

BANK OF SOUTH CAROLINA CORP

Form 10KSB

March 04, 2005

**U.S. SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

**FORM 10-KSB**

**þ ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2004

**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: 0-27702

**BANK OF SOUTH CAROLINA CORPORATION**

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(Name of small business issuer in its charter)

South Carolina  
(State or other jurisdiction of  
incorporation or organization)

57-1021355  
(IRS Employer  
Identification Number)

256 Meeting Street, Charleston, SC  
(Address of principal executive offices)

29401  
(Zip Code)

Issuer's telephone number: (843) 724-1500

Securities registered under Section 12(b) of the Exchange Act: NONE

Securities registered under Section 12(g) of the Exchange Act:

Common Stock  
(Title of Class)

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

Yes  No

Check if disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained to the best of the registrant's knowledge, in definitive proxy information statements incorporated by reference in Part III of this Form 10-KSB or any amendments to this Form 10-KSB.

Not applicable

Issuer's revenues for its most recent fiscal year: \$10,602,615

Aggregate market value of the voting stock held by non-affiliates, computed by reference to the closing price of such

stock on February 25, 2005 was: \$24,164,322

As of February 25, 2005, the Registrant has outstanding 2,805,610 shares of common stock.

Transitional Small Business Disclosure Format (check one): Yes  No

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BANK OF SOUTH CAROLINA CORPORATION  
AND SUBSIDIARY

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## PART I

### **Item 1. Description of Business**

The Bank of South Carolina (the Bank) is a FDIC insured, state-chartered financial institution, which was organized on October 22, 1986, and opened for business on February 26, 1987. The Bank is a wholly-owned subsidiary of Bank of South Carolina Corporation (the Company). The reorganization of The Bank of South Carolina into a subsidiary of a one-bank holding company became effective on April 17, 1995. Each issued and outstanding share of the Bank was exchanged for two shares of Bank of South Carolina Corporation stock. Since the primary asset of the Company is its wholly-owned subsidiary, the majority of the following discussion relates to the Bank.

The Bank serves Berkeley, Charleston and Dorchester counties (the Tri-County Area) as an independent, community-oriented commercial bank concentrating on individuals and small and medium-sized businesses desiring a high level of personalized services.

The Bank offers a full range of deposit services. Checking account services include regular non-interest bearing checking accounts as well as interest bearing negotiable order of withdrawal (NOW) accounts. Savings and certificate of deposit accounts include accounts ranging from a daily maturity (regular savings and also money market accounts) to longer term certificates as authorized by regulation. The Bank offers tiered interest to its customers on both money market and NOW accounts. In addition, Individual Retirement Accounts are available. All deposit accounts are insured by the FDIC to the full amount permitted by law. Deposit accounts are solicited from individuals, businesses, professional organizations and governmental authorities.

Lending services include a full range of commercial, personal and mortgage loans. The Bank's primary focus is on business lending. The types of commercial loans that are available include both secured and unsecured loans for working capital (including inventory and receivables), business expansion (including acquisition of real estate and improvements) and purchase of machinery and equipment. From time to time the Bank may make real estate lending for land acquisition, land development or open-end construction loans. The types of personal loans that are available include secured and unsecured loans for such purposes as financing automobiles, home improvements, education, lot acquisition, construction, home equity loans and personal investments. In the fourth quarter of 1993, a residential mortgage lending department was opened with mortgage loans being provided through correspondent relationships. The Bank originates, processes and closes the loan and sells (each individually) to a correspondent.

The Bank offers credit cards (through correspondent banking services) including MasterCard (TM) and Visa (TM) along with a personal checking account related line of credit. The line of credit is available for both protection against unexpected overdrafts and also for the convenience of having a pre-arranged loan that can be activated simply by a check drawn on a personal checking account. Other services offered, but not limited to, include safe deposit boxes, letters of credit, travelers checks, direct deposit of payroll, social security and dividend payments and automatic payment of insurance premiums and mortgage loans. The Bank does not have a proprietary automated teller machine but participates in a national ATM network through the Visa Debit Card Program. This service is called Check Card by the Bank and also offers purchases by the cardholder where Visa debit cards are accepted worldwide using a direct charge to their checking account. The Bank operates a courier service and ACH organization service as part of its deposit services for commercial customers. During 2001, the Bank introduced Internet Banking. This service is called ESafe by the Bank and offers twenty-four hour information, up-to-the minute account activity, automatic transfers or one-time transfers between accounts, actual images of customer checks, and statement viewing. All banking services are available through four banking house locations, 256 Meeting Street, Charleston, SC, 100 N. Main Street, Summerville, SC, 1337 Chuck Dawley Boulevard, Mt. Pleasant, SC, and 2027 Sam Rittenberg Boulevard, Charleston, SC.



The Company is a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended and as such, is under the supervisory and regulatory authority of the Board of Governors of the Federal Reserve System (the Federal Reserve). The Company is publicly traded on the National Association of Securities Dealers Automated Quotations (NASDAQ), and is under the reporting authority of the Securities and Exchange Commission (SEC). As a bank holding company registered under the laws of the South Carolina Bank Holding Company Act, the Company is also subject to regulation by the South Carolina State Board of Financial Institutions. Thus, the Company is required to file annual reports and other information with the Federal Reserve and the South Carolina State Board of Financial Institutions regarding its financial condition, results of operations, management and intercompany relationships and transactions between the Company and its subsidiaries.

The Company's subsidiary bank, The Bank of South Carolina, is a state chartered financial institution, and as such, is subject to various statutory requirements, supervision and regulation, of which regular bank examinations are a part, promulgated and enforced primarily by the Federal Deposit Insurance Corporation and the South Carolina State Board of Financial Institutions.

The Company's accounting policies are discussed in Item 7, Note 1 to the Consolidated Financial Statements. Of these significant accounting policies, the Company considers its policies regarding the allowance for loan losses to be its most critical accounting policy due to the significant degree of management judgment. For additional discussion concerning the Company's allowance for loan losses and related matters, see Item 6, Allowance for Loan Losses.

The Company was authorized by its Board of Directors at its December 1995, board meeting to repurchase up to 84,700 shares of its common stock on the open market from time to time, and, at its October, 1999 Board meeting, to repurchase up to 27,500 shares of its common stock on the open market from time to time, and, at its October, 2001 Board meeting, to repurchase up to 33,000 shares of its common stock on the open market from time to time. As of this date, 145,092 shares have been repurchased by the Company.

Compliance with federal, state and local provisions regulating the discharge of materials into the environment had no material effect on the capital expenditures, earnings and competitive position of the Bank in the fiscal year ended December 31, 2004.

