securities of the surviving entity and the shares of Series T Preferred Stock remaining outstanding or such preference securities have such rights, preferences, privileges and voting power as are not materially less favorable to the holders than the rights, preferences, privileges and voting power of the shares of Series T Preferred Stock.

We are exposed to the possibility of technology failure and a disruption in our operations may adversely affect our business.

We rely on our computer systems and the technology of outside service providers. Our daily operations depend on the operational effectiveness of their technology. We rely on our systems to accurately track and record our assets and liabilities. If our computer systems or outside technology sources become unreliable, fail, or experience a breach of security, our ability to maintain accurate financial records may be impaired, which could materially affect our business operations and financial condition. In addition, a disruption in our operations resulting from failure of transportation and telecommunication systems, loss of power, interruption of other utilities, natural disaster, fire, global climate changes, computer hacking or viruses, failure of technology, terrorist activity or the domestic and foreign response to such activity or other events outside of our control could have an adverse impact on the financial services industry as a whole and/or on our business. Our business recovery plan may not be adequate and may not prevent significant interruptions of our operations or substantial losses.

Item 1B. Unresolved Staff Comments.

Not applicable.

Item 2. Properties.

Lexington Property. The principal place of business of both the company and our bank is located at 5455 Sunset Boulevard, Lexington, South Carolina 29072. This site, which is also the bank's main office branch, is a 2.29 acre plot of land. The site was purchased for $576 thousand and the building costs were approximately $1.0 million. The branch operates in an 8,500 square foot facility located on this site.

In October 2000, the bank acquired an additional 2.0 acres adjacent to the existing facility for approximately $300 thousand. This site was designed to allow for a 24,000 to 48,000 square foot facility at some future date. The bank completed construction and occupied the 28,000 square foot administrative center in July 2006. The total construction cost for the building was approximately $3.4 million. The Lexington property is owned by the bank.

Forest Acres Property. We operate a branch office facility at 4404 Forest Drive, Columbia, South Carolina 29206. The Forest Acres site is .71 acres. The banking facility is approximately 4,000 square

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feet with a total cost of land and facility of approximately $920 thousand. This property is owned by the bank.

Irmo Property. We operate a branch office facility at 1030 Lake Murray Boulevard, Irmo, South Carolina 29063. The Irmo site is approximately one acre. The banking facility is approximately 3,200 square feet with a total cost of land and facility of approximately $1.1 million. This property is owned by the bank.

Cayce/West Columbia Property. We operate a branch office facility at 506 Meeting Street, West Columbia, South Carolina, 29169. The Cayce/West Columbia site is approximately 1.25 acres. The banking facility is approximately 3,800 square feet with a total cost of land and facility of approximately $935 thousand. This property is owned by the bank.

Gilbert Property. We operate a branch office at 4325 Augusta Highway Gilbert, South Carolina 29054. The facility is an approximate 3,000 square foot facility located on an approximate one acre lot. The total cost of the land and facility was approximately $768 thousand. This property is owned by the bank.

Chapin Office. We operate a branch office facility at 137 Amicks Ferry Rd., Chapin, South Carolina 29036. The facility is approximately 3,000 square feet and is located on a three acre lot. The total cost of the facility and land was approximately $1.3 million. This property is owned by the bank.

Northeast Columbia. We operate a branch office facility at 9822 Two Notch Rd., Columbia, South Carolina 29223. The facility is approximately 3,000 square feet and is located on a one acre lot. The total cost of the facility and land was approximately $1.2 million. This property is owned by the bank.

Prosperity Property. We operate a branch office at 101 N. Wheeler Avenue, Prosperity, South Carolina 29127. This office was acquired in connection with the DutchFork merger. The banking facility is approximately 1,300 square feet and is located on a .31 acre lot. The total cost of the facility and land was approximately $175 thousand. This property is owned by the bank.

Wilson Road. We operate a branch office at 1735 Wilson Road, Newberry, South Carolina 29108. The banking office was acquired in connection with the DutchFork merger. This banking facility is approximately 12,000 square feet and is located on a 1.56 acre lot. Adjacent to the branch facility is a 13,000 square foot facility which was formerly utilized as the DutchFork operations center. The total cost of the facility and land was approximately $3.3 million. This property is owned by the bank.

Redbank Property. We operate a branch office facility at 1449 Two Notch Road, Lexington, South Carolina 29073. This branch opened for operation on February 3, 2005. The facility is approximately 3,000 square feet and is located on a one acre lot. The total cost of the facility and land was approximately $1.3 million. This property is owned by the bank.

Camden Property. We operate a branch office facility at 631 DeKalb Street, Camden, South Carolina 29020. This office was acquired in connection with the DeKalb merger. The facility is approximately 11,247 square feet and is located on a two acre lot. The total cost of the facility and land was approximately $2.2 million. This property is owned by the bank.

Highway 219 Property. A .61 acre lot located on highway 219 in Newberry County was acquired in connection with the DutchFork merger. This lot may be used for a future branch location but no definitive plans have been made. The cost of the lot was $430 thousand. This property is owned by the bank.

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Item 3. Legal Proceedings.

Neither the company nor the bank is a party to, nor is any of their property the subject of, any material pending legal proceedings related to the business of the company or the bank.

Item 4. (Removed and Reserved.)

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PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities.

As of March 29, 2011, there were approximately 1,573 shareholders of record of our common stock. On January 15, 2003, our stock began trading on The NASDAQ Capital Market under the trading symbol of "FCCO." Prior to January 15, 2003, our stock was quoted on the OTC Bulletin Board under the trading symbol "FCCO.OB." The following table sets forth the high and low sales price information as reported by NASDAQ in 2010 and 2009, and the dividends per share declared on our common stock in each such quarter. All information has been adjusted for any stock splits and stock dividends effected during the periods presented.

	High	Low	Dividends
2010			
Quarter ended March 31, 2010	$ 6.50	$ 5.75	$ 0.04
Quarter ended June 30, 2010	$ 6.75	$ 5.55	$ 0.04
Quarter ended September 30, 2010	$ 6.05	$ 5.00	$ 0.04
Quarter ended December 31, 2010	$ 5.78	$ 5.00	$ 0.04
2009			
Quarter ended March 31, 2009	$ 7.82	$ 5.25	$ 0.08
Quarter ended June 30, 2009	$ 8.00	$ 6.25	$ 0.08
Quarter ended September 30, 2009	$ 7.25	$ 5.49	$ 0.04
Quarter ended December 31, 2009	$ 7.00	$ 5.60	$ 0.04

Notwithstanding the foregoing, the future dividend policy of the company is subject to the discretion of the board of directors and will depend upon a number of factors, including future earnings, financial condition, cash requirements, and general business conditions. Our ability to pay dividends is generally limited by the ability of our subsidiary bank to pay dividends to us. As a national bank, our bank may only pay dividends out of its net profits then on hand, after deducting expenses, including losses and bad debts. In addition, the bank is prohibited from declaring a dividend on its shares of common stock until its surplus equals its stated capital, unless there has been transferred to surplus no less than one-tenth of the bank's net profits of the preceding two consecutive half-year periods (in the case of an annual dividend). The approval of the OCC will be required if the total of all dividends declared in any calendar year by the bank exceeds the bank's net profits to date, as defined, for that year combined with its retained net profits for the preceding two years less any required transfers to surplus. In addition, pursuant to the terms of the Formal Agreement, the bank is currently prohibited from paying dividends to the company without the prior approval of the OCC. The OCC also has the authority under federal law to enjoin a national bank from engaging in what in its opinion constitutes an unsafe or unsound practice in conducting its business, including the payment of a dividend under certain circumstances.

We are currently prohibited from declaring or paying dividends without the prior consent of the Federal Reserve. In addition, as long as shares of our Series T Preferred Stock are outstanding, no dividends may be paid on our common stock unless all dividends on the Series T Preferred Stock have been paid in full. Additionally, prior to November 21, 2011, so long as the Treasury owns shares of the Series T Preferred Stock, we are not permitted to increase cash dividends on our common stock above $0.08 per quarter without the Treasury's consent.

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Item 6. Selected Financial Data

(Dollars in thousands except per share amounts)	As of or For the Years Ended December 31, 2010	2009	2008	2007	2006
Balance Sheet Data:					
Total Assets	$ 599,023	$ 605,827	$ 650,233	$ 565,613	$ 548,056
Loans	329,954	344,187	332,964	310,028	275,189
Deposits	455,344	449,576	423,798	405,855	414,941
Total common shareholders' equity	30,762	30,501	57,306	63,996	63,208
Total shareholders' equity	41,797	41,440	68,156	63,996	63,208
Average shares outstanding, basic	3,262	3,252	3,203	3,234	3,097
Average shares outstanding, diluted	3,262	3,252	3,203	3,284	3,174
Results of Operations:					
Interest income	$ 27,511	$ 30,981	$ 33,008	$ 30,955	$ 27,245
Interest expense	9,374	13,104	15,810	15,665	12,922
Net interest income	18,137	17,877	17,198	15,290	14,323
Provision for loan losses	1,878	3,103	2,129	492	528
Net interest income after provision for loan losses	16,259	14,774	15,069	14,798	13,795
Non-interest income (loss)	3,017	3,543	(10,056)	4,968	4,470
Securities gains (losses)	827	1,489	(28)	49	(69)
Non-interest expenses	17,684	16,580	15,539	14,125	13,243
Impairment of goodwill		27,761			
Income (loss) before taxes	2,419	(24,535)	(10,554)	5,690	4,953
Income tax expense (benefit)	565	696	(3,761)	1,725	1,452
Net income (loss)	1,854	(25,231)	(6,793)	3,965	3,501
Amortization of warrants	96	89	9		
Preferred stock dividends, including discount accretion	568	567	62		
Net income (loss) available to common shareholders	1,190	(25,887)	(6,864)	3,965	3,501
Per Share Data:					
Basic earnings (loss) per common	$ 0.36	$ (7.95)	$ (2.14)	$ 1.23	$ 1.13

share					
Diluted earnings (loss) per common share	0.36	(7.95)	(2.14)	1.21	1.10
Book value at period end	9.41	9.38	17.76	19.93	19.36
Tangible book value at period end	9.14	8.92	8.50	10.67	10.05
Dividends per common share	0.16	0.24	0.32	0.27	0.23
Asset Quality Ratios:					
Non-performing assets to total assets(4)	2.20%	1.38%	0.39%	0.22%	0.09%
Non-performing loans to period end loans	1.90%	1.50%	0.54%	0.36%	0.17%
Net charge-offs to average loans	0.54%	0.84%	0.34%	0.06%	0.13%
Allowance for loan losses to period-end total loans	1.49%	1.41%	1.38%	1.14%	1.17%
Allowance for loan losses to non-performing assets	37.39%	58.21%	178.53%	286.06%	688.44%

