SUMMIT FINANCIAL GROUP INC
Form 10-Q
May 17, 2010

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

FORM 10 – Q

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

For the quarterly period ended March 31, 2010.
or
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 For the transition period from ___________ to __________.

Commission File Number 0-16587

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

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

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Sections 13 or 15(d) of the Securities and Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes o No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer o Accelerated filero

Non-accelerated filer o Smaller reporting companyþ

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

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock as of the latest practicable date.

Common Stock, $2.50 par value
7,425,472 shares outstanding as of May 12, 2010

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

Dollars in thousands	March 31, 2010 (unaudited)	December 31, 2009 (*)	March 31, 2009 (unaudited)
ASSETS			
Cash and due from banks	$5,163	$6,813	$15,358
Interest bearing deposits with other banks	9,032	34,247	114
Federal funds sold	-	-	-
Securities available for sale	262,565	271,654	295,706
Other investments	24,008	24,008	24,000
Loans held for sale, net	429	1	1,327
Loans, net	1,112,526	1,137,336	1,186,042
Property held for sale	50,562	40,293	7,807
Premises and equipment, net	24,001	24,234	23,407
Accrued interest receivable	6,519	6,323	6,991
Intangible assets	9,265	9,353	9,617
Other assets	32,426	30,363	28,599
Total assets	$1,536,496	$1,584,625	$1,598,968
LIABILITIES AND SHAREHOLDERS' EQUITY			
Liabilities			
Deposits			
Non interest bearing	$71,100	$74,119	$70,483
Interest bearing	939,936	943,219	884,875
Total deposits	1,011,036	1,017,338	955,358
Short-term borrowings	27,456	49,739	120,480
Long-term borrowings	361,335	381,492	396,098
Subordinated debentures	16,800	16,800	15,000
Subordinated debentures owed to unconsolidated subsidiary trusts	19,589	19,589	19,589
Other liabilities	9,746	9,007	8,839
Total liabilities	1,445,962	1,493,965	1,515,364
Commitments and Contingencies			
Shareholders' Equity			
Preferred stock and related surplus - authorized 250,000 shares			
Series 2009, 8% Non-cumulative convertible preferred stock,			
par value $1.00; issued 2009 - 3,710 shares	3,519	3,519	-
Common stock and related surplus, authorized 20,000,000 shares,			
$2.50 par value; issued and outstanding 2010 - 7,425,472 shares,			
December 2009 - 7,425,472 shares;			
March 2009 - 7,415,310 shares	24,508	24,508	24,453
Retained earnings	63,519	63,474	66,475
Accumulated other comprehensive income (loss)	(1,012)	(841)	(7,324)
Total shareholders' equity	90,534	90,660	83,604

Total liabilities and shareholders' equity	$1,536,496	$1,584,625	$1,598,968

(*) - December 31, 2009 financial information has been extracted from audited consolidated financial statements

See Notes to Consolidated Financial Statements

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

	Three Months Ended	
Dollars in thousands, except per share amounts	March 31, 2010	March 31, 2009
Interest income		
Interest and fees on loans		
Taxable	$ 16,958	$ 18,147
Tax-exempt	83	107
Interest and dividends on securities		
Taxable	3,138	4,224
Tax-exempt	455	513
Interest on interest bearing deposits with other banks	11	-
Interest on Federal funds sold	-	-
Total interest income	20,645	22,991
Interest expense		
Interest on deposits	5,498	6,620
Interest on short-term borrowings	57	213
Interest on long-term borrowings and subordinated debentures	4,858	4,822
Total interest expense	10,413	11,655
Net interest income	10,232	11,336
Provision for loan losses	5,350	4,000
Net interest income after provision for loan losses	4,882	7,336
Other income		
Insurance commissions	1,209	1,344
Service fees	707	735
Realized securities gains (losses)	264	256
Gain (loss) on sale of assets	12	(9)
Other	353	329
Total other-than-temporary impairment loss on securities	(454)	(215)
Portion of loss recognized in other comprehensive income	425	-
Net impairment loss recognized in earnings	(29)	(215)
Total other income	2,516	2,440
Other expense		
Salaries, commissions, and employee benefits	3,724	4,279
Net occupancy expense	521	597
Equipment expense	629	568
Supplies	109	194
Professional fees	274	334
Amortization of intangibles	88	88
FDIC premiums	825	383
OREO foreclosure expense	232	55
Other	1,208	1,253
Total other expense	7,610	7,751
Income (loss) before income taxes	(212)	2,025
Income tax expense (benefit)	(332)	260
Net Income (loss)	120	1,765

