FIRST MARINER BANCORP
Form 10-Q
November 07, 2011

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2011.

o **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: 0-21815

FIRST MARINER BANCORP
(Exact name of registrant as specified in its charter)

Maryland		**52-1834860**
(State of Incorporation)		(I.R.S. Employer Identification Number)
1501 South Clinton Street, Baltimore, MD	**21224**	**410-342-2600**
(Address of principal executive offices)	(Zip Code)	(Telephone Number)

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 during the preceding 12 months (or for such shorter period that the registrant was required to file such report, and (2) has been subject to such filing requirements for the past 90 days.
Yes x 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 x No o (Not Applicable)

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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer o Non-accelerated filer o Smaller reporting company x

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

The number of shares of common stock outstanding as of November 3, 2011 is 18,860,482 shares.

FIRST MARINER BANCORP AND SUBSIDIARIES
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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

Some of our statements contained in, or incorporated by reference into, this Quarterly Report on Form 10-Q are 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. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 and are including this statement for purposes of invoking these safe harbor provisions. Forward-looking statements are not guarantees of performance or results. When we use words like may, plan, contemplate, anticipate, believe, intend, co expect, project, predict, estimate, target, could, is likely, should, would, will, and similar expressions, you should consider the forward-looking statements, although we may use other phrasing. These forward-looking statements involve risks and uncertainties and are based on our beliefs and assumptions and on the information available to us at the time that these disclosures were prepared. These forward-looking statements involve risks and uncertainties and may not be realized due to a variety of factors, including, but not limited to, the following:

the strength of the United States economy in general, the strength of the local economies in which we conduct operations, and the unfavorable effects of future economic conditions, including inflation, recession, or a continuing decrease in real estate values;

geopolitical conditions, including acts or threats of terrorism, actions taken by the United States or other governments in response to acts or threats of terrorism and/or military conflicts, which could impact business and economic conditions in the United States and abroad;

the effects of, and changes in, trade, monetary, and fiscal policies and laws, including interest rate policies of the Federal Reserve Board, inflation, interest rate, market, and monetary fluctuations;

the risks of changes in interest rates on the level and composition of deposits, loan demand, and the values of loan collateral, securities, and interest sensitive assets and liabilities;

the effect of changes in accounting policies and practices, as may be adopted from time-to-time by bank regulatory agencies, the Securities and Exchange Commission, the Financial Accounting Standards Board, or other accounting standards setters;

adverse changes in the securities markets;

the effects of competition from other commercial banks, thrifts, mortgage-banking firms, consumer finance companies, credit unions, securities brokerage firms, insurance companies, money market and other mutual funds, and other financial institutions operating in our market area and elsewhere, including institutions operating regionally, nationally, and internationally, together with competitors offering banking products and services by mail, telephone, and the Internet;

costs and potential disruption or interruption of operations due to cyber security incidents;

a decline in demand for our products and services;

an inability to attract and retain deposits;

the timely development of competitive new products and services and the acceptance of these products and services by new and existing customers;

changes in consumer spending and savings habits;

the effect of any mergers, acquisitions, or other transactions to which we or our subsidiary may from time to time be a party;

our ability to effectively manage market risk, credit risk, and operational risk;

unanticipated regulatory or judicial proceedings;

the success and timing of our business strategies and our ability to effectively carry out our business and capital plans;

our ability to continue to operate as a going concern;

our inability to realize the benefits from our cost saving initiatives;

our ability to meet our interest payment obligations on our junior subordinated deferrable interest debentures upon expiration of the deferral period in 2013;

All written or oral forward-looking statements attributable to us are expressly qualified in their entirety by this Cautionary Note. Our actual results may differ significantly from those we discuss in these forward-looking statements. For other factors, risks, and uncertainties that could cause our actual results to differ materially from estimates and projections contained in these forward-looking statements, please read the Risk Factors in Item 1A in Part II of this Quarterly Report on Form 10-Q, Item 1A in Part II of the Quarterly Reports on Form 10-Q for the quarters ended March 31, 2011 and June 30, 2011, and in Item 1A in Part I of our Annual Report on Form 10-K as of and for the year ended December 31, 2010. Any forward-looking statement speaks only as of the date which such statement was made, and, except as required by law, we expressly disclaim any obligation or undertaking to disseminate any updates or revisions to any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events.