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(Dollars in thousands except per share amounts)	2010	2009	2008	2007	2006
	As of or For the Years Ended December 31,				
Selected Ratios:					
Return on average assets:					
GAAP earnings (loss)	0.20%	(3.90)%	(1.10)%	0.72%	0.68%
Operating earnings(3)	0.20%	.39%	0.48%	0.72%	0.68%
Return on average common equity:					
GAAP earnings (loss)	3.73%	(49.66)%	(11.11)%	6.20%	5.54%
Operating earnings (loss)(3)	3.73%	4.98%	4.82%	6.20%	5.54%
Return on average tangible common equity:					
GAAP earnings (loss)	3.87%	(89.13)%	(21.60)%	11.83%	12.68%
Operating earnings (loss)	3.87%	8.94%	9.37%	11.83%	12.68%
Efficiency Ratio(1)	73.07%	73.47%	72.74%	68.41%	69.11%
Noninterest income to operating revenue(2)	17.48%	21.97%	19.78%	24.71%	23.50%
Net interest margin	3.26%	3.10%	3.16%	3.21%	3.27%
Equity to assets	6.97%	6.84%	10.48%	11.31%	11.53%
Tangible common shareholders' equity to tangible assets	5.00%	4.80%	4.42%	6.39%	6.34%
Tier 1 risk-based capital	13.73%	12.41%	12.58%	13.66%	13.48%
Total risk-based capital	14.99%	13.56%	13.73%	14.61%	14.40%
Leverage	8.79%	8.41%	8.28%	9.31%	9.29%
Average loans to average deposits	73.53%	76.99%	75.45%	73.45%	64.83%

(1) The efficiency ratio is a key performance indicator in our industry. The ratio is computed by dividing non-interest expense, less goodwill impairment, by the sum of net interest income on a tax equivalent basis and non-interest income, net of any securities gains or losses and OTTI on securities. It is a measure of the relationship between operating expenses and earnings.

(2) Operating revenue is defined as net interest income plus noninterest income, excluding OTTI related to the write-down of FHLMC preferred shares in 2008.

(3) Constitutes a non-GAAP financial measure. Please see "Reconciliation of Non-GAAP Financial Measures" below.

(4) Includes non-accrual loans, loans > 90 days delinquent and still accruing interest and OREO.

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Reconciliations

The following is a reconciliation for the five years ended December 31, 2010, of net income (loss) as reported for generally accepted accounting principles ("GAAP") and the non-GAAP measure referred to throughout our discussion of "operating earnings."

	December 31,				
(Dollars in thousands)	**2010**	**2009**	**2008**	**2007**	**2006**
Net income (loss), As Reported (GAAP)	$ 1,854	$ (25,231)	$ (6,793)	$ 3,965	$ 3,501
Add: Income tax expense (benefit)	565	696	(3,761)	1,725	1,452
	2,419	(24,535)	(10,554)	5,690	4,953
Non-operating items:					
Goodwill impairment charge		27,761			
Other-than-temporary-impairment on FHLMC preferred shares			14,325		
Pre-tax operating earnings	2,419	3,226	3,771	5,690	4,953
Related income tax expense	565	696	825	1,725	1,452
Operating earnings, (net income, excluding non operating items)	$ 1,854	$ 2,530	$ 2,946	$ 3,965	$ 3,501

The following is a reconciliation for the five years ended December 31, 2010, of non-interest income (loss) as reported for GAAP and the non-GAAP measure referred to throughout our discussion regarding non-interest income (loss).

(Dollars in thousands)	**2010**	**2009**	**2008**	**2007**	**2006**
Non-interest income (loss), as reported (GAAP)	$ 3,844	$ 5,032	$ (10,084)	$ 5,017	$ 4,401
Non-operating items:					
Other-than-temporary-impairment charge			14,325		
Operating non-interest income	$ 3,844	$ 5,032	$ 4,241	$ 5,017	$ 4,401

The following is a reconciliation for the five years ended December 31, 2010, of non-interest expense as reported for GAAP and the non-GAAP measure referred to throughout our discussion regarding non-interest expense.

(Dollars in thousands)	**2010**	**2009**	**2008**	**2007**	**2006**
Non-interest expense, as reported (GAAP)	$ 17,684	$ 44,341	$ 15,539	$ 14,125	$ 13,243
Non-operating items:					
Impairment of goodwill		27,761			
Operating non-interest expense	$ 17,684	$ 16,580	$ 15,539	$ 14,125	$ 13,243

Our management believes that the non-GAAP measures above are useful because they enhance the ability of investors and management to evaluate and compare our operating results from period to period in a meaningful manner. These non-GAAP measures should not be considered as an alternative to any measure of performance as promulgated under GAAP, and investors should consider the OTTI charges in the second and third quarter of 2008 when assessing the performance of the company. Non-GAAP measures have limitations as analytical tools, and investors should not consider them in isolation or as a substitute for analysis of the company's results as reported under GAAP.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Overview

First Community Corporation is a one bank holding company headquartered in Lexington, South Carolina. We operate from our main office in Lexington, South Carolina and our 11 full-service offices located in Lexington (two), Forest Acres, Irmo, Cayce-West Columbia, Gilbert, Chapin, Northeast Columbia, Prosperity, Newberry and Camden. During the second quarter of 2006, we completed our acquisition of DeKalb Bankshares, Inc., the holding company for The Bank of Camden. The merger added one office in Kershaw County located in the Midlands of South Carolina. During the fourth quarter of 2004, we completed our first acquisition of another financial institution when we merged with DutchFork Bancshares, Inc., the holding company for Newberry Federal Savings Bank. The merger added three offices in Newberry County. In 2007, our College Street office in Newberry was consolidated with our Wilson Road Office in Newberry. We engage in a general commercial and retail banking business characterized by personalized service and local decision making, emphasizing the banking needs of small to medium-sized businesses, professional concerns and individuals.

The following discussion describes our results of operations for 2010 as compared to 2009 as compared to 2008, and also analyzes our financial condition as of December 31, 2010 as compared to December 31, 2009. Like most community banks, we derive most of our income from interest we receive on our loans and investments. A primary source of funds for making these loans and investments is our deposits, on which we pay interest. Consequently, one of the key measures of our success is our amount of net interest income, or the difference between the income on our interest-earning assets, such as loans and investments, and the expense on our interest-bearing liabilities, such as deposits. Another key measure is the spread between the yield we earn on these interest-earning assets and the rate we pay on our interest-bearing liabilities.

We have included a number of tables to assist in our description of these measures. For example, the "Average Balances" table shows the average balance during 2010, 2009 and 2008 of each category of our assets and liabilities, as well as the yield we earned or the rate we paid with respect to each category. A review of this table shows that our loans typically provide higher interest yields than do other types of interest earning assets, which is why we intend to channel a substantial percentage of our earning assets into our loan portfolio. Similarly, the "Rate/Volume Analysis" table helps demonstrate the impact of changing interest rates and changing volume of assets and liabilities during the years shown. We also track the sensitivity of our various categories of assets and liabilities to changes in interest rates, and we have included a "Sensitivity Analysis Table" to help explain this. Finally, we have included a number of tables that provide detail about our investment securities, our loans, and our deposits and other borrowings.

There are risks inherent in all loans, so we maintain an allowance for loan losses to absorb probable losses on existing loans that may become uncollectible. We establish and maintain this allowance by charging a provision for loan losses against our operating earnings. In the following section we have included a detailed discussion of this process, as well as several tables describing our allowance for loan losses and the allocation of this allowance among our various categories of loans.

In addition to earning interest on our loans and investments, we earn income through fees and other expenses we charge to our customers. We describe the various components of this noninterest income, as well as our noninterest expense, in the following discussion. The discussion and analysis also identifies significant factors that have affected our financial position and operating results during the periods included in the accompanying financial statements. We encourage you to read this discussion and analysis in conjunction with the financial statements and the related notes and the other statistical information also included in this report.

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On October 14, 2008, the Treasury announced the CPP under the EESA, pursuant to which the Treasury could make senior preferred stock investments in participating financial institutions that qualifies as Tier I capital. Based on our risk-weighted assets as of September 30, 2008, we were eligible to issue up to $11.3 million in new senior preferred stock under the program. On November 21, 2008, as part of the CPP established by the Treasury under the EESA, First Community Corporation entered into the CPP Purchase Agreement with the Treasury dated November 21, 2008 pursuant to which we issued and sold to the Treasury (i) the Series T Preferred Stock and (ii) the CPP Warrant, for an aggregate purchase price of $11.3 million in cash. The proceeds from this offering qualify as Tier 1 capital under the regulatory capital guidelines.

Cumulative dividends on the Series T Preferred Stock accrue on the liquidation preference at a rate of 5% per annum for the first five years, and at a rate of 9% per annum thereafter, but will be paid only if, as, and when declared by the company's board of directors. The Series T Preferred Stock has no maturity date and ranks senior to the common stock with respect to the payment of dividends and distributions and amounts payable upon liquidation, dissolution and winding up of the company. The Series T Preferred Stock generally is non-voting.

Under the terms of the agreement the company may redeem the Series T Preferred Stock at par after February 15, 2012. Prior to this date, the company may redeem the Series T Preferred Stock at par if (i) the company has raised aggregate gross proceeds in one or more Qualified Equity Offerings (as defined in the CPP Purchase Agreement) in excess of approximately $2.8 million, and (ii) the aggregate redemption price does not exceed the aggregate net proceeds from such Qualified Equity Offerings. The Recovery Act signed by the President on February 17, 2009 amended the terms of the agreement and allows the company to redeem the Series T Preferred Stock prior to February 15, 2012. Any redemption is subject to the consent of the Board of Governors of the Federal Reserve System.

Recent Regulatory Development

On April 6, 2010, the bank entered into the Formal Agreement with the OCC, our primary bank regulator. The Formal Agreement is based on the findings of the OCC during a 2009 on-site examination of the bank. As reflected in the Formal Agreement, the OCC's primary concern with the bank is driven by the rating agencies downgrades of non-agency mortgage backed securities (MBS) in its investment portfolio. These securities, purchased in 2004 through 2008, were all rated AAA by the rating agencies at the time of purchase; however, they have been impacted by the economic recession and the stress on the residential housing sector. These ratings do not reflect the discounted purchase price paid by the bank. They only reflect their analysis of the performance of the security overall, and therefore, a downgrade does not capture the risk of loss to the bank. The Formal Agreement did not require any adjustment to the bank's balance sheet or income statement; nor did it change the Bank's "well capitalized" status. The OCC has, however, separately established the following individual minimum capital ratios for the bank: a Tier 1 leverage capital ratio of at least 8.00%, a Tier 1 risk-based capital ratio of at least 10.00%, and a Total risk-based capital ratio of at least 12.00%. As of December 31, 2010, the bank exceeds each of these ratios and remains "well capitalized."