Dividends on preferred shares		74		-
Net Income (loss) applicable to common shares	$	46	$	1,765
Basic earnings per common share	$	0.01	$	0.24
Diluted earnings per common share	$	0.01	$	0.24

See Notes to Consolidated Financial Statements

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

Dollars in thousands, except per share amounts	Common Stock and Related Surplus	Preferred Stock and Related Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance, December 31, 2009	$24,508	$3,519	$63,474	$ (841)	$90,660
Three Months Ended March 31, 2010					
Comprehensive income:					
Net income	-	-	120	-	120
Other comprehensive income:					
Non-credit related other-than-temporary impairment on available for sale debt securities of $425, net of deferred taxes of $161	-	-	-	(264)	(264)
Net unrealized gain on available for sale debt securities of $150, net of deferred taxes of $57 and reclassification adjustment for net realized gains included in net income of $264	-	-	-	93	93
Total comprehensive income					(51)
Exercise of stock options	-	-	-	-	-
Stock compensation expense	-	-	-	-	-
Preferred stock cash dividends declared ($20.00 per share)	-	-	(75)	-	(75)
Balance, March 31, 2010	$24,508	$3,519	$63,519	$ (1,012)	$90,534
Balance, December 31, 2008	$24,453	$-	$64,709	$ (1,918)	$87,244
Three Months Ended March 31, 2009					
Comprehensive income:					
Net income	-	-	1,765	-	1,765
Other comprehensive income:					
Net unrealized loss on securities of $5,662, net of deferred tax benefit of $3,175 and reclassification adjustment for gains included in net income of $256	-	-	-	(5,406)	(5,406)
Total comprehensive income					(3,641)
Exercise of stock options	-	-	-	-	-
Stock compensation expense	-	-	-	-	-

Balance, March 31, 2009	$24,453	$-	$66,474	$ (7,324)	$83,603

See Notes to Consolidated Financial Statements

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

	Three Months Ended	
Dollars in thousands	March 31, 2010	March 31, 2009
Cash Flows from Operating Activities		
Net income	$120	$1,765
Adjustments to reconcile net earnings to net cash		
provided by operating activities:		
Depreciation	407	406
Provision for loan losses	5,350	4,000
Deferred income tax (benefit)	(437)	(537)
Loans originated for sale	(1,781)	(4,821)
Proceeds from loans sold	1,354	4,485
(Gain) on sales of loans held for sale	-	(13)
Securities (gains)	(264)	(256)
Writedown of equity investment	-	215
Other-than-temporary impairment of debt securities	29	-
Loss (gain) on disposal of other repossessed assets & property held for sale	(12)	9
Amortization of securities premiums, net	(302)	(586)
Amortization of goodwill and purchase accounting		
adjustments, net	91	91
Increase (decrease) in accrued interest receivable	(196)	225
(Increase) decrease in other assets	(1,574)	193
Increase in other liabilities	739	254
Net cash provided by operating activities	3,524	5,430
Cash Flows from Investing Activities		
Net (increase) decrease in interest bearing deposits		
with other banks	25,215	(6)
Proceeds from maturities and calls of securities available for sale	6,034	3,367
Proceeds from sales of securities available for sale	4,078	9,730
Principal payments received on securities available for sale	13,144	16,729
Purchases of securities available for sale	(13,907)	(6,020)
Purchases of other investments	-	(982)
Net decrease in Federal funds sold	-	2
Net (loans made) principal payments received on loans	8,792	1,885
Purchases of premises and equipment	(175)	(1,379)
Proceeds from sales of other repossessed assets & property held for sale	462	45
Net cash provided by (used in) investing activities	43,643	23,371
Cash Flows from Financing Activities		
Net increase in demand deposit, NOW and		
savings accounts	6,935	31,448
Net (decrease) in time deposits	(13,236)	(41,940)
Net (decrease) in short-term borrowings	(22,284)	(32,620)
Proceeds from long-term borrowings	-	40,000
Repayment of long-term borrowings	(20,158)	(26,649)
Proceeds from issuance of subordinated debentures	-	4,962

Dividends paid on preferred stock	(74)	-
Net cash provided by (used in) financing activities	(48,817)	(24,799)
Increase (decrease) in cash and due from banks	(1,650)	4,002
Cash and due from banks:		
Beginning	6,813	11,356
Ending	$5,163	$15,358