At year end 2004, the Bank employed 64 people, 5 of whom are part time employees, none of whom are subject to a collective bargaining agreement. Management believes its relationship with its employees is excellent.

The business of the Bank is not considered to be seasonal nor is the Bank's business dependent on any one industry.

In the Bank's primary service area, there are 12 commercial banks, of which four are considered to have their headquarters in the Bank's service area. Of the 12 commercial banks, three have a large share of the market. These three are Wachovia Bank, N.A., Bank of America, N.A. and First Federal Savings and Loan Association. In addition, there are two savings banks and various credit unions with offices in the Tri-County Area. The Bank encounters strong competition from these financial institutions as well as consumer and commercial finance companies, insurance companies, brokerage firms and other financial institutions, some of which are not subject to the same degree of regulation and restrictions as the Bank. Many of these competitors have substantially greater resources and lending limits than the Bank has and offer certain services, such as trust and international banking services, which the Bank is not providing. The Bank does, however, provide a means for clearing international checks and drafts through a third party or correspondent bank.

Since January 1, 1986, South Carolina law has permitted regional interstate banking. Pursuant to such law, several of the banks in the Tri-County Area have been acquired by banks with headquarters outside the State of South Carolina. In addition, South Carolina laws permit statewide branching by banks and savings and loan associations. Accordingly,

the Bank could face increased competition from other banks and savings and loan associations not currently located in the Tri-County Area.



## **Item 2. Description of Property**

The Bank leases its headquarters and office facilities at 256 Meeting Street in downtown Charleston. Base rent is payable in equal monthly installments of \$27,899 in advance to be increased to \$29,014 in March 2005. The base rent will increase at the end of each rental year by the lesser of (i) 8% of the base rent or (ii) the percentage increase in the Consumer Price Index, Urban Index, For All Wage Earners, issued by the U.S. Department of Labor.

On June 30, 1995, the Bank was successful in renegotiating its 256 Meeting Street facilities lease for one hundred forty (140) months with two additional ten-year terms. Base rent was \$26,432 monthly payable in advance for the first twenty (20) months and the remaining one hundred twenty (120) months of the term (which began March 1, 1997) and for the two (2) extensions of the original term is \$24,801 per month in advance and is adjustable by 4% of the base rent every two years. In addition, the Bank leases adjacent parking facilities at \$2,928 per month.

In October of 1993, the Bank opened an office at 100 N. Main Street, Summerville, SC and entered into a lease agreement on August 9, 1993, with an original termination date of June 30, 1999, and two 5-year options to renew. In June of 2004, the bank was successful in renegotiating its 100 N. Main Street facilities lease beginning July 1, 2004 to an annual rent of \$30,725 with an increase of \$3,582 each year thereafter until July 1, 2009. The lease was a fixed rate of \$2,262 through July 1, 2009, however, the new lease was negotiated so that the bank could remain in its current location with the option to expand. At the end of the Five year term (June 30, 2009) The Bank of South Carolina will have three (3) ten (10) year options for renewal. During the renewal periods, the annual rent will be adjusted by the current Consumer Price Index (CPI) capped at 3% annually.

On November 1, 1995, the Bank entered into an agreement with an individual to lease property for construction of a new banking facility at 1337 Chuck Dawley Boulevard, Mt. Pleasant, SC. The original term of the lease is for fifteen (15) years with six (6) additional terms of five (5) years each. The base rent for the first ten (10) years will be \$2,250 per month paid in advance. Rent for years 11 through 15 and each six (6) option periods shall be adjusted to reflect an annualized return determined by multiplying the average yield on five (5) year U.S. Treasury Notes plus 150 basis points times an assumed raw land value of \$325,000. The monthly rent, however, shall never be less than the original rent of \$2,250 per month.

In the first quarter of 1997, the Bank purchased one acre of land for approximately \$838,000 in order to construct a full service banking office and operations center in the West Ashley community of Charleston. In March, 1998, the two-story, 12,000 square foot facility was completed at a cost of approximately \$1,334,000 representing construction costs and furnishings. At this same time, the Bank spent approximately \$839,000 to upgrade its computer system and to install a new check processing and check imaging system.

The Summerville facility is leased to the Bank by Summerville Solutions, LLC. Summerville Solutions, LLC was formed by Mary B. Graham, sister of Nathaniel I. Ball, III, Executive Vice President and Secretary of the Bank and the Company. No other Bank facilities are affiliated with any of the officers or directors of the Bank or the Company or any stockholders having more than five percent (5%) beneficial ownership of the Common Stock of the Company.

All leased properties are in good order and condition.

## **Item 3. Legal Proceedings**

In the opinion of management, there are no legal proceedings pending other than routine litigation incidental to its business. To the knowledge of management, no proceedings have been instituted or are contemplated by or against any governmental authority against or by the Company or The Bank.

**Item 4. Submission of Matters to a Vote of Security Holders**

No matters were submitted to a vote of security holders during the fourth quarter of the fiscal year ended December 31, 2004.

**PART II****Item 5. Market for the Company's Common Equity and Related Stockholder Matters**

There were issued and outstanding 2,805,610 shares of the 6,000,000 authorized shares of common stock of the Company at the close of the Company's fiscal year ended December 31, 2004. These outstanding shares were held by approximately 1,200 shareholders in nominee names and of record on December 31, 2004. The common stock of the Company is traded in the over-the-counter (OTC) market by five market making investment banking firms. These firms are The Robinson-Humphrey Company, Inc., Sterne, Agee & Leach, Inc., Scott and Stringfellow, Inc., Nite Securities LP and Speer, Leeds & Kellogg. Stock quotations are available through the National Association of Securities Dealers Automated Quotations (NASDAQ) where the Bank's shares are listed as BKSC.

According to information supplied by The Nasdaq Stock Market, the range of high and low bid quotations for each quarterly period in the fiscal years 2004, 2003 and 2002 has been as follows:

	2004		2003		2002	
	High	Low	High	Low	High	Low
First Quarter	14.50	13.00	11.51	10.01	15.25	13.54
Second Quarter	13.94	12.35	14.95	11.36	16.00	14.45
Third Quarter	13.34	11.35	14.66	13.38	15.44	11.75
Fourth Quarter	14.00	12.66	14.69	13.62	12.75	10.91

The Board of Directors of Bank of South Carolina Corporation declared quarterly dividends in 2004 of \$.11 per share to shareholders of record March 31, 2004, payable April 30, 2004; \$.11 per share to shareholders of record June 30, 2004, payable July 30, 2004; \$.11 per share to shareholders of record September 30, 2004, payable October 29, 2004; \$.11 per share to shareholders of record December 31, 2004, payable January 31, 2005.