The Board of Directors has appointed an independent compliance committee made up of directors to monitor and report on compliance with the terms of the Formal Agreement. The bank intends to take all actions necessary to enable it to comply with the requirements of the Formal Agreement, and as of the date hereof management has submitted all documentation required as of this date to the OCC. There can be no assurance that the bank will be able to comply fully with the provisions of the Formal Agreement, and the determination of our compliance will be made by the OCC. However, management believes the bank is currently in compliance with all provisions of the Formal Agreement. Failure to meet the requirements of the Formal Agreement could result in additional regulatory requirements, which could result in regulators taking additional enforcement actions against the bank.

Critical Accounting Policies

We have adopted various accounting policies that govern the application of accounting principles generally accepted in the United States and with general practices within the banking industry in the preparation of our financial statements. Our significant accounting policies are described in the notes to our consolidated financial statements in this report.

Certain accounting policies involve significant judgments and assumptions by us that have a material impact on the carrying value of certain assets and liabilities. We consider these accounting policies to be critical accounting policies. The judgment and assumptions we use are based on historical experience and other factors, which we believe to be reasonable under the circumstances. Because of the nature of the judgment and assumptions we make, actual results could differ from these judgments and estimates that could have a material impact on the carrying values of our assets and liabilities and our results of operations.

We believe the allowance for loan losses is the critical accounting policy that requires the most significant judgment and estimates used in preparation of our consolidated financial statements. Some of the more critical judgments supporting the amount of our allowance for loan losses include judgments about the credit worthiness of borrowers, the estimated value of the underlying collateral, the assumptions about cash flow, determination of loss factors for estimating credit losses, the impact of current events, and conditions, and other factors impacting the level of probable inherent losses. Under different conditions or using different assumptions, the actual amount of credit losses incurred by us may be different from management's estimates provided in our consolidated financial statements. Refer to the portion of this discussion that addresses our allowance for loan losses for a more complete discussion of our processes and methodology for determining our allowance for loan losses.

The evaluation and recognition of other-than-temporary impairment ("OTTI") on certain investments including our private label mortgage-backed securities and other corporate debt security holdings requires significant judgment and estimates. Some of the more critical judgments supporting the evaluation of OTTI include projected cash flows including prepayment assumptions, default rates and severities of losses on the underlying collateral within the security. Under different conditions or utilizing different assumptions, the actual OTTI recognized by us may be different from the actual amounts recognized in our consolidated financial statements. See Note 5 to the financial statements for the disclosure of certain of the assumptions used as well as OTTI recognized in the financial statements during the years ended December 31, 2010, 2009 and 2008.

Results of Operations

Our net income was $1.9 million, or $0.36 diluted earnings per common share, for the year ended December 31, 2010, as compared to net loss of $25.2 million, or $7.95 diluted loss per common share, for the year ended December 31, 2009, and a net loss of $6.8 million, or $2.14 diluted loss per common share, for the year ended December 31, 2008.During the year ended December 31, 2010, we returned to profitability after two years of net losses which were primarily a result of two specific transactions one occurring in 2009 and one in 2008 each of which are discussed in the following paragraphs below. During the year ended December 31, 2010, we were able to improve our net interest income and the related net interest margin. We continued to control the growth in assets by reducing funding from brokered certificates of deposits and other borrowings. As a result of the continued slow economic recovery, loan demand remained very weak throughout 2010. Loans decreased by $14.2 million at December 31, 2010 as compared to December 31, 2009. Average loan balances were relatively flat during 2010 at $337.1 million as compared to $337.7 million in 2009.

During the year ended December 31, 2009, we recognized a non-cash goodwill impairment charge of $27.8 million, or $8.51 per diluted share, that represented the complete write-off of our goodwill intangible. Goodwill resulted from business acquisitions and represented the value attributable to

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unidentifiable intangible elements in the businesses acquired. The analysis and valuation which was performed in the third quarter 2009 resulted in our determination that goodwill was impaired. This determination was reflective of the impact of the then and ongoing economic environment and its effect on the banking industry and our company. The calculation of fair value as part of the goodwill impairment test is subject to significant management judgment and estimates. Industry-wide, market capitalization and acquisition multiples had significantly declined since 2004 and 2006, which are the dates of the acquisition of Dutchfork Bankshares and DeKalb Bancshares, respectively. Our company experienced the same trend, with a decline in its market price per share and an extended period of time trading at a discount to book value and tangible book value. This non-cash charge represented the accounting recognition of the events. Given the non-cash nature of a goodwill charge, this non-interest expense item had no adverse impact upon our regulatory capital, liquidity position, operating performance or our prospects for future earnings. There was no tax benefit recognized as a result of this goodwill impairment charge.

The net loss for the year ended December 31, 2008 included a charge to recognize an OTTI in the amount of $14.3 million on our investment in a preferred stock issue of Freddie Mac (a GSE) reflecting a write-down of substantially all of its carrying value. During the second quarter of 2008, we made a decision to recognize an unrealized mark-to-market loss on the security that at that time was rated investment grade in the amount of $6.2 million as an OTTI based on the significant decline in the market value of the security caused by potential deterioration of Freddie Mac's financial condition, and the then current lack of clarity about the impact of an announced plan (which was approved by the House and Senate and signed into law by the President). That plan provided support for Freddie Mac as well as other GSEs. On September 7, 2008, the Secretary of the Treasury announced a decision to place Freddie Mac into conservatorship and as part of that decision the dividend payments on existing preferred shares would be terminated for an unspecified period of time. As a result of that decision we took an additional $8.1 million OTTI charge in the third quarter of 2008 to write off substantially all of the remaining investment in this Freddie Mac security. The preferred stock issue was purchased in 2003 and acquired by First Community Corporation in the 2004 merger with Dutchfork Bankshares.

As noted above in Item 6 under "Reconciliations," our operating earnings were $1.9 million, or $0.36 per diluted common share, for 2010 as compared to $2.5 million, or $0.78 diluted earnings per common share, for 2009. Net interest income increased by $260 thousand in 2010 from $17.9 million in 2009 to $18.1 million in 2010. The increase in net interest income is primarily due to the increase in the net interest margin in 2010 as compared to 2009. The impact of the improvement in net interest margin was somewhat offset by a decrease in average earning assets of $20.8 million from $576.8 million during 2009 to $556.0 million in 2010. The net interest margin, on a tax equivalent basis, during 2010 was 3.28% as compared to 3.12% during 2009. Net interest spread, the difference between the yield on earning assets and the rate paid on interest-bearing liabilities, was 2.80% in 2009 as compared to 3.01% in 2010. See below under "Net Interest Income" and "Market Risk and Interest Rate Sensitivity" for a further discussion about the effect of the increase in net interest margin. The provision for loan losses was $3.1 million in 2009 as compared to $1.9 million in 2010. Non-interest income was $3.8 million in 2010 as compared to $5.0 million in 2009. This decrease is primarily due to a negative fair value adjustment on an interest rate swap contract, higher other-than-temporary-impairment charges, and less gains on sales of investments in 2010 as compared to 2009. Operating non-interest expense (see "Reconciliation" above) increased to $17.7 million in 2010 as compared to $16.6 million in 2009. As discussed below under "Non-interest income and expense" the increase is primarily attributable to increases in salary and benefits of $680 thousand and $622 thousand in other real estate expenses in 2010 as compared to 2009.

Our operating earnings (see "Reconciliation" above) were $2.5 million, or $0.78 per diluted common share, for 2009 as compared to $2.9 million, or $0.92 diluted earnings per common share, for 2008. Net interest income increased by $679 thousand in 2009 from $17.2 million in 2008 to

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$17.9 million in 2009. The increase in net interest income is primarily due to the increase in the level of average earning assets. Average earning assets equaled $543.7 million during 2008 as compared to $576.8 million during 2009. The effect of the increase in earning assets was offset by a 9 basis point decrease in the net interest margin from 3.21% during 2008 to 3.12% during 2009 on a tax equivalent basis. Net interest spread, the difference between the yield on earning assets and the rate paid on interest-bearing liabilities, was 2.78% in 2008 as compared to 2.80% in 2009. The provision for loan losses was $2.1 million in 2008 as compared to $3.1 million in 2009. Non-interest income, excluding the FHLMC OTTI charge of $14.3 million, was $4.2 million in 2008 as compared to $5.0 million in 2009. This increase is primarily due to a negative fair value adjustment on interest rate contracts of $560 thousand in 2008 as compared to a positive adjustment of $7 thousand in 2009. Operating non-interest expense (see "Reconciliation" above) increased to $16.6 million in 2009 as compared to $15.5 million in 2008. This increase is primarily attributable to a substantial increase in the FDIC/FICO premiums from $267 thousand in 2008 to $1.1 million in 2009.

Net Interest Income

Net interest income is our primary source of revenue. Net interest income is the difference between income earned on assets and interest paid on deposits and borrowings used to support such assets. Net interest income is determined by the rates earned on our interest-earning assets and the rates paid on our interest-bearing liabilities, the relative amounts of interest-earning assets and interest-bearing liabilities, and the degree of mismatch and the maturity and repricing characteristics of its interest-earning assets and interest-bearing liabilities.

Net interest income totaled $18.1 million in 2010, $17.9 million in 2009 and $17.2 million in 2008. The yield on earning assets was 4.95%, 5.37%, and 6.07% in 2010, 2009 and 2008, respectively. The rate paid on interest-bearing liabilities was 1.94%, 2.57%, and 3.29% in 2010, 2009, and 2008, respectively. The fully taxable equivalent net interest margin was 3.28% in 2010, 3.12% in 2009 and 3.21% in 2008. Our loan to deposit ratio on average during 2010 was 73.5%, as compared to 77.0% during 2009 and 75.5% during 2008. Loans typically provide a higher yield than other types of earning assets and thus one of our goals is to grow the loan portfolio as a percentage of earning assets which should improve the overall yield on earning assets and the net interest margin. At December 31, 2010, the loan to deposit ratio was 72.5%.