PART I FINANCIAL INFORMATION

Item 1 Financial Statements

First Mariner Bancorp and Subsidiary
Consolidated Statements of Financial Condition
(dollars in thousands, except per share data)

	September 30, 2011	December 31, 2010
	(unaudited)	
ASSETS		
Cash and due from banks	$ 152,224	$ 169,557
Federal funds sold and interest-bearing deposits	34,440	48,404
Securities available for sale, at fair value	22,646	27,826
Loans held for sale, at fair value	126,191	140,343
Loans receivable	736,672	811,687
Allowance for loan losses	(14,112)	(14,115)
Loans, net	722,560	797,572
Real estate acquired through foreclosure	24,739	21,185
Restricted stock investments	6,969	7,095
Premises and equipment, net	38,927	41,068
Accrued interest receivable	3,848	3,844
Bank-owned life insurance	37,172	36,188
Prepaid expenses and other assets	27,945	16,555
Total assets	$ 1,197,661	$ 1,309,637
LIABILITIES AND STOCKHOLDERS (DEFICIT) EQUITY		
Liabilities:		
Deposits:		
Noninterest-bearing	$ 103,153	$ 103,450
Interest-bearing	928,725	1,018,439
Total deposits	1,031,878	1,121,889
Short-term borrowings	44,062	84,399
Long-term borrowings	73,746	33,888
Junior subordinated deferrable interest debentures	52,068	52,068
Accrued expenses and other liabilities ($48 and $137 at fair value, respectively)	17,479	13,647
Total liabilities	1,219,233	1,305,891
Stockholders (deficit) equity:		
Common stock, $.05 par value; 75,000,000 shares authorized; 18,860,482 and 18,050,117 shares issued and outstanding at September 30, 2011 and December 31, 2010, respectively	939	902
Additional paid-in capital	80,102	79,667
Retained deficit	(99,479)	(73,210)
Accumulated other comprehensive loss	(3,134)	(3,613)
Total stockholders (deficit) equity	(21,572)	3,746

Total liabilities and stockholders (deficit) equity	$ 1,197,661	$ 1,309,637

See accompanying notes to the consolidated financial statements

First Mariner Bancorp and Subsidiary
Consolidated Statements of Operations
(dollars in thousands except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	**2010**	**2011**	**2010**
	(unaudited)		*(unaudited)*	
Interest income:				
Loans	$ 11,222	$ 13,270	$ 33,867	$ 39,531
Investments and other earning assets	455	509	1,651	1,945
Total interest income	11,677	13,779	35,518	41,476
Interest expense:				
Deposits	3,625	4,895	12,217	15,957
Short-term borrowings	61	99	232	232
Long-term borrowings	852	932	2,476	3,583
Total interest expense	4,538	5,926	14,925	19,772
Net interest income	7,139	7,853	20,593	21,704
Provision for loan losses	5,000	9,750	11,580	16,290
Net interest income (loss) after provision for loan losses	2,139	(1,897)	9,013	5,414
Noninterest income:				
Total other-than-temporary impairment (OTTI) charges	(299)	(302)	(327)	(609)
Less: Portion included in other comprehensive income (pre-tax)	(382)	(514)	(491)	(640)
Net OTTI charges on securities available for sale	(681)	(816)	(818)	(1,249)
Mortgage-banking revenue	4,609	8,804	7,942	13,499
ATM fees	755	745	2,314	2,279
Gain on debt exchange				958
Service fees on deposits	717	933	2,194	3,109
Gain on financial instruments carried at fair value		331		1,661
Gain on sale of securities available for sale	638		781	54
Gain on sale of premises and equipment	2	2	4	192
Commissions on sales of nondeposit investment products	75	110	347	381
Income from bank-owned life insurance	316	353	984	1,066
Other	1,289	154	1,779	589
Total noninterest income	7,720	10,616	15,527	22,539
Noninterest expense:				
Salaries and employee benefits	5,876	6,501	18,003	19,409
Occupancy	2,202	2,297	6,407	6,863
Furniture, fixtures, and equipment	426	585	1,357	1,800
Professional services	1,259	838	3,742	2,149
Advertising	219	153	470	420
Data processing	393	460	1,237	1,343
ATM servicing expenses	217	227	655	655
Write-downs, losses, and costs of real estate acquired through foreclosure	3,218	1,849	6,635	6,393
FDIC insurance premiums	878	1,029	3,390	2,927
Service and maintenance	594	559	1,872	1,756