The Board of Directors of Bank of South Carolina Corporation declared quarterly dividends in 2003 of \$.11 per share to shareholders of record March 31, 2003, payable April 30, 2003; 10% stock dividend to shareholders of record as of June 30, 2003, effective July 15, 2003; \$.11 per share to shareholders of record June 30, 2003, payable July 31, 2003; \$.11 per share to shareholders of record September 30, 2003, payable October 31, 2003; \$.11 per share to shareholders of record December 31, 2003, payable January 30, 2004.

The Board of Directors of Bank of South Carolina Corporation declared quarterly dividends in 2002 of \$.11 per share to shareholders of record April 1, 2002, payable April 30, 2002; \$.11 per share to shareholders of record July 1, 2002, payable July 31, 2002; \$.11 per share to shareholders of record September 30, 2002, payable October 31, 2002; \$.11 per share to shareholders of record December 31, 2002, payable January 31, 2003 and a special dividend of \$.15 per share to shareholders of record December 31, 2002, payable January 31, 2003.

As of January 1, 2005, there were approximately 1,200 shareholders of record with shares held by individuals and in nominee names, and on February 25, 2005, the market price for the common stock of the Company was \$14.01. It is the intent of the Company to continue paying dividends in the future.

Cash dividends, when declared, are paid by the Bank to the Company for distribution to shareholders of the Company. Certain regulatory requirements restrict the amount of dividends which the Bank can pay to the Company.

**Consolidated Financial Highlights**

	2004	2003	2002	2001	2000
<b>For December 31:</b>					
Net Income	\$ 1,845,623	\$ 1,904,713	\$ 1,858,319	\$ 1,802,951	\$ 2,371,375
Selected Year End Balances:					
Total Assets	201,235,286	187,342,649	169,480,463	158,466,073	159,776,502
Total Loans	129,107,437	125,235,883	127,887,401	118,492,932	104,262,014
Investment Securities					
Available for Sale	45,638,694	26,489,162	21,536,340	24,580,858	37,608,360
Federal Funds Sold and Resale Agreements	15,476,959	22,522,973	8,324,145	4,478,358	7,325,000
Interest Bearing Deposits in Other Banks					
	7,783	7,725	7,653	7,527	7,239
Earning Assets	190,230,873	174,255,743	157,755,539	147,559,675	149,202,613
Deposits	179,070,078	166,142,512	144,448,211	133,138,739	131,094,405
Shareholders Equity	19,990,716	19,647,839	19,314,129	19,301,495	18,554,282
Weighted Average Shares Outstanding-Diluted	2,816,751	2,815,587	2,812,816	2,836,623	2,838,865
<b>For the Year:</b>					
Selected Average Balances:					
Total Assets	192,034,402	174,154,907	162,207,337	161,089,339	155,717,433
Total Loans	123,923,761	130,056,441	117,654,356	108,786,605	98,994,148
Investment Securities					
Available for Sale	34,808,745	21,202,689	23,316,608	29,494,213	39,645,741
Investment Securities Held to Maturity					
					157,408
Federal Funds Sold and Resale Agreements	20,431,597	11,275,653	10,412,467	12,506,915	5,004,918
Interest Bearing Deposits in Other Banks					
	7,754	7,693	7,606	7,415	7,091
Earning Assets	179,171,857	162,542,476	151,391,038	150,795,148	143,809,306
Deposits	171,036,567	152,955,447	138,722,411	133,901,375	125,722,863
Shareholders Equity	19,904,862	19,626,907	19,474,929	19,251,627	17,650,334
<b>Performance Ratios:</b>					
Return on Average Equity	9.27%	9.70%	9.54%	9.37%	13.44%
Return on Average Assets	.96%	1.09%	1.15%	1.12%	1.52%
Average Equity to Average Assets	10.37%	11.27%	12.01%	11.95%	11.33%
Net Interest Margin	3.93%	4.36%	4.76%	5.05%	5.93%
Net Charge-offs to Average Loans	0.02%	0.15%	0.03%	0.64%	0.01%
	.81%	.93%	1.06%	1.01%	1.49%

Allowance for Loan Losses  
as a Percentage of Total  
Loans

**Per Share:**

Basic Earnings	\$	0.66	\$	0.68	\$	0.66	\$	0.64	\$	0.84
Diluted Earnings		0.66		0.68		0.66		0.64		0.84
Year End Book Value		7.13		7.00		6.94		6.83		6.20
Cash Dividends Declared		0.44		0.44		0.59		0.44		0.52
Dividend Payout Ratio		66.89%		61.87%		80.98%		62.86%		56.52%

Full Time Employee Equivalents		64		62		67		67		70
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All share and per share data have been restated to reflect a 10% stock dividend declared on June 19, 2003.

The following tables, as well as the previously presented consolidated financial highlights, set forth certain selected financial information concerning the Company and its wholly owned subsidiary. The information was derived from audited consolidated financial statements. The information should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations, which follows, and the audited consolidated financial statements and notes which are presented elsewhere in this report.

	<b>For Years Ended December 31,</b>				
	<b>2004</b>	<b>2003</b>	<b>2002</b>	<b>2001</b>	<b>2000</b>
<b>Operating Data:</b>					
Interest and fee income	\$ 7,904,128	\$ 7,855,161	\$ 8,565,542	\$ 11,100,801	\$ 12,781,576
Interest expense	857,801	764,647	1,364,804	3,491,281	4,254,428
Net interest income	7,046,327	7,090,514	7,200,738	7,609,520	8,527,148
(Recovery) provision for loan losses	(103,000)	9,230	195,000	335,000	315,000
Net interest income after (recovery) provision for loan losses	7,149,327	7,081,284	7,005,738	7,274,520	8,212,148
Other income	1,748,715	2,096,959	1,888,010	1,653,278	1,258,720
Other expense	6,073,609	6,261,182	6,088,861	6,205,237	5,840,493
Income before income taxes	2,824,433	2,917,061	2,804,887	2,722,561	3,630,375
Income tax expense	978,810	1,012,348	946,568	919,610	1,259,000
Net income	\$ 1,845,623	\$ 1,904,713	\$ 1,858,319	\$ 1,802,951	\$ 2,371,375
Basic income per share	\$ 0.66	\$ 0.68	\$ 0.66	\$ 0.64	\$ 0.84
Diluted income per share	\$ 0.66	\$ 0.68	\$ 0.66	\$ 0.64	\$ 0.84
Weighted average common shares-basic	2,805,610	2,805,610	2,807,259	2,836,385	2,838,865
Weighted average common shares diluted	2,816,751	2,815,587	2,812,816	2,836,623	2,838,865
Dividends per common share	\$ 0.44	\$ 0.44	\$ 0.59	\$ 0.44	\$ 0.52
	<b>As of December 31,</b>				
	<b>2004</b>	<b>2003</b>	<b>2002</b>	<b>2001</b>	<b>2000</b>
<b>Balance Sheet Data:</b>					
Investment securities available for sale	\$ 45,638,694	\$ 26,489,162	\$ 21,536,340	\$ 24,580,858	\$ 37,608,360
Total loans	129,107,437	125,235,883	127,887,401	118,492,932	104,262,014
Allowance for loan losses	1,043,901	1,169,627	1,361,438	1,201,091	1,558,530
Total assets	201,235,286	187,342,649	169,480,463	158,466,073	159,776,502
Total deposits	179,070,078	166,142,512	144,448,211	133,138,739	131,094,405
Shareholders' equity	19,990,716	19,647,839	19,314,129	19,301,495	18,554,282

All share and per share data have been restated to reflect a 10% stock dividend declared on June 19, 2003.