The net interest margin improved in 2010 as compared to 2009 after two years of declining margins in 2009 and 2008. Starting in early 2008 and continuing through 2010, interest rates have been at historic lows. The yield on earning assets decreased by 42 basis points and our cost of funds decreased by 63 basis points in 2010 as compared to 2009. This resulted in an increase in our net interest spread of 21 basis points in 2010 as compared to 2009. Our average borrowings and time deposits, which are typically the higher costing funding source, decreased $38.8 million and $10.3 million, respectively, in 2010 as compared to 2009. During the same period our average transaction accounts (interest and non-interest bearing, money market accounts and savings deposits increased by $24.3 million. This change in the mix of funding sources contributed to the increase in our margin between the two periods. Throughout 2010, time deposits and borrowed funds represented 70.3% of our total interest bearing funding sources and in 2009 these balances represented 76.4% of our interest bearing funding sources.

In comparing 2009 to 2008, the yield on earning assets decreased by 70 basis points and our cost of funds decreased by 72 basis points in 2009 as compared to 2008. This resulted in an increase in our net interest spread of 2 basis points in 2009 as compared to 2008. Despite this, our net interest margin decreased 6 basis points as a slightly higher percentage of our average earning assets (volume) were funded by interest bearing liabilities (volume) in 2009 as compared to 2008. In addition, a slight change in the mix of funding sources in 2009 as compared to 2008, contributed to the decline in our margin. Throughout 2008, time deposits and borrowed funds represented 75.4% of our total interest bearing

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funding sources and in 2009 these balances represented 76.4% of our interest bearing funding sources. As previously stated, these sources of funding are typically higher cost funds than alternative sources.

Average Balances, Income Expenses and Rates. The following table depicts, for the periods indicated, certain information related to our average balance sheet and our average yields on assets and average costs of liabilities. Such yields are derived by dividing income or expense by the average balance of the corresponding assets or liabilities. Average balances have been derived from daily averages.

	Year ended December 31,								
	2010			2009			2008		
(Dollars in thousands)	Average Balance	Income/ Expense	Yield/ Rate	Average Balance	Income/ Expense	Yield/ Rate	Average Balance	Income/ Expense	Yield/ Rate
Assets									
Earning assets									
Loans(1)	$ 337,143	$ 19,851	5.89%	$ 337,743	$ 20,226	5.99%	$ 318,954	$ 21,503	6.74%
Securities	194,426	7,566	3.89%	219,947	10,658	4.85%	214,718	11,189	5.21%
Other short-term investments(2)	24,420	94	0.38%	19,131	97	0.51%	10,006	316	3.16%
Total earning assets	555,989	27,511	4.95%	576,821	30,981	5.37%	543,678	33,008	6.07%
Cash and due from banks	7,556			8,464			9,199		
Premises and equipment	18,343			19,159			19,597		
Intangible assets	1,189			22,498			29,678		
Other assets	30,755			25,068			21,475		
Allowance for loan losses	(4,882)			(4,373)			(3,643)		
Total assets	$ 608,950			$ 647,637			$ 619,984		
Liabilities									
Interest-bearing liabilities(2)									
Interest-bearing transaction accounts	$ 70,138	359	0.51%	$ 60,152	270	0.45%	$ 59,077	530	0.90%
Money market accounts	44,293	307	0.69%	36,027	324	0.90%	35,289	742	2.10%
Savings deposits	29,271	76	0.26%	24,596	71	0.29%	23,837	109	0.46%
Time deposits	238,297	5,539	2.32%	248,607	8,069	3.25%	233,061	9,883	4.24%
Other borrowings	102,282	3,093	3.02%	141,047	4,370	3.10%	129,225	4,546	3.52%
Total interest-bearing liabilities	484,281	9,374	1.94%	510,429	13,104	2.57%	480,489	15,810	3.29%
Demand deposits	76,485			69,276			71,472		
Other liabilities	5,269			6,233			5,659		
Shareholders' equity	42,915			61,699			62,364		

Total liabilities and shareholders' equity	$ 608,950			$ 647,637			$ 619,984	
Net interest spread			3.01%			2.80%		2.78%
Net interest income/margin		$ 18,137	3.26%		$ 17,877	3.10%	$ 17,198	3.16%
Net interest margin (tax equivalent)(3)			3.28%			3.12%		3.21%

(1) All loans and deposits are domestic. Average loan balances include non-accrual loans.

(2) The computation includes federal funds sold, securities purchased under agreement to resell and interest bearing deposits.

(3) Based on 32.5% marginal tax rate.

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The following table presents the dollar amount of changes in interest income and interest expense attributable to changes in volume and the amount attributable to changes in rate. The combined effect in both volume and rate, which cannot be separately identified, has been allocated proportionately to the change due to volume and due to rate.

	2010 versus 2009 Increase (decrease) due to			2009 versus 2008 Increase (decrease) due to		
(In thousands)	**Volume**	**Rate**	**Net**	**Volume**	**Rate**	**Net**
Assets						
Earning assets						
Loans	$ (36)	$ (340)	$ (375)	$ 1,218	$ (2,495)	$ (1,277)
Investment securities	(1,237)	(2,099)	(3,092)	268	(799)	(531)
Other short-term investments	27	(23)	(3)	162	(381)	(219)
Total earning assets	(1,119)	(2,439)	(3,470)	1,932	(3,959)	(2,027)
Interest-bearing liabilities						
Interest-bearing transaction accounts	45	38	89	9	(269)	(260)
Money market accounts	74	(74)	(17)	16	(434)	(418)
Savings deposits	13	(7)	5	3	(41)	(38)
Time deposits	(335)	(2,290)	(2,530)	721	(2,535)	(1,814)
Other short-term borrowings	(1,201)	(105)	(1,277)	579	(755)	(176)
Total interest-bearing liabilities	(671)	(3,224)	(3,730)	937	(3,643)	(2,706)
Net interest income			$ 260			$ 679

Market Risk and Interest Rate Sensitivity

Market risk reflects the risk of economic loss resulting from adverse changes in market prices and interest rates. The risk of loss can be measured in either diminished current market values or reduced current and potential net income. Our primary market risk is interest rate risk. We have established an Asset/Liability Management Committee ("ALCO") to monitor and manage interest rate risk. The ALCO monitors and manages the pricing and maturity of its assets and liabilities in order to diminish the potential adverse impact that changes in interest rates could have on our net interest income. The ALCO has established policy guidelines and strategies with respect to interest rate risk exposure and liquidity.

A monitoring technique employed by us is the measurement of our interest sensitivity "gap," which is the positive or negative dollar difference between assets and liabilities that are subject to interest rate repricing within a given period of time. Also, asset/liability modeling is performed to assess the impact varying interest rates and balance sheet mix assumptions will have on net interest income. Interest rate sensitivity can be managed by repricing assets or liabilities, selling securities available-for-sale, replacing an asset or liability at maturity or by adjusting the interest rate during the life of an asset or liability. Managing the amount of assets and liabilities repricing in the same time interval helps to hedge the risk and minimize the impact on net interest income of rising or falling interest rates. Neither the "gap" analysis or asset/liability modeling are precise indicators of our interest sensitivity position due to the many factors that affect net interest income including, the timing, magnitude and frequency of interest rate changes as well as changes in the volume and mix of earning assets and interest-bearing liabilities.

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The following table illustrates our interest rate sensitivity at December 31, 2010.

Interest Sensitivity Analysis

(Dollars in thousands)	Within One Year	One to Three Years	Three to Five Years	Over Five Years	Total
Assets					
Earning assets					
Loans(1)	$ 105,655	$ 109,504	$ 84,334	$ 24,570	$ 324,063
Securities(2)	66,035	43,653	33,510	56,451	199,649
Federal funds sold, securities purchased under agreements to resell and other earning assets	18,738				18,738
Total earning assets	190,428	153,157	117,844	81,021	542,450
Liabilities					
Interest bearing liabilities					
Interest bearing deposits					
NOW accounts	20,174	35,184	11,728	11,728	78,814
Money market accounts	33,592	11,198			44,790
Savings deposits	8,966	12,552	4,184	4,184	29,886
Time deposits	137,145	78,502	12,518	1,064	229,229
Total interest-bearing deposits	199,877	137,436	28,430	16,976	382,719
Other borrowings	48,051	11,007	5,129	32,177	96,364
Total interest-bearing liabilities	247,928	148,443	33,559	49,153	479,083
Period gap	$ (57,500)	$ 4,714	$ 84,285	$ 31,868	$ 63,367
Cumulative gap	$ (57,500)	$ (52,786)	$ 31,499	$ 63,367	$ 63,367
Ratio of cumulative gap to total earning assets	(10.60)%	(9.73)%	5.81%	11.68%	11.68%

(1) Loans classified as non-accrual as of December 31, 2010 are not included in the balances.

(2) Securities based on amortized cost.

We entered into a five year interest rate swap agreement on October 8, 2008. The swap agreement has a $10.0 million notional amount. We receive a variable rate of interest on the notional amount based on a three month LIBOR rate and pay a fixed rate interest of 3.66%. The contract was entered into to protect us from the negative impact of rising interest rates. Our exposure to credit risk is limited to the ability of the counterparty to make potential future payments required pursuant to the agreement. Our exposure to market risk of loss is limited to the changes in the market value of the swap between reporting periods. At December 31, 2010 and 2009 the fair value of the contract was a negative $778 thousand and $535 thousand, respectively. The fair value adjustment during each reporting period is recognized in other income. For the years ended December 31, 2010, 2009 and 2008 the adjustment reflected in earnings amounted to ($581) thousand, $7 thousand and ($725) thousand, respectively. The fair value of the contract is the present value, over the remaining term of the contract, of the difference between the estimated swap rate, for the remaining term, as the reporting date multiplied by the notional amount and the fixed interest rate of 3.66% multiplied by the notional amount of the contract.

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At December 31, 2008, we had an interest rate cap agreement with a notional amount of $10.0 million. The cap rate of interest is 4.50% three month LIBOR. The cap agreement expired on August 1, 2009 and at December 31, 2008 the agreement had no value. In the first quarter of 2008, we had a floor agreement with a notional amount of $10.0 million which was sold and received $608 thousand in cash and recognized a gain in the amount of $179 thousand in other income. These agreements are entered into to protect assets and liabilities from the negative effects of volatility in interest rates. The agreements provide for a payment to the bank of the difference between the cap/floor rate of interest and the market rate of interest. The bank's exposure to credit risk is limited to the ability of the counterparty to make potential future payments required pursuant to the agreement. The bank's exposure to market risk of loss is limited to the market value of the cap and floor. Gains or losses on the value of these interest rate contracts are recognized in earnings on a current basis. The bank received payments under the terms of the cap contract in the amounts of $15 thousand during the year ended December 31, 2008. The bank recognized ($14 thousand) in other income to reflect the decrease in the value of the cap contract for the years ended December 31, 2008.