Corporate insurance	388	301	1,069	902
Consulting fees	377	333	1,042	745
Loan collection expenses	329	785	608	1,176
Other	1,443	1,862	4,322	4,668
Total noninterest expense	17,819	17,779	50,809	51,206
Net loss from continuing operations before income taxes and discontinued operations	(7,960)	(9,060)	(26,269)	(23,253)
Income tax benefit - continuing operations		(4,452)		(10,748)
Net loss from continuing operations	(7,960)	(4,608)	(26,269)	(12,505)
Loss from discontinued operations				(200)
Net loss	$ (7,960)	$ (4,608)	$ (26,269)	$ (12,705)

First Mariner Bancorp and Subsidiary
Consolidated Statements of Operations (Continued)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
	(unaudited)		*(unaudited)*	
Net loss per common share from continuing operations:				
Basic	$ (0.42)	$ (0.26)	$ (1.41)	$ (0.92)
Diluted	$ (0.42)	$ (0.26)	$ (1.41)	$ (0.92)
Net loss per common share from discontinued operations:				
Basic	$	$	$	$ (0.01)
Diluted	$	$	$	$ (0.01)
Net loss per common share:				
Basic	$ (0.42)	$ (0.26)	$ (1.41)	$ (0.93)
Diluted	$ (0.42)	$ (0.26)	$ (1.41)	$ (0.93)

See accompanying notes to the consolidated financial statements.

First Mariner Bancorp and Subsidiary
Consolidated Statements of Changes in Stockholders (Deficit) Equity
(dollars in thousands except per share data)

For the Nine Months Ended September 30, 2011 (unaudited)

	Number of Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Deficit	Accumulated Other Comprehensive Loss	Total Stockholders (Deficit) Equity	Comprehensive Loss
Balance at December 31, 2010	18,050,117	$ 902	$ 79,667	$ (73,210)	$ (3,613)	$ 3,746	
Net loss				(26,269)		(26,269)	$ (26,269)
Common stock issued, net of costs	810,365	37	430			467	
Stock-based compensation expense			5			5	
Changes in unrealized losses on securities, net of taxes					479	479	479
Comprehensive loss							$ (25,790)
Balance at September 30, 2011	18,860,482	$ 939	$ 80,102	$ (99,479)	$ (3,134)	$ (21,572)	

For the Nine Months Ended September 30, 2010 (unaudited)

	Number of Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Deficit	Accumulated Other Comprehensive Loss	Total Stockholders Equity	Comprehensive Loss
Balance at December 31, 2009	6,452,631	$ 323	$ 56,771	$ (26,621)	$ (3,486)	$ 26,987	
Net loss				(12,705)		(12,705)	$ (12,705)
Common stock issued, net of costs	11,509,818	570	22,704			23,274	
Stock-based compensation expense			21			21	
Other			231	(231)			
Changes in unrealized losses on securities, net of taxes					1,194	1,194	1,194
Comprehensive loss							$ (11,511)
Balance at September 30, 2010	17,962,449	$ 893	$ 79,727	$ (39,557)	$ (2,292)	$ 38,771	

See accompanying notes to the consolidated financial statements.