## **Item 6. Management's Discussion and Analysis or Plan of Operations**

Management's discussion and analysis is included to provide the shareholders with an expanded narrative of the Company's results of operations, changes in financial condition, liquidity and capital adequacy. This narrative should be reviewed in conjunction with the audited consolidated financial statements and notes included in this report. Since the primary asset of the Company is its wholly-owned subsidiary, most of the discussion and analysis relates to the Bank.

### **DISCUSSION OF FORWARD-LOOKING STATEMENTS**

Management's Discussion and Analysis of Financial Condition and Results of Operations and other portions of this annual report contain certain forward-looking statements concerning the future operations of the Bank of South Carolina Corporation. Management desires to take advantage of the safe harbor provisions of the Private Securities Litigation Reform Act of 1996 and is including this statement for the express purpose of availing the Company of protections of such safe harbor with respect to all forward-looking statements contained in this Form 10-KSB. We have used forward-looking statements to describe future plans and strategies including our expectations of the Company's future financial results. Management's ability to predict results or the effect of future plans or strategies is inherently uncertain. Factors which could affect actual results include interest rate trends, the general economic climate in the Company's market area and the country as a whole, the ability of the Company to control costs and expenses, the ability of the Company to successfully address competitive products and pricing, loan delinquency rates, and changes in federal and state regulation. These factors should be considered in evaluating the forward-looking statements and undue reliance should not be placed on such statements.

### **CRITICAL ACCOUNTING POLICIES**

The Company's significant accounting policies are set forth in Note One of the consolidated financial statements. Of these policies, the Company considers its policy regarding the allowance for loan losses to be its most critical accounting policy, because it requires many of management's most subjective and complex judgements. The Company has developed what it believes to be appropriate policies and procedures for assessing the adequacy of the allowance for loan losses, recognizing that this process requires a number of assumptions and estimates with respect to its loan portfolio. The Company's assessments may be impacted in future periods by changes in economic conditions, the impact of regulatory examinations and the discovery of information with respect to borrowers which were not known by management at the time of the issuance of the consolidated financial statements. For additional discussion concerning the Company's allowance for loan losses and related matters, see Allowance for Loan Losses .

### **OVERVIEW**

Earnings for the year were \$1,845,623 or basic and diluted earnings per share of \$.66 down 3% from 2003's earnings of \$1,904,713 or basic and diluted earnings per share of \$.68. Earnings for the fourth quarter of 2004 were \$524,929 or basic and diluted earnings per share of \$.19, up 23% from fourth quarter 2003 earnings of \$425,191 or basic and diluted earnings per share of \$.15. Our return on average equity and return on average assets for the year were 9.27% and .96%, respectively, compared to the 2003 return on average equity and return on average assets of 9.70% and 1.09%, respectively.

During 2004, the Company declared 4 regular quarterly cash dividends of \$.11 per share, thereby sharing its profits with its owners as it has in prior years.



### COMPARISON OF THE YEAR ENDED DECEMBER 31, 2004 TO DECEMBER 31, 2003

Net income decreased \$59,090 from \$1,904,713 for 2003, to \$1,845,623 for 2004 or 3% decreasing basic and diluted earnings per share to \$.66 for 2004, compared to basic and diluted earnings per share of \$.68 for 2003. This decrease is primarily due to a decrease in our interest earned on investment securities available for sale, mortgage banking income and service charge fees on business account, offset by an increase in other interest income and the recovery of loan loss reserve. Interest on investment securities available for sale decreased \$131,850 from \$1,008,160 for 2003 to \$876,310 for 2004. This decrease is due to the reinvestment of maturing securities at lower yields. Interest on federal funds sold increased \$140,550 from \$106,583 to \$247,133 or 1.32%. Mortgage banking income decreased \$278,555 from \$907,608 for 2003 to \$629,053 for 2004. The decrease in mortgage banking income is primarily due to the decrease in the volume of mortgage loan originations due to an increase in interest rates and an end to the refinance boom. The recovery of loan losses of (\$103,000) was attributable to improvements in classified and delinquent loans. Service charge fees on business accounts decreased \$31,950 to \$267,423 for 2004 from \$299,373 for 2003. The decrease in service charge fees on the business accounts was caused by an increase in the earnings credits and an increase in average balance maintained, which offset the service charges.

Net interest income depends upon the volume of and rates associated with interest earning assets and interest bearing liabilities, which result in the net interest spread. Net interest income decreased \$44,187 from \$7,090,514 for 2003 to \$7,046,327 for 2004. This decrease is primarily due to a decrease in interest earned on investment securities and an increase on interest paid on interest bearing liabilities, which resulted in a decline in our net interest margin and a change in asset mix from a decrease in loans and mortgage loans held for sale and an increase in lower earning federal funds sold and investment securities. Net interest margin decreased from 4.36% for the year ended December 31, 2003 to 3.93% for the year ended December 31, 2004.

Total interest and fee income increased .62% or \$48,967 to \$7,904,128 at year ended December 31, 2004 from \$7,855,161 at year ended December 31, 2003. This increase in interest and fee income is due to an increase in average earning assets. Average interest earning assets increased from \$162,542,476 for the year ended December 31, 2003 to \$179,171,857 for the year ended December 31, 2004 primarily due to an increase in average investments available for sale of \$13,606,056 between periods. The yield on interest earning assets decreased 42 basis points between years to 4.41% for the year ended December 31, 2004 compared to 4.83% for the year ended December 31, 2003. The decrease in yield on average interest earning assets is due to a decrease in the yield on average investments available for sale of 223 basis points to 2.52% for the year ended December 31, 2004 compared to 4.75% for the year ended December 31, 2003.