Through simulation modeling, we monitor the effect that an immediate and sustained change in interest rates of 100 basis points and 200 basis points up and down will have on net-interest income over the next 12 months. Based on the many factors and assumptions used in simulating the effect of changes in interest rates, the following table estimates the hypothetical percentage change in net interest income at December 31, 2010 and 2009 over the subsequent 12 months. Even though we are liability sensitive, the model at December 31, 2010 reflects a decrease in net interest income in a 200 basis point declining rate environment. This primarily results from the current level of interest rates being paid on our interest bearing transaction accounts as well as money market accounts. The interest rates on these accounts are at a level where they cannot be repriced in proportion to the change in interest rates. The increase and decrease of 100 and 200 basis points assume a simultaneous and parallel change in interest rates along the entire yield curve.

Net Interest Income Sensitivity

Change in short-term interest rates	**Hypothetical percentage change in net interest income December 31, 2010**	**2009**
+200bp	-0.48%	+2.26%
+100bp	-0.37%	+1.85%
Flat		
-100bp	-1.69%	-1.61%
-200bp	-6.72%	-6.89%

We also perform a valuation analysis projecting future cash flows from assets and liabilities to determine the Present Value of Equity ("PVE") over a range of changes in market interest rates. The sensitivity of PVE to changes in interest rates is a measure of the sensitivity of earnings over a longer time horizon. At December 31, 2010 and 2009, the PVE exposure in a plus 200 basis point increase in market interest rates was estimated to be -30.04% and -43.60%, respectively. During 2010, we were able to modestly reduce our PVE exposure in a rising rate environment. We continue to reduce our current exposure to increases in interest rates by shortening the lives or repricing periods of our earning assets as well as extending the length of repricing periods on our interest bearing liabilities.

Provision and Allowance for Loan Losses

At December 31, 2010, the allowance for loan losses amounted to $4.9 million, or 1.49% of total loans, as compared to $4.9 million, or 1.41% of total loans, at December 31, 2009. Our provision for

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loan loss was $1.9 million for the year ended December 31, 2010 as compared to $3.1 million and $2.1 million and for the years ended December 31, 2009 and 2008, respectively. The provision is made based on our assessment of general loan loss risk and asset quality. The allowance for loan losses represents an amount which we believe will be adequate to absorb probable losses on existing loans that may become uncollectible. Our judgment as to the adequacy of the allowance for loan losses is based on a number of assumptions about future events, which we believe to be reasonable, but which may or may not prove to be accurate. Our determination of the allowance for loan losses is based on evaluations of the collectability of loans, including consideration of factors such as the balance of impaired loans, the quality, mix, and size of our overall loan portfolio, economic conditions that may affect the borrower's ability to repay, the amount and quality of collateral securing the loans, our historical loan loss experience, and a review of specific problem loans. We also consider subjective issues such as changes in the lending policies and procedures, changes in the local/national economy, changes in volume or type of credits, changes in volume/severity of problem loans, quality of loan review and board of director oversight and concentrations of credit. Periodically, we adjust the amount of the allowance based on changing circumstances. We charge recognized losses to the allowance and add subsequent recoveries back to the allowance for loan losses. There can be no assurance that charge-offs of loans in future periods will not exceed the allowance for loan losses as estimated at any point in time or that provisions for loan losses will not be significant to a particular accounting period, especially considering the overall weakness in the commercial real estate market in our market areas.

We perform an analysis quarterly to assess the risk within the loan portfolio. The portfolio is segregated into similar risk components for which historical loss ratios are calculated and adjusted for identified changes in current portfolio characteristics. Historical loss ratios are calculated by product type and by regulatory credit risk classification (See Note 6 Loans). The annualized weighted average loss ratios over the last 24 months for loans classified substandard, special mention and pass have been approximately 7.7%, 2.3% and 0.4%, respectively. The allowance consists of an allocated and unallocated allowance. The allocated portion is determined by types and ratings of loans within the portfolio. The unallocated portion of the allowance is established for losses that exist in the remainder of the portfolio and compensates for uncertainty in estimating the loan losses. As a result of the economic downturn beginning in 2008 and continuing throughout 2010 real estate values have been dramatically impacted. With our loan portfolio consisting of a large percentage of real estate secured loans we, like most financial institutions, have experienced increasing delinquencies and problem loans. We are not immune to the continued effects of the recessionary economy and continue to experience some deterioration of our loan portfolio in general as evidenced by the increase in non-performing assets from $2.5 million (0.28% of total assets) at December 31, 2008 to $8.3 million (0.85% of total assets) at December 31, 2009 and $13.2 million (2.20% of total assets) at December 31, 2010. While we believe these ratios remain favorable in comparison to current industry results, we are concerned about the impact of this economic environment on our customer base of local businesses and professionals. As noted below in the "Allocation of the Allowance for Loan Losses" table the unallocated portion of the allowance as a percentage of the total allowance has grown over the last several years. The allocated portion of the allowance is based on historical loss experience as well as certain qualitative factors as explained above. The qualitative factors have been established based on certain assumptions made as a result of the current economic conditions and as conditions change are adjusted to be directionally consistent with these changes. With the ongoing uncertainty in economic conditions and particularly real estate valuations we do not believe it would be prudent to reduce substantially the overall level of our allowance at this time. As economic conditions show sustainable improvement the unallocated portion of the allowance should decrease as a percentage of the total allowance. In the near term this percentage may continue to increase slightly.

Our company has a significant portion of its loan portfolio with real estate as the underlying collateral. At December 31, 2010, approximately 91.9% of the loan portfolio had real estate collateral as compared to approximately 91.4% at December 31, 2009 (see Note 16 to financial statements for concentrations of credit). When loans, whether commercial or personal, are granted, they are based on the borrower's ability to generate repayment cash flows from income sources sufficient to service the debt. Real estate is generally taken to reinforce the likelihood of the ultimate repayment and as a secondary source of repayment. During this economic cycle many borrowers' traditional income sources have been impacted significantly and real estate values have dropped significantly. We will continue to work closely with all our borrowers that are experiencing economic problems as a result of this cycle and believe we have the processes in place to monitor and identify problem credits. Until this economic cycle reverses we are likely to continue to experience higher than historical delinquencies and problem loans. Therefore, we anticipate funding our provision for loan losses at levels higher than we have historically experienced. There can be no assurance that charge-offs of loans in future periods will not exceed the allowance for loan losses as estimated at any point in time or that provisions for loan losses will not be significant to a particular accounting period. The allowance is also subject to examination and testing for adequacy by regulatory agencies, which may consider such factors as the methodology used to determine adequacy and the size of the allowance relative to that of peer institutions. Such regulatory agencies could require us to adjust our allowance based on information available to them at the time of their examination.

At December 31, 2010, 2009, and 2008, we had non-accrual loans in the amount of $5.9 million, $4.1 million and $1.8 thousand, respectively. Nonaccrual loans at December 31, 2010 consisted of 41 loans. All of these loans are considered to be impaired, are substantially all real estate related, and have been measured for impairment under the fair value of the collateral method. We consider a loan to be impaired when, based upon current information and events, it is believed that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. Such fair values are obtained using independent appraisals, which we consider to be level 2 inputs. The aggregate amount of impaired loans was $9.6 and $5.7 million for the years ending December 31, 2010 and 2009, respectively. The non-accrual loans range in size from $1 thousand to $1.3 million. The largest relationship is in the amount of $1.3 million with a mortgage on a developed parking complex near the University of South Carolina athletic complex.

In addition to the non-accrual loans that are considered to be impaired, we have six loans totaling $3.7 million that are classified as trouble debt restructurings but are accruing loans as of December 31, 2010. The largest of these is for $2.2 million. This loan is collateralized by owner occupied commercial real estate and certain marketable securities. The debtors cash flow coverage to service the debt has been impacted over the last couple of years and therefore the loan was placed on interest only for a period of time and has subsequently been termed and is amortizing principle and interest on a monthly basis. Due to the collateral coverage on this credit, it is not anticipated that we would incur a material loss in the event the debtor fails to service the debt under the restructured terms. The other five loans included as troubled debt restructurings range in size from $40 thousand to $600 thousand and have been evaluated for impairment based on the fair value of the underlying collateral (See Note 6 "Loans", to the consolidated financial statements for additional disclosures related to impaired loans and troubled debt restructurings).

There were $2.4 million, $2.2 million, and $2.0 million in loans delinquent 30 to 89 days at December 31, 2010, 2009 and 2008, respectively. There were $373 thousand, $1.0 thousand and $59 thousand in loans greater than 90 days delinquent and still accruing interest at December 31, 2010, 2009 and 2008, respectively.

Our management continuously monitors non-performing, classified and past due loans to identify deterioration regarding the condition of these loans. We have identified three loans in the amount of $899 thousand which are current as to principal and interest at December 31, 2010 and not included in non-performing assets but that could be potential problem loans. Each of these loans are real estate related and range in size from $253 thousand to $395 thousand. They have been identified as potential problems based on our review that their traditional sources of cash flow have been impacted

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significantly and they may ultimately not be able to service the debt. These loans are continually monitored and are considered in our overall evaluation of the adequacy of our allowance for loan losses.

The following table summarizes the activity related to our allowance for loan losses.

Allowance for Loan Losses

(Dollars in thousands)	2010	2009	2008	2007	2006
Average loans outstanding	$ 337,143	$ 337,743	$ 318,954	$ 296,991	$ 249,209
Loans outstanding at period end	$ 329,954	$ 344,187	$ 332,964	$ 310,028	$ 275,189
Total nonaccrual loans	$ 5,890	$ 4,136	$ 1,757	$ 600	$ 449
Loans past due 90 days and still accruing	$ 373	$ 1,022	$ 59	$ 501	$ 22
Beginning balance of allowance	$ 4,854	$ 4,581	$ 3,530	$ 3,215	$ 2,701
Loans charged-off:					
Construction and development loans		1,402			
1-4 family residential mortgage	1,273	450	763	320	97
Non-farm non-residential mortgage	223	117			
Home equity	187	107	16	32	
Commercial	125	700	271	28	142
Installment & credit card	91	174	90	103	53
Overdrafts	50	34	110	140	153
Total loans charged-off	1,949	2,984	1,250	623	445
Recoveries:					
1-4 family residential mortgage	43	9	41	80	2
Non-farm non-residential mortgage	2	8			
Home equity	9	4	4	5	
Commercial	32	73	52	281	59
Installment & credit card	19	54	18	16	20
Overdrafts	23	6	57	64	30
Total recoveries	128	154	172	446	111
Net loans charged off	1,821	2,830	1,078	177	334
Provision for loan losses	1,878	3,103	2,129	492	528
Purchased in acquisition					320
Balance at period end	$ 4,911	$ 4,854	$ 4,581	$ 3,530	$ 3,215

Net charge -offs to average loans	0.54%	0.84%	0.34%	0.06%	0.13%
Allowance as percent of total loans	1.49%	1.41%	1.38%	1.14%	1.17%
Non-performing loans as % of total loans	1.90%	1.50%	.55%	.36%	.17%
Allowance as % of non-performing loans	78.41%	94.11%	252.26%	320.62%	682.59%

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The following table presents an allocation of the allowance for loan losses at the end of each of the past five years. The allocation is calculated on an approximate basis and is not necessarily indicative of future losses or allocations. The entire amount is available to absorb losses occurring in any category of loans.