First Mariner Bancorp and Subsidiary
Consolidated Statements of Cash Flows
(dollars in thousands)

	Nine Months Ended September 30,	
	2011	**2010**
	(unaudited)	
Cash flows from operating activities:		
Net loss	$ (26,269)	$ (12,705)
Adjustments to reconcile net loss to net cash from operating activities:		
Loss from discontinued operations		200
Stock-based compensation	5	21
Depreciation and amortization	2,472	2,947
Amortization of unearned loan fees and costs, net	283	144
Amortization (accretion) of premiums and discounts on mortgage-backed securities, net	29	(22)
Gain on financial instruments carried at fair value		(1,661)
Origination fees and gain on sale of mortgage loans	(6,750)	(11,481)
Gain on debt exchange		(958)
Net OTTI charges on securities available for sale	818	1,249
Gain on sale of securities available for sale	(781)	(54)
(Increase) decrease in accrued interest receivable	(4)	715
Provision for loan losses	11,580	16,290
Write-downs and losses on sale of real estate acquired through foreclosure	5,704	4,936
Gain on sale of premises and equipment	(4)	(192)
Increase in cash surrender value of bank-owned life insurance	(984)	(1,066)
Originations of mortgage loans held for sale (LHFS)	(691,831)	(915,771)
Proceeds from sales of mortgage LHFS	710,702	897,714
Net increase in accrued expenses and other liabilities	4,318	735
Net increase in prepaids and other assets	(11,716)	(6,561)
Net cash used in operating activities	(2,428)	(25,520)
Cash flows from investing activities:		
Loan principal repayments, net	49,542	32,441
Repurchase of loans previously sold	(435)	(1,208)
Sale of restricted stock investments	126	564
Purchases of premises and equipment	(336)	(1,070)
Proceeds from disposals of premises and equipment	9	775
Sales of trading securities		10,083
Maturities/calls/repayments of trading securities		735
Activity in securities available for sale:		
Maturities/calls/repayments	16,206	4,280
Sales	49,511	8,011
Purchases	(59,799)	(8,090)
Additional funds disbursed on real estate acquired through foreclosure	(1,754)	
Proceeds from sales of real estate acquired through foreclosure	8,570	12,974
Net cash provided investing activities	61,640	59,495
Cash flows from financing activities:		
Net decrease in deposits	(90,010)	(40,000)
Net decrease in other borrowed funds	(479)	(887)
Net (costs of) proceeds from stock issuance	(20)	10,453
Net cash used in financing activities	(90,509)	(30,434)

(Decrease) increase in cash and cash equivalents	(31,297)	3,541
Cash and cash equivalents at beginning of period	217,961	173,703
Cash and cash equivalents at end of period	$ 186,664	$ 177,244
Supplemental information:		
Interest paid on deposits and borrowed funds	$ 13,997	$ 20,420
Real estate acquired in satisfaction of loans	$ 16,073	$ 17,919
Transfers of loans held for sale to loan portfolio	$ 2,031	$

See accompanying notes to the consolidated financial statements

First Mariner Bancorp and Subsidiary
Notes to Consolidated Financial Statements
(Information as of and for the three and nine months ended September 30, 2011 and 2010 is unaudited)

(1) Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements for First Mariner Bancorp have been prepared in accordance with the instructions for Form 10-Q and, therefore, do not include all information and notes necessary for a full presentation of financial condition, results of operations, and cash flows in conformity with accounting principles generally accepted in the United States of America (U.S.) (GAAP). The consolidated financial statements should be read in conjunction with the audited financial statements included in First Mariner Bancorp s Annual Report on Form 10-K as of and for the year ended December 31, 2010. When used in these notes, the terms the Company, we, us, and our refer to First Mariner Bancorp and, unless the context requires otherwise, it s consolidated subsidiary.

The consolidated financial statements include the accounts of First Mariner and its wholly owned subsidiary, 1st Mariner Bank (the Bank). All significant intercompany accounts and transactions have been eliminated in consolidation. Events occurring after the date of the financial statements were considered in the preparation of the financial statements. Certain reclassifications have been made to amounts previously reported to conform to classifications made in 2011.

The consolidated financial statements as of September 30, 2011 and for the three and nine months ended September 30, 2011 and 2010 are unaudited but include all adjustments, consisting only of normal recurring adjustments, which we consider necessary for a fair presentation of financial position and results of operations for those periods. The results of operations for the three and nine months ended September 30, 2011 are not necessarily indicative of the results that will be achieved for the entire year or any future interim period.