Total interest expense increased 12.18% or \$93,154 to \$857,801 at December 31, 2004 from \$764,647 at year end December 31, 2003. The increase in interest expense is primarily due to an increase in the interest bearing liabilities. Interest paid on deposits for the year ended December 31, 2004, was \$851,053 compared to \$757,755 for the year ended December 31, 2003, an increase of \$93,298 or 12.31%. Total interest bearing deposits averaged approximately \$117,249,815 for the year ended December 31, 2004 compared to \$105,977,713 for the year ended December 31, 2003. The average cost of interest bearing liabilities was .73% and .72% for the years ended December 31, 2004 and 2003, respectively.

The total recovery of loan losses for 2004 was (\$103,000) compared to a provision for loan losses of \$9,230 for 2003. The decrease in the provision is attributable to improvements in classified and delinquent loans. The allowance for loan losses as a percentage of total loans decreased from .93% in 2003 to .81% in 2004. Management believes the allowance for loan losses is adequate to absorb probable losses in the loan portfolio based on an evaluation at December 31, 2004; however, assessing adequacy of the allowance is a process that requires considerable judgement. For further discussion, see Non-accrual and Past Due Loans and Allowance for Loan Losses.

Total other income decreased from \$2,096,959 for 2003, to \$1,748,715 for 2004. This decrease is attributable to a decrease in service charges, fees and commissions, a decrease in mortgage banking income, as well as a decrease in other non-interest income. Service charges, fees and commissions decreased \$33,681 or 3.00% to \$1,090,395 for the year ended December 31, 2004, from \$1,124,076 for the year ended December 31, 2003 due to a decrease in service charges. The

decrease in service charges on the business accounts was caused by an increase in the earnings credits and an increase in average balance maintained, which offset the service charges. Mortgage banking income decreased \$278,555 or 30.69% to \$629,053 for the year ended December 31, 2004, from \$907,608 for the year ended December 31, 2003, due to a decrease in the volume of mortgage loan originations. Gain on the sale of other real estate owned was \$36,312 in 2003 and \$0 in 2004.

Salaries and employee benefits decreased \$114,759 or 3.19% to \$3,483,438 for the year ended December 31, 2004 from \$3,598,197 for the year ended December 31, 2003. This decrease is primarily due to a decrease in salaries and employee benefits as a result of the resignation of a loan officer whose position the Company decided not to fill at this time and another officer currently on an extended medical leave of absence.

Net occupancy expense decreased \$30,975 from \$1,233,608 for 2003 to \$1,202,633 for 2004. This decrease is primarily due to a decrease in depreciation expense on furniture and fixtures and equipment and on automobiles. Depreciation expense decreased due to several assets, which are still in use, becoming fully depreciated during 2004.

Total other expense decreased \$187,573 from \$6,261,182 for 2003 to \$6,073,609 for 2004. Other operating expenses decreased \$41,839 or 2.93% to \$1,387,538 for the year ended December 31, 2004 from \$1,429,377 for the year ended December 31, 2003. This decrease is primarily due to a decrease in expenses associated with postage, packages and non-postal shipments and mileage.

Income tax expense decreased from \$1,012,348 for 2003 to \$978,810 for 2004 due to lower income levels. The Company's effective tax rate was approximately 35% for the year ended December 31, 2004 and 35% for the year ended December 31, 2003.

#### **COMPARISON OF THE YEAR ENDED DECEMBER 31, 2003 TO DECEMBER 31, 2002**

Net income increased \$46,394 from \$1,858,319 for 2002, to \$1,904,713 for 2003 or 2.50% increasing basic and diluted earnings per share to \$.68 for 2003, compared to basic and diluted earnings per share of \$.66 for 2002. This increase is primarily due to an increase in our service charges, mortgage banking income and a gain on the sale of other real estate owned.

Net interest income depends upon the volume of and rates associated with interest earning assets and interest bearing liabilities, which result in the net interest spread. Net interest income decreased \$110,224 from \$7,200,738 for 2002 to \$7,090,514 for 2003. This decrease is primarily due to a decline in interest rates, which resulted in a decline in our net interest margin. The net interest margin decreased to 4.36% in 2003 from 4.76% in 2002.

Total interest and fee income decreased 8.29% or \$710,381 in 2003. This decrease in interest and fee income is due to a decrease in average yield of interest earning assets. Average interest earning assets increased from \$151,391,038 for the year ended December 31, 2002 to \$162,542,476 for the year ended December 31, 2003 primarily due to an increase in average loans of \$12,402,085 between periods. The yield on interest earning assets decreased 83 basis points between years to 4.83% for the year ended December 31, 2003 compared to 5.66% for the year ended December 31, 2002. The decrease in yield on average interest earning assets is due to a decrease in the yield on average loans of 72 basis points to 5.18% for the year ended December 31, 2003 compared to 5.90% for the year ended December 31, 2002, as well as a decrease in the yield on average securities available for sale of 151 basis points, a decrease in the yield on average federal funds sold of 58 basis points and a decrease in the yield on other average short term investments of 74 basis points. The decrease in yield on average loans is due to the fact that the majority of the Bank's loans reprice with the Bank's prime rate. The Bank's prime rate was 4.125% and 4.25% at December 31, 2003 and 2002, respectively.

Total interest expense decreased 43.97% or \$600,157 in 2003. The decrease in interest expense is primarily due to the decrease

in the average cost of funds. Interest paid on deposits for the year ended December 31, 2003, was \$757,755 compared to \$1,325,507 for the year ended December 31, 2002, a decrease of \$567,752 or 42.83%. Total interest bearing deposits averaged approximately \$105,977,713 for the year ended December 31, 2003 compared to \$98,344,569 for the year ended December 31, 2002. The average cost of deposits decreased 63 basis points from 1.35% for the year ended December 31, 2002 to .72% for the year ended December 31, 2003. Interest on short-term borrowings decreased \$32,405 or 82.46% to \$6,892 for the year ended December 31, 2003, from \$39,297 for the year ended December 31, 2002. Short-term borrowings consist of federal funds purchased, demand notes to the U. S. Treasury and securities sold under agreement to repurchase. Short-term borrowings averaged approximately \$798,383 for the year ended December 31, 2003 compared to approximately \$3,423,874 for the year ended December 31, 2002. The average cost of interest bearing liabilities was .72% and 1.34% for the years ended December 31, 2003 and 2002, respectively.

The provision for loan losses decreased from \$195,000 for 2002 to \$9,230 for 2003. The decrease in the provision is attributable to improvements in classified and delinquent loans. The allowance for loan losses as a percentage of total loans decreased from 1.06% in 2002 to .93% in 2003. Management believes the allowance for loan losses is adequate to absorb inherent losses in the loan portfolio based on an evaluation at December 31, 2003. For further discussion, see Non-accrual and Past Due Loans and Allowance for Loan Losses.