Allocation of the Allowance for Loan Losses

Dollars in thousands	2010 Amount	2010 % of loans in category	2009 Amount	2009 % of loans in category	2008 Amount	2008 % of loans in category	2007 Amount	2007 % of loans in category	2006 Amount	2006 % of loans in category
Commercial, Financial and Agricultural	$ 681	6.2%	$ 634	6.6%	$ 681	8.3%	$ 129	8.7%	$ 83	8.6%
Real Estate Construction	905	3.2%	1,331	5.8%	1,319	8.7%	343	9.1%	884	11.4%
Real Estate Mortgage:										
Commercial	1,404	66.2%	1,522	62.2%	1,641	57.7%	1,989	55.8%	1,692	50.5%
Residential	465	14.1%	243	14.8%	289	15.7%	553	16.8%	323	17.4%
Consumer	414	10.3%	133	10.6%	100	9.6%	198	9.6%	133	12.1%
Unallocated	1,043	N/A	991	N/A	551	N/A	318	N/A	100	N/A
Total	$ 4,911	100.0%	$ 4,854	100.0%	$ 4,581	100.0%	$ 3,530	100.0%	$ 3,215	100.0%

Accrual of interest is discontinued on loans when we believe, after considering economic and business conditions and collection efforts that a borrower's financial condition is such that the collection of interest is doubtful. A delinquent loan is generally placed in nonaccrual status when it becomes 90 days or more past due. At the time a loan is placed in nonaccrual status, all interest, which has been accrued on the loan but remains unpaid, is reversed and deducted from earnings as a reduction of reported interest income. No additional interest is accrued on the loan balance until the collection of both principal and interest becomes reasonably certain.

Noninterest Income and Expense

Noninterest Income. Our primary source of noninterest income is service charges on deposit accounts. In addition, we originate mortgage loans that are pre-sold and funded by the third party acquirer, for which we receive a fee. Other sources of noninterest income are derived from investment advisory fees and commissions on non-deposit investment products, bankcard fees, ATM/debit card fees, commissions on check sales, safe deposit box rent, wire transfer and official check fees. Non-interest income decreased from $5.0 million in 2009 to $3.8 million in 2010. Deposit service charges decreased by $437 thousand in 2010 as compared to 2009. Over the last two years we have experienced fewer items being presented for payment on accounts with insufficient funds and as a result this source of fee income has continued to decline since 2007. In addition, changes to Regulation E that became effective July 1, 2010 required that customers affirmatively opt in to our overdraft protection program. To the extent customers who have utilized this product do not opt in, this will reduce fees related to the program that result from ATM and point of sale transactions. It is expected that this regulatory change along with other proposals or recommendations related to overdraft protection programs, mandated limitations on the number of items an institution can charge within established time frames, as well as, the order in which items presented for payment must be processed on accounts, may continue to reduce deposit service charge fees in the future. Mortgage origination fees increased by $281 thousand to $1.0 million in 2010 from $753 thousand in 2009. This increase is primarily as a result of an increase in the level of refinancing activity during 2010. Changes to underwriting and appraisal requirements established by FNMA and FHLMC as well as changes in the regulatory environment continue to impact the ability of individuals to qualify for loans. In

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addition, regulatory changes related to allowable compensation arrangements for loan originators, as well as, new registration requirements for all mortgage loan originators may have an impact on this source of fee income and the cost related to providing these services in the future. For the year ended December 31, 2010, we had gains on the sale of securities in the amount of $827 thousand, as compared to $1.5 million in the comparable period of 2009.

During 2010, we restructured a portion of our available-for-sale investments. During the second quarter of 2010, we sold a CDO (see Note-5-Investment Securities to our Consolidated Financial Statements for further information), and realized a loss in the amount of $1.7 million. Approximately $41.0 million in available-for-sale GSE bonds and MBSs were sold that realized a gain of approximately $1.7 million. In the third and fourth quarters of 2010, we sold two corporate securities, certain non-taxable municipal securities and other GSE securities and realized gains of $711 thousand. The sales and resulting net gains during the last half of 2010 were a result of our desire to restructure the portfolio to better position us for a rising rate environment as well as investing in securities that have a lower regulatory risk weighting such as GNMA mortgage-backed securities and SBA pools. Other-than-temporary-impairment charges of $477 thousand (credit component) on nine private label mortgage backed securities and of $1.1 million on one pooled trust preferred security were recognized during 2010 (see Note -5-Investment Securities to our Consolidated Financial Statements for further information). During 2009, we recognized aggregate OTTI in the amount of $1.0 million on five investments. The first, in the amount of $510 thousand, was an equity investment in another financial institution that was closed by the OCC and placed into receivership on May 1, 2009. The charge of $510 thousand represented the entire balance of the investment. An additional charge of $491,000 was taken on four private label mortgage backed securities ("PLMBSs"). We engage a third party to obtain information about structure and anticipated cash flows to assist us in evaluating and monitoring our private label mortgage backed securities portfolio (see Note 5 "Investments" to our Consolidated Financial Statements for further information). During 2010, we recorded a negative fair value adjustment on an interest rate swap with a notional amount of $10.0 million in the amount of $581 thousand. This compares to a positive fair value adjustment of $58 thousand during 2009. The interest rate swap was entered into in 2008 to protect assets and liabilities from the negative impact in a rising interest rate environment (See "Market Risk and Interest Rate Sensitivity" discussion). Other noninterest income increased by $164 thousand in 2010 as compared to 2009. The increase primarily relates to increases in ATM surcharge and debit card exchange fees as well as modest increases in other miscellaneous fees. During 2010, we realized fee income related to ATM and debit card usage, to include interchange fees, of approximately $840 thousand. The impact of the changes to allowable fees assessed will not be known until the final regulatory guidance is issued.

As a result of the OTTI charge on FLLMC preferred stock we had a non-interest income loss during 2008 of $10.1 million. Operating non-interest income for 2009 was $5.0 million (see "Reconciliation" above) as compared to $4.2 million in 2008. Deposit service charges decreased by $370 thousand in 2009 as compared to 2008. This decrease in deposit service charges resulted from a continued decline in overdraft fees in 2009 as compared to 2008. In 2009, we realized gains on the sale of securities in the amount of $1.5 million. This gain was partially offset by a $658 thousand loss on the early extinguishment of certain Federal Home Loan Bank advances. We sold approximately $13.0 million in investments in the fourth quarter of 2009 to fund the early extinguishment of $25.0 million in advances. The balance of the payoff was funded from short-term overnight funds. The gain on the sale of the investments offset the loss on the paydown of the advances. Other gains realized throughout 2009 were realized to take advantage of favorable spreads on certain available-for sale securities and shorten the average life of the portfolio. Mortgage origination fees increased by $174 thousand in 2009 as compared to 2008. Continued low interest rates as well as tax credits available to new home buyers increased the volume of loans closed in 2009 as compared to 2008. In addition, there were fewer mortgage origination alternatives available as compared to prior years due to the ongoing economic cycle causing many origination businesses to close. OTTI charges in 2009

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included the write-off of a $510 thousand investment in stock of Silverton Bank NA, which was closed by the OCC in May 2009. In addition, we realized $491 thousand in OTTI charges on 4 different PLMBSs. The $491 thousand represents the realized credit loss associated with the securities (see Note 5 to the financial statements). Adjustment to assets and liabilities carried at fair value had a negative impact on non-interest income of $623 thousand in 2008 whereas it had a positive impact of $58 thousand in 2009 (see Note 3 to financial statements). Other noninterest income increased by $118 thousand in 2009 as compared to 2008. The increase primarily related to modest increases in ATM surcharge and debit card exchange fees, loan late charges as well as other miscellaneous fees.

Noninterest Expense. In the very competitive financial services industry, we recognize the need to place a great deal of emphasis on expense management and continually evaluate and monitor growth in discretionary expense categories in order to control future increases. During the third quarter of 2009, we recognized an impairment charge of $27.8 million related to goodwill acquired in previous acquisitions (see discussion above under "Results of Operations"). Operating noninterest expense increased from $16.6 million in 2009 to $17.7 million in 2010. Total non-interest expense, excluding the goodwill impairment in 2009, increased by $1.1 million, or 6.6%, 2010, as compared to 2009. Salary and benefit expense increased $680 thousand from $8.3 million in 2009 to $8.9 million in the 2010. At December 31, 2010 we had 147 full time equivalent employees as compared to 140 full time employees at December 31, 2009. The increase in number of full time equivalent employees, normal salary adjustments made over the last 12 months as well as a lower amount of deferred salary expense resulting from decreased loan originations account for the increase in salary and benefit expense in 2010 as compared to 2009. FDIC insurance assessments decreased $102,000 in 2010 as compared 2009. During the second quarter of 2009, the FDIC assessed a one-time special assessment on all insured institutions of 10 basis points. This special assessment amounted to $500 thousand and was expensed in the second quarter of 2009. The FDIC assessment rate for 2010 averaged approximately 19.9 basis points. The recently passed financial institution reform legislation broadens the assessment base for calculation of the FDIC assessment. The new assessment base is scheduled to take effect in the second quarter of 2011. It is estimated that we will have reduced assessments in the amount of approximately $120 thousand annually when compared to the existing assessment base. In November 2009, all insured institutions with limited exceptions were required to prepay insurance assessments for a three-year period. Our prepayment made in December 2009 amounted to approximately $2.9 million. At December 31, 2010, the remaining prepaid insurance assessment amounted to $1.8 million and is included in "Other assets". Other real estate expense increased to $823thousand during 2010 as compared to $201thousand in the same period of 2009. This is a result of the increased balance of other real estate owned and includes cost associated with foreclosure, force placed insurance coverage as well as property taxes paid on prior year delinquent taxes on these properties. It is anticipated that these other real estate costs will remain at or near the 2010 levels throughout 2011. Non-interest expense "Other Miscellaneous" decreased by $132 thousand from $756 thousand in 2009 to $624 thousand in 2010.