(Continued)

See Notes to Consolidated Financial Statements

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

	Three Months Ended	
Dollars in thousands	March 31, 2010	March 31, 2009
Supplemental Disclosures of Cash Flow Information		
Cash payments for:		
Interest	$10,636	$11,832
Income taxes	$-	$-
Supplemental Schedule of Noncash Investing and Financing Activities		
Other assets acquired in settlement of loans	$10,668	$230

See Notes to Consolidated Financial Statements

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

Note 1. Basis of Presentation

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

The presentation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from these estimates. For the first quarter of 2010, we evaluated subsequent events through May 17, 2010, the filing date of this report.

The results of operations for the three months ended March 31, 2010 are not necessarily indicative of the results to be expected for the full year. The consolidated financial statements and notes included herein should be read in conjunction with our 2009 audited financial statements and Annual Report on Form 10-K. Certain accounts in the consolidated financial statements for December 31, 2009 and March 31, 2009, as previously presented, have been reclassified to conform to current year classifications.

Note 2. Significant New Authoritative Accounting Guidance

ASU No. 2010-06, Fair Value Measurements and Disclosures (Topic 820) - Improving Disclosures About Fair Value Measurements, requires expanded disclosures related to fair value measurements including (i) the amounts of significant transfers of assets or liabilities between Levels 1 and 2 of the fair value hierarchy and the reasons for the transfers, (ii) the reasons for transfers of assets or liabilities in or out of Level 3 of the fair value hierarchy, with significant transfers disclosed separately, (iii) the policy for determining when transfers between levels of the fair value hierarchy are recognized and (iv) for recurring fair value measurements of assets and liabilities in Level 3 of the fair value hierarchy, a gross presentation of information about purchases, sales, issuances and settlements.
ASU 2010-06 further clarifies that (i) fair value measurement disclosures should be provided for each class of assets and liabilities (rather than major category), which would generally be a subset of assets or liabilities within a line item in the statement of financial position and (ii) company’s should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements for each class of assets and liabilities included in Levels 2 and 3 of the fair value hierarchy. The disclosures related to the gross presentation of purchases, sales, issuances and settlements of assets and liabilities included in Level 3 of the fair value hierarchy will be required for us beginning January 1, 2011. The remaining disclosure requirements and clarifications made by ASU 2010-06 became effective for us on January 1, 2010. See Note 3 – Fair Value Measurements.

ASU No. 2010-11, Derivatives and Hedging (Topic 815) - Scope Exception Related to Embedded Credit Derivatives clarifies that the only form of an embedded credit derivative that is exempt from embedded derivative bifurcation requirements are those that relate to the subordination of one financial instrument to another. As a result, entities that have contracts containing an embedded credit derivative feature in a form other than such subordination may need to separately account for the embedded credit derivative feature. The provisions of ASU 2010-11 will be effective for us on July 1, 2010 and are not expected to have a significant impact on our financial statements.

Note 3. Fair Value Measurements

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

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

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

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

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

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

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

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

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

Loans: We do not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and an allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment in accordance with ASC Topic 310, Accounting by Creditors for Impairment of a Loan. The fair value of impaired loans is estimated using one of several methods, including collateral value, liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At March 31, 2010, substantially all of the total impaired loans were evaluated based on the fair value of the collateral. In accordance with ASC Topic 310, impaired loans where an allowance is established based on the fair value of collateral requires classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, we record the impaired loan as nonrecurring Level 2. When a current appraised value is not available and there is no observable market price, we record the impaired loan as nonrecurring Level 3.

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

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

allocated allowance for loan losses, as appropriate. In addition, management also assigns a discount of 7–10% for the estimated costs to sell the collateral. As of March 31, 2010, the total fair value of our collateral dependent impaired loans which had a related specific allowance or charge-off was $3,344,000 less than the related appraised values of the underlying collateral for such loans.

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

Derivative Assets and Liabilities: Substantially all derivative instruments held or issued by us for risk management or customer-initiated activities are traded in over-the-counter markets where quoted market prices are not readily available. For those derivatives, we measure fair value using models that use primarily market observable inputs, such as yield curves and option volatilities, and include the value associated with counterparty credit risk. We classify derivative instruments held or issued for risk management or customer-initiated activities as Level 2. Examples of Level 2 derivatives are interest rate swaps.