Total other income increased from \$1,888,010 for 2002, to \$2,096,959 for 2003. This increase is attributable to an increase in service charges, fees and commissions, an increase in mortgage banking income, as well as a gain on the sale of other real estate owned. Service charges, fees and commissions increased \$65,468 or 6.18% to \$1,124,076 for the year ended December 31, 2003, from \$1,058,608 for the year ended December 31, 2002 due to an increase in fees charged on accounts and an increase in average deposits. The mortgage banking income increased \$116,151 or 14.68% to \$907,608 for the year ended December 31, 2003, from \$791,457 for the year ended December 31, 2002, due to an increase in the volume of mortgage loan originations. Other non-interest income increased \$62,335 to \$65,275 for the year ended December 31, 2003, from \$2,940 for the year ended December 31, 2002, due to a \$36,311 gain on the sale of other real estate.

Total other expense increased \$172,321 from \$6,088,861 for 2002 to \$6,261,182 for 2003. Other operating expenses increased \$47,419 or 3.43% to \$1,429,377 for the year ended December 31, 2003 from \$1,381,958 for the year ended December 31, 2002. This increase is primarily due to an increase in expenses associated with business development and professional audit fees.

Salaries and employee benefits increased \$156,959 or 4.56% to \$3,598,197 for the year ended December 31, 2003 from \$3,441,238 for the year ended December 31, 2002. This increase is primarily due to an increase in salaries and employee benefits as a result of annual merit increases.

Income tax expense increased from \$946,568 for 2002 to \$1,012,348 for 2003. The Company's effective tax rate was approximately 35% for the year ended December 31, 2003 and 34% for the year ended December 31, 2002.

### **ASSET AND LIABILITY MANAGEMENT**

The assets and liabilities of the Company are managed to provide a consistent level of liquidity to accommodate normal fluctuations in loans and deposits. At year end 2004, total assets were \$201,235,286 an increase of 7.42% from the end of the previous year, and total deposits were \$179,070,078, an increase of 7.78% from the end of the previous year, while short-term borrowings, consisting of Demand Notes Issued to U.S. Treasury, increased \$507,975 or 53.25% to \$1,461,929 for the year ended December 31, 2004 from \$953,954 for the year ended December 31, 2003.



At December 31, 2004, approximately 95% of the Company's assets were earning assets composed of U.S. Treasury, Federal Agency and municipal securities in the amount of \$45,638,694, Federal Funds Sold and interest bearing deposits in other banks in the amount of \$15,484,742, and loans in the amount of \$129,107,437.

The yield on a majority of the Company's earning assets adjusts simultaneously with changes in the general level of interest rates. Some of the Company's liabilities are issued with fixed terms and can be repriced only at maturity. During 2002 and 2003 loans continued to grow at a faster rate than deposits, however, our net interest margin declined by 29 basis points from January to December 2002 and 40 basis points from January to December 2003 with the decline in interest rates. During 2004 deposits grew at a faster rate than loans and our net interest margin decreased 43 basis points from January to December.

### **MARKET RISK**

Market risk is the risk of loss from adverse changes in market prices and rates. For the Company, this risk is constituted primarily of interest rate risk in its lending and investing activities as they relate to their funding by deposit and borrowing activities.

The Bank's policy is to minimize interest rate risk between interest bearing assets and liabilities at various maturities and to attempt to maintain an asset positive position over a 6 month period. In adhering to this policy, unless there is a sudden extraordinary drop in the interest rate, it is anticipated that the Bank's net interest margins will not be materially affected by changes in interest rates. The net interest rate spread for 2004 decreased to 3.68% from 4.12% for 2003 and the net interest margin for 2004 decreased to 3.93% from 4.36% for 2003. Management will continue to monitor its asset sensitive position.

Since the rates on most of the Bank's interest bearing liabilities can vary on a daily basis, management continues to maintain a loan portfolio priced predominately on a variable rate basis. The Bank seeks stable, long-term deposit relationships to fund its loan portfolio.

At December 31, 2004, the average maturity of the investment portfolio was 4 months with an average yield of 2.53% compared to 7 months with an average yield of 3.11% at December 31, 2003.

The Bank does not own, nor has it ever purchased, derivative financial instruments. The Company does not take foreign exchange or commodity risks.

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The following table summarizes the Bank's interest sensitivity position as of December 31, 2004:

Earning Assets	1 Day	3	6	1 Year	5 years or More	Total	Estimated Fair Value	
		Less Than 3 Months	to Less Than 6 Months	to Less Than 1 Year				to Less Than 5 Years
(in 000 s)								
Loans	\$ 118,530	\$ 4,871	\$ 3,222	\$ 899	\$ 1,465	\$ 120	\$ 129,107	\$ 129,360
Investment securities		23,944	12,024	8,099	1,255	200	45,522	45,639
Short term investments	8						8	8
Federal funds sold	15,477						15,477	15,477
Total	\$ 134,015	\$ 28,815	\$ 15,246	\$ 8,998	\$ 2,720	\$ 320	\$ 190,114	\$ 190,484
<b>Interest Bearing Liabilities</b>								
(in 000 s)								
CD's and other time deposits 100,000 and over	\$	\$ 14,781	\$ 4,051	\$ 404	\$ 218	\$	\$ 19,454	\$ 19,433
CD's and other time deposits under 100,000	114	5,243	2,986	2,724	668		11,735	11,633
Money market and interest bearing demand accounts	77,814						77,814	77,814
Savings	15,416						15,416	15,416
Short term borrowings	1,462						1,462	1,462
	\$ 94,806	\$ 20,024	\$ 7,037	\$ 3,128	\$ 886	\$	\$ 125,881	\$ 125,758
Net	\$ 39,209	\$ 8,791	\$ 8,209	\$ 5,870	\$ 1,834	\$ 320	\$ 64,233	\$ 64,726
Cumulative		\$ 48,000	\$ 56,209	\$ 62,079	\$ 63,913	\$ 64,233		

**LIQUIDITY**

Historically, the Company has maintained its liquidity at levels believed by management to be adequate to meet requirements of normal operations, potential deposit outflows and strong loan demand and still allow for optimal investment of funds and return on assets. The following table summarizes future contractual obligations as of December 31, 2004:

**Payment Due by Period**  
**Less than 1-5 After 5**



	<b>Total</b>	<b>1 Year</b>	<b>Years</b>	<b>Years</b>
<b>Contractual Obligations (in 000 s)</b>				
Time deposits	\$ 31,189	\$ 30,303	\$ 886	\$
Short-term borrowings	1,462	\$ 1,462	\$	\$
Operating leases	1,227	444	738	45
Total contractual cash obligations	\$ 33,878	\$ 32,209	\$ 1,624	\$ 45

The Bank manages its assets and liabilities to ensure that there is sufficient liquidity to enable management to fund deposit withdrawals, loan demand, capital expenditures, reserve requirements, operating expenses and dividends and to manage daily operations on an ongoing basis. Funds are primarily provided by the Bank through customer s deposits, principal and interest payments on loans, mortgage loan sales, the sale or maturity of securities, temporary investments and earnings.