Operating noninterest expense increased to $16.6 million for the year ended December 31, 2009 from $15.5million for the year ended December 31, 2008. This increase is primarily attributable to increases in salary and benefit expense of $298 thousand and an increase in FDIC/FICO premiums of $838 thousand in 2009 as compared to 2008. The increase in salary and benefit expenses are a result of normal salary increases and a modest increase in cost of medical insurance provided to employees. The FDIC/FICO premiums increase resulted from significant increases in the normal assessment rates implemented by the FDIC as well as a special assessment in the third quarter of 2009 in the amount of approximately $300 thousand. Professional fees and "Other" noninterest expense increased by $155 thousand and $187 thousand, respectively in 2009 as compared to 2008. These increases are primarily related to additional cost related to loan collection efforts as well as legal fees associated with loan workouts and general increases related to addressing and complying with regulatory changes and issues facing the industry. Marketing and public raelations expenses decreased by $220 thousand in

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2009 as compared to 2008. This decrease was a result of our intentional reduction in this discretionary expense during 2009.

The following table sets forth for the periods indicated the primary components of noninterest expense:

	Year ended December 31,		
(In thousands)	**2010**	**2009**	**2008**
Salary and employee benefits	$ 8,942	$ 8,262	$ 7,964
Occupancy	1,229	1,198	1,155
Equipment	1,162	1,249	1,289
Marketing and public relations	402	343	563
ATM/debit card processing	414	342	342
Supplies	150	221	188
Telephone	302	300	331
Courier	63	79	98
Correspondent services	97	34	102
FDIC/FICO premium	1,003	1,105	267
Insurance	220	194	188
Other real estate expenses	823	201	78
Professional fees	1,068	1,132	977
Loss on limited partnership interest	119	119	382
Postage	181	192	191
Director fees	264	232	225
Amortization of intangibles	621	621	507
Impairment of goodwill		27,761	
Other	624	756	692
	$ 17,684	$ 44,341	$ 15,539

Income Tax Expense

Income tax expense for 2010 was $565 thousand as compared to income tax expense (benefit) for the year ended December 31, 2009 of $696 thousand and $(3.8) million for the year ended December 31, 2008. We recognize deferred tax assets for future deductible amounts resulting from differences in the financial statement and tax bases of assets and liabilities and operating loss carry forwards. A valuation allowance is then established to reduce the deferred tax asset to the level that it is more likely than not that the tax benefit will be realized. In 2008, we established a deferred tax valuation allowance of $425 thousand primarily related to contribution carryforwards that expired at the end of 2010. Contribution carry forwards of approximately $710 thousand expired in 2010 and the related valuation allowance in the amount of $241 thousand was reversed. At December 31, 2010, there is a remaining deferred tax valuation reserve in the amount of $184 thousand primarily related to a capital loss carryforward. The net loss generated during 2009 was a result of the impairment of goodwill acquired in tax free acquisitions and therefore is not deductible for income tax purposes. As previously discussed, we had an OTTI charge on certain securities of $14.5 million during 2008. The loss is not deductible for federal income tax purposes until the securities are sold or deemed worthless. Therefore, the loss resulted in recognizing a deferred tax asset in the amount of $4.9 million in 2008. The net operating loss carryforward period for federal income taxes is generally 20 years. Any carry forward period related to realized tax losses on these securities will not start until they are sold or deemed worthless. We have a net operating loss carry forward acquired in the acquisition of DutchFork and DeKalb for federal income tax purposes of approximately $1.6 million to offset future taxable income through 2025. See Note 14 to the financial statements for a reconciliation of the tax expense/benefit. It is anticipated that our effective tax rate for 2011 will be between 30% and 33%.

Financial Position

Assets totaled $599.0 million at December 31, 2010 as compared to $605.8 million at December 31, 2009, a decrease of $6.8 million. Loans at December 31, 2010 were $330.0 million as compared to $344.2 million at December 31, 2009. We funded in excess of $44.7 million of new loan production in 2010, but due to scheduled pay downs during the period as well as transfers from loans to other real estate owned, loans declined by $14.2 million from December 31, 2009 to December 31, 2010. At December 31, 2010, loans accounted for 60.6% of earning assets, as compared to 62.1% at December 31, 2009. The loan-to-deposit ratio at December 31, 2010 was 72.5% as compared to 76.6% at December 31, 2009. Investment securities increased from $195.8 million at December 31, 2009 to $196.2 million at December 31, 2010. Short-term federal funds sold and interest-bearing bank balances increased from $14.1 million at December 31, 2009 to $18.7 million at December 31, 2010. Deposits increased by $5.7 million to $455.3 million at December 31, 2010 as compared to $449.6 million at December 31, 2009. In 2010, we paid down $14.9 million in callable brokered certificates of deposits. At December 31, 2010, we had no brokered certificates of deposits. Due to the current economic cycle and the significant emphasis by regulators and the investment community on tangible capital, regulatory capital ratios and overall liquidity, we have attempted to control the growth of our balance sheet and enhance our liquidity throughout 2010. We have focused on growing our core deposit base while continuing to fund soundly underwritten loans. To enhance our liquidity and improve our exposure to rising interest rates (see "Market Risk Management" section), the growth in deposits was invested in interest-bearing deposits with the Federal Reserve Bank of Richmond and shorter maturity amortizing investments such as agency CMO's and SBA pools.

During the second quarter of 2010, we restructured a portion of our available-for-sale investments. We sold a CDO with a carrying value of $4.9 million and realized a loss in the amount of $1.7 million. This security had been previously downgraded to below investment grade (See Note 5 Investment Securities to our Consolidated Financial Statements) and did not mature until July 2014. Approximately $41.0 million in "GSE" bonds and mortgage-backed securities were sold that realized a gain of approximately $1.7 million. The funds received from this transaction were primarily invested in other securities that have a lower regulatory risk weighting such as GNMA mortgage-backed securities and SBA pools. Both of these types of securities carry a zero percent regulatory risk weighting and are backed by the full faith and credit of the United States Government. In the third and fourth quarter we sold two corporate securities, certain non-taxable municipal securities and other GSE securities and realized gains of $711 thousand. These funds from these sales were primarily reinvested in lower regulatory risk weighted assets. A significant portion of the proceeds were reinvested into adjustable rate securities. As a result of these transactions, we believe we have structured the balance sheet to continue to provide for improvement in our net interest margin in a rising interest rate environment, reduced the level of investments rated below investment grade, as well as improved our overall regulatory capital ratios.

During the second and third quarter of 2010, we reclassified five private label mortgage-backed securities with a carrying value of $5.7 million, previously categorized in the held-to-maturity portfolio to the available-for-sale category. This transfer was made as a result of changes in circumstances that meet the accounting guidance in accordance with ASC 320-10-25-6. This transfer meets the guidance as outlined in section (a) of ASC 320-10-25-6 as a result of a "significant deterioration in the issuer's creditworthiness". During the fourth quarter of 2010, we reclassified all of the remaining investment securities in the held-to-maturity portfolio to the available-for-sale portfolio. The majority of the investments in the held-to-maturity portfolio were non-agency mortgage backed securities. As a result of this transfer, the difference in the carrying value and fair value was recorded as an unrealized loss of approximately $1.6 million (net of tax) in other comprehensive income (loss). The ratings agencies approach to downgrading these mortgage-backed securities has varied significantly over the past two years and we do not believe a rating downgrade by itself is necessarily enough or the only factor to be considered to meet criteria a of the guidance. We believe this significant deterioration is further determined by whether or not OTTI was recorded on the security. These securities transferred in the second and third quarters of 2010 had incurred OTTI and in accordance with ASC 320-10-35, at the time of the OTTI, we also recorded an unrealized loss in accumulated other comprehensive income/(loss). The unrealized loss on these securities is treated differently than unrealized losses on our available-for- sale securities for regulatory capital purposes, specifically in the way it treats the deferred tax asset on the unrealized loss. Based on the deterioration in credit quality (as discussed above), we believe we have met the requirements in section (a) described above and did not taint the remaining held-to-maturity portfolio at the time of these transfers. We made the decision to reclassify the remaining held-to-maturity securities to the available-for sale portfolio as a result of differences in regulatory capital treatment of deferred tax assets related to unrealized losses on available-for-sale securities versus those in the held-to-maturity portfolio and the potential that some of these would be transferred when or if they incurred OTTI. At December 31, 2010, there are no securities classified as held-to-maturity. We also do not consider any of our investments to have additional other-than-temporary impairment in excess of amounts previously recognized at December 31, 2010.

Subsequent to December 31, 2010, we have sold nine non-agency mortgage-backed securities with a total book value of $22.8 million. Six of these securities with a total book value amount of approximately $14.0 million were rated below investment grade by the rating agencies and the other three were rated above investment grade. The transaction resulted in a net realized gain of approximately $30 thousand. Since December 31, 2009, and including this subsequent transaction, the company's portfolio of non-agency mortgage-backed securities has decreased from $65.8 million to $28.6 million and its total book value of securities rated below investment grade has decreased from $51.7 million to $24.8 million during this same period (See "Note 5 "Investments" to the consolidated financial statements).

Shareholders' equity totaled $41.4 million at December 31, 2009 as compared to $41.8 million at December 31, 2010. As previously discussed, we incurred a goodwill impairment charge of $27.8 million in the third quarter of 2009 which was the reason we recorded a net loss for the year ended December 31, 2009 of $25.2 million. Net income available to common shareholders less dividend payments to common shareholders stock resulted in retained deficit decreasing to $19.7 million as of December 31, 2010.

Earning Assets

Loans. Loans typically provide higher yields than the other types of earning assets. During 2010, loans accounted for 60.6% of average earning assets as compared to 58.5% of average earning assets in 2009. The loan portfolio averaged $337.1 million in 2010 as compared to $337.7 million in 2009. Loans decreased from $344.2 million at December 31, 2009 to $330.0 million at December 31, 2010. Quality loan portfolio growth continues to be a strategic focus into 2011 and thereafter. Associated with the higher loan yields are the inherent credit and liquidity risks, which we attempt to control and counterbalance. A goal of the Treasury's CPP, which we participated in 2008, was to provide funds/capital to financial institutions to assist in unfreezing the credit markets. One of our goals as a community bank has, and continues to be, to grow our assets through quality loan growth by providing credit to small and mid-size businesses, as well as individuals within the markets we serve. In 2010, we funded new loans of approximately $44.7 million. Loan production and portfolio growth rates continue to be impacted by the current economic recession, as borrowers are less inclined to leverage their corporate and personal balance sheets. However, we remain committed to meeting the credit needs of our local markets. A continuation of the very slow recovery from recessionary national and local

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economic conditions as well as deterioration of asset quality within our company could significantly impact our ability to grow our loan portfolio. Significant increases in regulatory capital expectations beyond the traditional "well capitalized" ratios and significantly increased regulatory burdens will impede our ability to leverage our balance sheet and expand the loan portfolio.