Assets and Liabilities Recorded at Fair Value on a Recurring Basis

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

Dollars in thousands	Total at March 31, 2010	Fair Value Measurements Using: Level 1	Level 2	Level 3
Available for sale securities				
U.S. Government sponsored agencies	$ 53,800	$ -	$ 53,800	$ -
Mortgage backed securities:				
Government sponsored agencies	99,068	-	99,068	-
Nongovernment sponsored agencies	63,290	-	63,290	-
State and political subdivisions	4,301	-	4,301	-
Corporate debt securities	352	-	352	-
Other equity securities	77	-	77	-
	41,677	-	41,677	-

Tax-exempt state and political subdivisions								
Total available for sale securities	$	262,565	$	-	$	262,565	$	-

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Notes to Consolidated Financial Statements (unaudited)

Dollars in thousands	Balance at December 31, 2009	Fair Value Measurements Using: Level 1	Level 2	Level 3
Available for sale securities				
U.S. Government sponsored agencies	$ 54,961	$ -	$ 54,961	$ -
Mortgage backed securities:				
Government sponsored agencies	100,036	-	100,036	-
Nongovernment sponsored agencies	69,797	-	69,797	-
State and political subdivisions	3,792	-	3,792	-
Corporate debt securities	356	-	356	-
Other equity securities	77	-	77	-
Tax-exempt state and political subdivisions	42,635	-	42,635	-
Total available for sale securities	$ 271,654	$ -	$ 271,654	$ -

There were no assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the period ended March 31, 2010.

Assets and Liabilities Recorded at Fair Value on a Nonrecurring Basis

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

Dollars in thousands	Total at March 31, 2010	Fair Value Measurements Using: Level 1	Level 2	Level 3
Residential mortgage loans held for sale	$ 429	$ -	$ 429	$ -
Impaired loans				
Commercial	1,495	-	-	1,495
Commercial real estate	44,020	-	27,695	16,325
Construction and development	23,049	-	16,623	6,426
Residential real estate	4,169	-	2,331	1,838
Total impaired loans	72,733	-	46,649	26,084
OREO	50,562	-	46,597	3,965

Dollars in thousands	Balance at December 31, 2009	Fair Value Measurements Using: Level 1	Level 2	Level 3
Residential mortgage loans held for sale	$ 1	$ -	$ 1	$ -
Impaired loans				
Commercial	104	-	-	104
Commercial real estate	48,057	-	30,585	17,472
Construction and development	25,621	-	20,717	4,904
Residential real estate	702	-	702	-
Total impaired loans	74,484	-	52,004	22,480
OREO	40,293	-	38,788	1,505

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral-dependent loans, had a carrying amount at March 31, 2010 of $83,178,000, with a valuation allowance of $10,445,000, resulting in an additional provision for loan losses of $3,566,000 for the three months ended March 31, 2010.

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

Cash and due from banks: The carrying values of cash and due from banks approximate their estimated fair value.

Interest bearing deposits with other banks: The fair values of interest bearing deposits with other banks are estimated by discounting scheduled future receipts of principal and interest at the current rates offered on similar instruments with similar remaining maturities.

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

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

Loans held for sale: The carrying values of loans held for sale approximate their estimated fair values.

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

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

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

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

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

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

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

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

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Notes to Consolidated Financial Statements (unaudited)

The carrying values and estimated fair values of our financial instruments are summarized below:

	March 31, 2010		December 31, 2009	
Dollars in thousands	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Financial assets:				
Cash and due from banks	$ 5,163	$ 5,163	$ 6,813	$ 6,813
Interest bearing deposits with other banks	9,032	9,032	34,247	34,247
Federal funds sold	-	-	-	-
Securities available for sale	262,565	262,565	271,654	271,654
Other investments	24,008	24,008	24,008	24,008
Loans held for sale, net	429	429	1	1
Loans, net	1,112,526	1,123,675	1,137,336	1,152,837
Accrued interest receivable	6,519	6,519	6,323	6,323
	$ 1,420,242	$ 1,431,391	$ 1,480,382	$ 1,495,883
Financial liabilities:				
Deposits	$ 1,011,036	$ 1,075,786	$ 1,017,338	$ 1,087,212
Short-term borrowings	27,456	27,456	49,739	49,739
Long-term borrowings	361,335	377,056	381,492	395,375
Subordinated debentures	16,800	16,800	16,800	16,800
Subordinated debentures owed to unconsolidated subsidiary trusts	19,589	19,589	19,589	19,589
Accrued interest payable	3,894	3,894	4,146	4,146
	$ 1,440,110	$ 1,520,581	$ 1,489,104	$ 1,572,861