Proper liquidity management is crucial to ensure that the Company is able to take advantage of new business opportunities

as well as meet the demands of its customers. Investment securities are an important tool in the Company's liquidity management. Securities classified as available for sale may be sold in response to changes in interest rates, liquidity needs and/or significant prepayment risk. All of the securities presently owned by the Bank are classified as Available for Sale. Net cash provided by operations and deposits from customers have been the primary sources of liquidity for the Company. At December 31, 2004, the Bank had unused short-term lines of credit totaling approximately \$18,500,000 (which are withdrawable at the lender's option). Management believes that these sources are adequate to meet its liquidity needs. Liquidity at the parent company level is provided through cash dividends from the Bank and the capacity of the parent company to raise additional borrowed funds as needed.

Composition of Average Assets

	2004	2003	2002	2001	2000
Loans	\$ 123,923,761	\$ 130,056,441	\$ 117,654,356	\$ 108,786,605	98,994,148
Investment securities available for sale	34,808,745	21,202,689	23,316,609	29,494,213	39,645,741
Investment securities held to maturity					157,408
Federal funds sold and other investments	20,439,351	11,283,346	10,420,073	12,514,330	5,012,009
Non-earning assets	12,862,545	11,612,431	10,816,299	10,294,191	11,908,127
<b>Total average assets</b>	<b>\$ 192,034,402</b>	<b>\$ 174,154,907</b>	<b>\$ 162,207,337</b>	<b>\$ 161,089,339</b>	<b>\$ 155,717,433</b>

Average earning assets increased by \$16,629,381 from 2003 to 2004 while average non-earning assets increased by \$1,250,114. Average earning assets increased primarily as a result of investment securities available for sale and federal funds sold and other investments.

Average investment securities available for sale for 2004 were up \$13,606,056 or 64.17% from 2003. The majority of the increase is primarily due to an increase in deposits and a decrease in loans during 2004.

**ANALYSIS OF CHANGES IN NET INTEREST INCOME**

The following table shows changes in interest income and expense based upon changes in volume and changes in rates:

	2004 vs. 2003			2003 vs. 2002			2002 vs. 2001		
	Volume	Rate	Net Dollar Change (1)	Volume	Rate	Net Dollar Change (1)	Volume	Rate	Net Dollar Change (1)
Loans	\$ (325,958)	\$ 366,225	\$ 40,267	\$ 690,831	\$ (897,305)	\$ (206,474)	\$ 675,336	\$ (2,568,308)	\$ (1,892,972)
Investment securities available for sale	471,317	(603,167)	(131,850)	(123,551)	(327,057)	(450,608)	(385,942)	32,378	(353,564)
	104,505	36,045	140,550	12,343	(65,642)	(53,299)	(65,345)	(223,378)	(288,723)

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Federal funds  
sold and and  
other  
investments

Interest Income \$ 249,864 \$ (200,897) \$ 48,967 \$ 579,623 \$ (1,290,004) \$ (710,381) \$ 224,049 \$ (2,759,308) \$ (2,535,259)

Interest-bearing  
transaction

accounts \$ 43,707 \$ 96,624 \$ 140,331 \$ 42,741 \$ (306,380) \$ (263,639) \$ 140,552 \$ (827,556) \$ (687,004)

Savings 5,032 8,912 13,944 43,177 (98,753) (55,576) 58,257 (156,439) (98,182)

Certificates of  
deposit 10,001 (70,978) (60,977) (37,596) (210,941) (248,537) (341,945) (792,064) (1,134,009)

Federal funds  
purchased (268) (267) (535) 441 (39) 402 (4,195) (3,027) (7,222)

Securities sold  
under

agreements to  
repurchase (176) (175) (351) (15,582) (9,032) (24,614) (81,084) (97,783) (178,867)

Demand notes  
issued to U.S.

Treasury (969) 1,711 742 (3,731) (4,462) (8,193) (86) (21,107) (21,193)

Interest  
expense \$ 57,327 \$ 35,827 \$ 93,154 \$ 29,450 \$ (629,607) \$ (600,157) \$ (228,501) \$ (1,897,976) \$ (2,126,477)

Decrease in net  
interest income \$ (44,187) \$ (110,224) \$ (408,782)

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(1) Volume/Rate changes have been allocated to each category based on the percentage of each to the total change.

**YIELDS ON AVERAGE EARNING ASSETS AND RATES ON AVERAGE INTEREST-BEARING  
LIABILITIES**

	2004			2003			2002		
	Average Balance	Interest Paid/ Earned	Average Yield/ Rate	Average Balance	Interest Paid/ Earned	Average Yield/ Rate	Average Balance	Interest Paid/ Earned	Average Yield/ Rate
<b>Interest-Earning Assets</b>									
Loans	\$ 123,923,761	\$ 6,780,685	5.47%	\$ 130,056,441	\$ 6,740,418	5.18%	\$ 117,654,356	\$ 6,946,892	5.90%
Investment securities available for sale	34,808,745	876,310	2.52%	21,202,689	1,008,160	4.75%	23,316,609	1,458,768	6.26%
Investment securities held to maturity									
Federal funds sold	20,431,597	247,074	1.21%	11,275,653	106,512	.95%	10,412,467	159,756	1.53%
Other investments	7,754	59	.76%	7,693	71	.92%	7,606	126	1.66%
Total earning assets	\$ 179,171,857	\$ 7,904,128	4.41%	\$ 162,542,476	\$ 7,855,161	4.83%	\$ 151,391,038	\$ 8,565,542	5.66%
<b>Interest-Bearing Liabilities:</b>									
Interest bearing transaction accounts	\$ 73,133,008	\$ 397,343	.54%	\$ 63,385,795	\$ 257,012	.41%	\$ 58,211,499	\$ 520,651	.89%
Savings	15,611,552	99,281	.64%	14,771,142	85,337	.58%	10,547,694	140,913	1.34%
Certificates of deposit	28,505,255	354,429	1.24%	27,820,776	415,406	1.49%	29,585,376	663,943	2.24%
Federal funds purchased				35,890	535	1.49%	6,781	133	1.96%
Securities sold under agreement to repurchase				77,284	351	.45%	2,412,766	24,965	1.03%
Demand notes issued to U.S. Treasury	584,736	6,748	1.15%	685,209	6,006	.88%	1,004,327	14,199	1.41%
Total interest bearing liabilities	\$ 117,834,551	\$ 857,801	.73%	\$ 106,776,096	\$ 764,647	.72%	\$ 101,768,443	\$ 1,364,804	1.34%
Net interest spread			3.68%			4.12%			4.32%

Net interest margin	3.93%	4.36%	4.76%
Net interest income	\$ 7,046,327	\$ 7,090,514	\$ 7,200,738

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(1) The effect of forgone interest income as a result of non-accrual loans was not considered in the above analysis. Average loan balances include non-accrual loans.