The following table shows the composition of the loan portfolio by category:

	December 31,				
(In thousands)	**2010**	**2009**	**2008**	**2007**	**2006**
Commercial, financial & agricultural	$ 20,555	$ 22,758	$ 27,833	$ 26,912	$ 23,595
Real estate:					
Construction	10,540	19,972	28,832	28,141	31,474
Mortgage residential	46,684	50,985	52,423	52,018	47,950
Mortgage commercial	218,298	214,178	191,832	173,173	138,886
Consumer:					
Home equity	27,747	28,824	23,872	21,183	23,934
Other	6,130	7,470	8,172	8,601	9,350
Total gross loans	329,954	344,187	332,964	310,028	275,189
Allowance for loan losses	(4,911)	(4,854)	(4,581)	(3,530)	(3,215)
Total net loans	$ 325,043	$ 339,333	$ 328,383	$ 306,498	$ 271,974

In the context of this discussion, a real estate mortgage loan is defined as any loan, other than loans for construction purposes, secured by real estate, regardless of the purpose of the loan. We follow the common practice of financial institutions in the company's market area of obtaining a security interest in real estate whenever possible, in addition to any other available collateral. This collateral is taken to reinforce the likelihood of the ultimate repayment of the loan and tends to increase the magnitude of the real estate loan components. Generally, we limit the loan-to-value ratio to 80%. The principal components of our loan portfolio at year-end 2010 and 2009 were commercial mortgage loans in the amount of $218.2 million and $214.2 million, representing 66.1% and 62.2% of the portfolio, respectively. Significant portions of these commercial mortgage loans are made to finance owner-occupied real estate. We continue to maintain a conservative philosophy regarding our underwriting guidelines, and believe it will reduce the risk elements of the loan portfolio through strategies that diversify the lending mix.

The repayment of loans in the loan portfolio as they mature is a source of liquidity. The following table sets forth the loans maturing within specified intervals at December 31, 2010.

Loan Maturity Schedule and Sensitivity to Changes in Interest Rates

	December 31, 2010			
(in thousands)	**One Year or Less**	**Over one Year Through Five Years**	**Over five years**	**Total**
Commercial, financial and agricultural	$ 8,131	$ 12,468	$ 46	$ 20,645
R/E-Construction	10,540			10,540
All other loan	44,578	190,102	64,089	298,769
	$ 63,249	$ 202,570	$ 64,135	$ 329,954
Loans maturing after one year with:				
Variable Rate				$ 47,341
Fixed Rate				219,364
				$ 266,705

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The information presented in the above table is based on the contractual maturities of the individual loans, including loans which may be subject to renewal at their contractual maturity. Renewal of such loans is subject to review and credit approval, as well as modification of terms upon their maturity.

Investment Securities

The investment securities portfolio is a significant component of our total earning assets. Total securities averaged $194.4 million in 2010, as compared to $219.9 million in 2009. This represents 35.0% and 38.1% of the average earning assets for the year ended December 31, 2010 and 2009, respectively. At December 31, 2010 and 2009 our investment securities portfolio amounted to $196.2 million and $195.8 million, respectively.

Beginning in 2008 and lasting through 2010 the bond markets and many institutional holders of bonds have come under a great deal of stress partially as a result of increasing delinquencies in the sub-prime mortgage lending market. As of December 31, 2010, we own total MBSs and CMOs with an amortized cost of $124.1 million and an approximate fair value of $121.3 million. These included securities with an amortized cost of $72.7 million and approximate fair value of $72.8 million issued by GSEs. The current economic recessionary cycle has impacted MBSs issued by GSEs, such as FHLMC and FNMA. These entities continue to experience increasing delinquencies in the underlying loans that make up the MBSs and CMOs. As of December 31, 2010 and 2009 all of the MBSs issued by GSEs are classified as "Available for Sale." Unrealized losses on certain of these investments are not considered to be "other than temporary" and we have the intent and ability to hold these until they mature or recover the current book value. The contractual cash flows of the investments are guaranteed by the GSE. Accordingly, it is expected that the securities would not be settled at a price less than our amortized cost.

Also included in our MBS and CMO portfolio are PLMBSs with an amortized cost of $51.4 million and approximate fair value of $48.5 million at December 31, 2010. Although these are not classified as sub-prime obligations or considered the "high risk" tranches, the majority of "structured" investments within all credit markets have been impacted by volatility and credit concerns and economic stresses throughout 2008 through 2010. The result has been that the market for these investments are less liquid and the spread as compared to alternative investments widened dramatically. During the second quarter of 2008, we implemented a leverage strategy whereby we acquired approximately $63.2 million in certain non-agency MBSs and CMOs. All of the mortgage assets acquired in this transaction were classified as prime or ALT-A securities and represented the senior or super-senior tranches of the securities. The assets acquired as part of this strategy were classified as held-to-maturity in the investment portfolio. Due to the significant spreads on these securities, they were all purchased at discounts. From the inception of the leverage strategy in 2008 through December 31, 2010, we have realized an approximate net interest margin of 2.23% on the strategy. A detailed analysis of each of the CMO pools included in this leverage transaction as well as privately held CMOs held previously in the available-for-sale portfolio have been analyzed by reviewing underlying loan delinquencies, collateral value and resulting credit support.

Starting in early 2009, many of these securities acquired in the leverage strategy, as well as others that were owned prior to 2008, began to be downgraded by the various rating agencies, and at December 31, 2010, 20 CUSIPs held have been downgraded below investment grade. We perform an internal detailed analysis on each CUSIP on a quarterly basis. Our internal analysis includes stressing each security using various assumptions for conditional default rate (CDR), prepayment speeds (CPR) and severities of loss on underlying collateral once it is liquidated. In addition, we have an independent third party perform an analysis of each security to assist with evaluating and stressing each of the securities that have been downgraded below investment grade. Our analysis to evaluate the credit loss component of the impairment includes stressing the expected cash flows using the average CPR, CDRs and severities over the last six months. Each CUSIP is reviewed and if circumstances indicate that a shorter time frame is appropriate because CDRs and severities are rapidly increasing, we will adjust these assumptions. For the year ended December 31, 2010 we recognized impairment charges on six PLMBS investments whereby the credit component was $477 thousand recognized through earnings and the amount recognized through other comprehensive income amounted to $2.2 million for the year ended December 31, 2010 (see Note 5 to the financial statements). For the year ended December 31, 2009 we recognized the credit impairment charges of $491 thousand as the credit component on four PLMBS securities through earnings and $1.7 million through other comprehensive income. All of these investments are held in our available-for-sale portfolio. The PLMBS's continue to experience high levels of delinquencies in the underlying loans that make up the PLMBSs, and as a result we could experience additional OTTI in the future.

The following table summarizes the PLMBSs portfolio by credit rating. The rating reflects the lowest rating by any major rating agency.

Credit Rating	**Number of CUSIPs**	**Par Value**	**Amortized Cost**	**Fair Value**
AAA	14	$ 6,881	$ 6,267	$ 6,613
AA-	1	4,086	3,916	4,237
A1	1	3,511	3,239	3,506
A	1	435	435	434
Baa1	1	524	357	435
Baa2	1	102	102	102
Below Investment Grade	20	41,513	37,091	33,202
Total	39	$ 57,052	$ 51,407	$ 48,529

In our opinion, the current rating system does not properly reflect the overall risk in these types of multi-obligor bonds. Generally, they are rated below investment grade when there is a projected loss of a level of principal based on the par value of the bond. The process does not adequately consider what the holder paid for the bond or the impact that they are multi-obligor securities. This can cause an entire security to be rated below investment grade even though a majority of the underlying obligors are paying timely on the underlying obligation. Based on the increased trading levels and prices paid for such securities, we believe that in 2010 certain investors became more comfortable with their ability to model the cash flows underlying this type of security and began to institute strategies to acquire portfolios of PLMBSs. As a result, the additional demand caused the spreads on these investments to narrow throughout 2010 and the amount of the unrealized losses on our portfolio has decreased. We believe that the robust internal and independent external monitoring process that we have in place allows us to properly evaluate the credit risk underlying these securities and record any further OTTI in a timely manner. As previously noted, subsequent to December 31, 2010, we sold nine non-agency mortgage-backed securities with a total book value of $22.8 million. Six of these securities with a total book value amount of approximately $14.0 million were rated below investment grade by the rating agencies and the other three were rated above investment grade. The transaction resulted in a net realized gain in the first quarter of 2011of approximately $30 thousand. Since December 31, 2009, and including these subsequent first quarter 2011 transactions, the company's portfolio of non-agency mortgage-backed securities has decreased from $65.8 million to $28.6 million and the total book value of securities rated below investment grade has decreased from $51.7 million to $24.8 million during this same period. The decrease was accomplished through the sales noted above as well as normal principal paydowns and to a lesser extent the OTTI charges discussed above. The result of selling these securities will have a negative impact on the overall yield on the investment portfolio but, while not eliminating, significantly reduces the overall risk and exposure to additional OTTI in the event the underlying collateral performance of these securities deteriorates in the future.

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We also hold corporate bonds and other securities with an amortized cost value of $3.4 million and fair value of $2.6 million as of December 31, 2010. The unrealized loss on investments in corporate bonds relates to bonds with four different issuers. All of these bonds are carried in the available-for-sale portfolio. The economic conditions throughout 2010 and 2009 have had a significant impact on all corporate debt obligations. As a result, the spreads on all of these securities have widened dramatically and the liquidity of many of these investments has been negatively impacted. Each of these bonds is rated BBB (investment grade) or better (S&P) with the exception of two bonds downgraded during the last 24 months. One downgraded investment is rated CC by Fitch and Ca by Moody's and is a preferred term security with a book value of $879 thousand and fair value of $182 thousand. This bond has a par value of $2.0 million and during 2010 we recognized OTTI in the amount of $1.1 million through earnings (credit component) and $697 thousand through other comprehensive income. The fourth bond is rated BBB- by S&P and Ba1 by Moody with a carrying value of $997 thousand and a fair value of $928 thousand. All of the corporate bonds held by the company are reviewed on a quarterly basis to identify downgrades by rating agencies as well as deterioration of the underlying collateral or in the issuer's ability to service the debt obligation.

For corporate debt securities, we review the underlying issuer's credit quality, additional underlying credit support, and the length of maturity of the bond. If our analysis determines that it is likely we will recover all of the projected cash flows, we do not deem the security to be OTTI.

At December 31, 2010, the estimated weighted average life of the portfolio was approximately 6.0 years, duration of approximately 3.9, and a weighted average tax equivalent yield of approximately 4.66%

The following table shows the investment portfolio composition.

(Dollars in thousands)	**&n**	**December 31,**