Note 4. Earnings per Share

The computations of basic and diluted earnings per share follow:

	For the Three Months Ended March 31,					
	2010			2009		
Dollars in thousands,	Income (Numerator)	Common Shares (Denominator)	Per Share	Income (Numerator)	Common Shares (Denominator)	Per Share

except per share amounts						
Net income	$ 120			$ 1,765		
Less preferred stock dividends	(74)			-		
Basic EPS	$ 46	7,425,472	$ 0.01	$ 1,765	7,415,310	$ 0.24
Effect of dilutive securities:						
Stock options	-	-		-	20,200	
Convertible preferred stock	-	-		-	-	
Diluted EPS	$ 46	7,425,472	$ 0.01	$ 1,765	7,435,510	$ 0.24

Stock option grants and the conversion of preferred stock are disregarded in this computation if they are determined to be anti-dilutive. Our anti-dilutive stock options at March 31, 2010 and 2009 totaled 309,180 shares and 265,980 shares, respectively. Our anti-dilutive convertible preferred shares totaled 674,545 shares at March 31, 2010.

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Note 5. Securities

The amortized cost, unrealized gains, unrealized losses and estimated fair values of securities at March 31, 2010, December 31, 2009, and March 31, 2009 are summarized as follows:

	March 31, 2010			
	Amortized	Unrealized		Estimated
Dollars in thousands	Cost	Gains	Losses	Fair Value
Available for Sale				
Taxable debt securities:				
U. S. Government agencies and corporations	$ 53,229	$ 679	$ 108	$ 53,800
Residential mortgage-backed securities:				
Government-sponsored agencies	94,777	4,365	74	99,068
Nongovernment-sponsored agencies	69,869	713	7,292	63,290
State and political subdivisions	4,280	38	17	4,301
Corporate debt securities	350	2	-	352
Total taxable debt securities	222,505	5,797	7,491	220,811
Tax-exempt debt securities:				
State and political subdivisions	41,613	480	416	41,677
Total tax-exempt debt securities	41,613	480	416	41,677
Equity securities	77	-	-	77
Total available for sale securities	$ 264,195	$ 6,277	$ 7,907	$ 262,565

	December 31, 2009			
	Amortized	Unrealized		Estimated
Dollars in thousands	Cost	Gains	Losses	Fair Value
Available for Sale				
Taxable debt securities:				
U. S. Government agencies and corporations	$ 54,850	$ 693	$ 582	$ 54,961
Residential mortgage-backed securities:				
Government-sponsored agencies	95,939	4,189	92	100,036
Nongovernment-sponsored agencies	75,546	662	6,411	69,797
State and political subdivisions	3,760	37	5	3,792

Corporate debt securities		350		6		-		356
Total taxable debt securities		230,445		5,587		7,090		228,942
Tax-exempt debt securities:								
State and political subdivisions		42,486		570		421		42,635
Total tax-exempt debt securities		42,486		570		421		42,635
Equity securities		77		-		-		77
Total available for sale securities	$	273,008	$	6,157	$	7,511	$	271,654

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	March 31, 2009			
	Amortized	Unrealized		Estimated
Dollars in thousands	Cost	Gains	Losses	Fair Value
Available for Sale				
Taxable debt securities:				
U. S. Government agencies				
and corporations	$ 35,340	$ 1,210	$ 3	36,547
Residential mortgage-backed securities:				
Government-sponsored agencies	131,035	5,047	10	136,072
Nongovernment-sponsored agencies	92,008	470	18,078	74,400
State and political subdivisions	3,760	28	3	3,785
Corporate debt securities	349	-	13	336
Total taxable debt securities	262,492	6,755	18,107	251,140
Tax-exempt debt securities:				
State and political subdivisions	44,845	732	1,217	44,360
Total tax-exempt debt securities	44,845	732	1,217	44,360
Equity securities	179	27	-	206
Total	$ 307,516	$ 7,514	$ 19,324	$ 295,706

The maturities, amortized cost and estimated fair values of securities at March 31, 2010, are summarized as follows:

	Available for Sale	
	Amortized	Estimated
Dollars in thousands		