**INVESTMENT PORTFOLIO**

The following is a schedule of the Bank's investment portfolio as of December 31, 2004, as compared to December 31, 2003, 2002:

	<b>DECEMBER 31, 2004</b>			<b>ESTIMATED FAIR VALUE</b>
	<b>AMORTIZED COST</b>	<b>GROSS UNREALIZED GAINS</b>	<b>GROSS UNREALIZED LOSSES</b>	
U.S. Treasury Bills	\$ 39,786,310	\$	\$ (37,021)	\$ 39,749,289
Other U.S. Treasury Obligations	1,998,258	33,742		2,032,000
Federal Agency Securities	1,997,889	40,111		2,038,000
Municipal Securities	1,740,000	79,405		1,819,405
<b>Total</b>	<b>\$ 45,522,457</b>	<b>\$ 153,258</b>	<b>\$ (37,021)</b>	<b>\$ 45,638,694</b>

	<b>DECEMBER 31, 2003</b>			<b>ESTIMATED FAIR VALUE</b>
	<b>AMORTIZED COST</b>	<b>GROSS UNREALIZED GAINS</b>	<b>GROSS UNREALIZED LOSSES</b>	
U.S. Treasury Bills	\$ 15,973,833		(5,273)	15,968,560
Other U.S. Treasury Obligations	3,998,249	\$ 191,751	\$	\$ 4,190,000
Federal Agency Securities	3,980,006	239,374		4,219,380
Municipal Securities	1,995,000	116,222		2,111,222
<b>Total</b>	<b>\$ 25,947,088</b>	<b>\$ 547,347</b>	<b>\$ (5,273)</b>	<b>\$ 26,489,162</b>

	<b>DECEMBER 31, 2002</b>			<b>ESTIMATED FAIR VALUE</b>
	<b>AMORTIZED COST</b>	<b>GROSS UNREALIZED GAINS</b>	<b>GROSS UNREALIZED LOSSES</b>	
U.S. Treasury Bills	\$			
Other U.S. Treasury Obligations	11,977,259	\$ 529,641	\$	\$ 12,506,900
Federal Agency Securities	5,932,378	509,502		6,441,880
Municipal Securities	2,465,000	122,560		2,587,560
<b>Total</b>	<b>\$ 20,374,637</b>	<b>\$ 1,161,703</b>	<b>\$</b>	<b>\$ 21,536,340</b>

The Bank's investment portfolio had a weighted average yield of 2.53%, 3.11% and 6.26% at December 31, 2004, 2003 and 2002, respectively.



**LOAN PORTFOLIO COMPOSITION**

The following is a schedule of the Bank's loan portfolio as of December 31, 2004, as compared to December 31, 2003, 2002, 2001 and 2000:

<b>Type</b>	<b>Book Value (in 000 \$)</b>				
	2004	2003	2002	2001	2000
Commercial and industrial loans	\$ 44,829	\$ 46,687	\$ 46,908	\$ 52,646	\$ 47,797
Real estate loans	77,797	71,289	75,053	59,024	48,839
Loans to individuals for household, family and other personal expenditures	6,256	7,045	5,863	6,778	7,331
All other loans (including overdrafts)	225	215	63	45	295
<b>Total Loans (excluding unearned income)</b>	<b>\$ 129,107</b>	<b>\$ 125,236</b>	<b>\$ 127,887</b>	<b>\$ 118,493</b>	<b>\$ 104,262</b>

As a Bank whose mission is to serve its community, there is a geographic concentration of loans in Charleston, Dorchester and Berkeley Counties.

The Bank had no foreign loans or loans to fund leveraged buyouts (LBO's) during 2004, 2003, 2002, 2001 or 2000.

**SELECTED LOAN MATURITY (in 000 \$)**

<b>Type</b>	Over one but less			<b>Total</b>
	One year or less	than five years	Over five years	
Commercial and industrial loans	\$ 20,912	\$ 17,153	\$ 6,764	\$ 44,829
Real Estate Loans	18,339	10,069	49,389	77,797
Loans to individuals for household, family and other personal expenditures	1,983	2,932	1,341	6,256
All other loans (including overdrafts)	171	54		225
<b>Total Loans (excluding unearned income)</b>	<b>\$ 41,405</b>	<b>\$ 30,208</b>	<b>\$ 57,494</b>	<b>\$ 129,107</b>

**IMPAIRED AND RESTRUCTURED LOANS**

The Bank had impaired loans totaling \$65,751 as of December 31, 2004 compared to \$128,504, \$198,309, \$169,807 and \$294,030 as of December 31, 2003, 2002, 2001 and 2000, respectively. The impaired loans include non-accrual loans with balances at December 31, 2004, 2003, 2002, 2001 and 2000 of \$65,751, \$102,588, \$198,309, \$161,500 and \$283,323, respectively. The Bank had no restructured loans at December 31, 2004, one restructured loan in the amount of \$25,916 at December 31, 2003, no restructured loans at December 31, 2002, one restructured loan in the amount of \$8,307 at December 31, 2001 and one restructured loan in the amount of \$10,707 at December 31, 2000. Management does not know of any loans, which will not meet their contractual obligations that are not otherwise discussed herein.





### **NON-ACCRUAL AND PAST DUE LOANS**

The Bank had \$65,751 in non-accrual loans as of December 31, 2004, compared to \$102,588, \$198,309, \$161,500 and \$283,323 as of December 31, 2003, 2002, 2001 and 2000, respectively. There were no loans over 90 days past due still accruing interest at December 31, 2004 compared to \$163,202 as of December 31, 2003.

The accrual of interest is generally discontinued on loans, which become 90 days past due as to principal or interest. The accrual of interest on some loans, however, may continue even though they are 90 days past due if the loans are well secured, in the process of collection, and management deems it appropriate. If non-accrual loans decrease their past due status to 30 days for a period of six months, they are reviewed individually by management to determine if they should be returned to accrual status.

### **ALLOWANCE FOR LOAN LOSSES**

The provision for loan losses is based on management's and the Loan Committee's review and evaluation of the loan portfolio and general economic conditions on a monthly basis and by the Board of Directors on a quarterly basis. Management's review and evaluation of the allowance for loan losses is based on an analysis of historical trends, sig