The preparation of the financial statements in conformity with GAAP requires management to make estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses (the allowance), loan repurchases and related valuations, real estate acquired through foreclosure, impairment of securities available for sale (AFS), valuations of financial instruments, and deferred income taxes. In connection with these determinations, management evaluates historical trends and ratios and, where appropriate, obtains independent appraisals for significant properties and prepares fair value analyses. Actual results could differ significantly from those estimates.

(2) Going Concern Consideration

Due to the conditions and events discussed later in Note 6, substantial doubt exists as to our ability to continue as a going concern. Management is taking various steps designed to improve the Bank s capital position. The Bank has developed a written alternative capital plan designed to improve the Bank s capital ratios. Such plan is dependent upon a capital infusion to meet the capital requirements of the various regulatory agreements (see Note 6 for more information on the agreements). The Company continues to work with its advisors in an attempt to improve capital ratios. The Company has entered into a definitive agreement regarding the raising of additional capital (see Note 6); however, no assurances can be made that the Company will ultimately meet the provisions and deadlines of the agreement.

The consolidated financial statements presented above and the accompanying Notes have been prepared on a going concern basis, which contemplates the realization of assets and the discharge of liabilities in the normal course of business for the foreseeable future, and does not include any adjustment to reflect the possible future effects on the recoverability and classification of assets, or the amounts and classification of liabilities that may result from the outcome of any extraordinary regulatory action, which would affect our ability to continue as a going concern.

(3) Securities

The composition of our securities portfolio (all AFS) is as follows:

(dollars in thousands)	September 30, 2011 Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Mortgage-backed securities	$ 1,846	$ 117	$	$ 1,963
Trust preferred securities	13,443	85	3,310	10,218
U.S. government agency notes	8,511	9	7	8,513
U.S. Treasury securities	1,015			1,015
Equity securities - banks	215		64	151
Equity securities - mutual funds	750	36		786
	$ 25,780	$ 247	$ 3,381	$ 22,646

(dollars in thousands)	December 31, 2010 Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Mortgage-backed securities	$ 2,216	$ 109	$	$ 2,325
Trust preferred securities	14,269	101	3,906	10,464
U.S. government agency notes	12,075	12	16	12,071
U.S. Treasury securities	1,000	1		1,001
Corporate obligations	913	97		1,010
Equity securities - banks	215	11	29	197
Equity securities - mutual funds	750	8		758
	$ 31,438	$ 339	$ 3,951	$ 27,826

The amount of OTTI recorded as accumulated other comprehensive loss for the three months ended September 30, 2011 and 2010 was $382,000 and $514,000, respectively, on trust preferred securities. For the nine months ended September 30, 2011 and September 30, 2010, such amounts were $491,000 and $640,000, respectively, on trust preferred securities.

Contractual maturities of debt securities at September 30, 2011 are shown below. Actual maturities may differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

(dollars in thousands)	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 9,526	$ 9,528
Due after one year through five years	502	511
Due after five years through ten years	1,024	920
Due after ten years	11,917	8,787
Mortgage-backed securities	1,846	1,963
	$ 24,815	$ 21,709

The following table shows the level of our gross unrealized losses and the fair value of the associated securities by type and maturity for AFS securities at September 30, 2011 and December 31, 2010:

	September 30, 2011					
	Less than 12 months		12 months or more		Total	
(dollars in thousands)	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
Trust preferred securities	$ 920	$ 80	$ 4,524	$ 3,230	$ 5,444	$ 3,310
U.S. government agency notes	1,993	7			1,993	7
Equity securities - banks			151	64	151	64
	$ 2,913	$ 87	$ 4,675	$ 3,294	$ 7,588	$ 3,381

	December 31, 2010					
	Less than 12 months		12 months or more		Total	
(dollars in thousands)	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
Trust preferred securities	$ 340	$ 14	$ 5,722	$ 3,892	$ 6,062	$ 3,906
U.S. government agency notes	4,984	16			4,984	16
Equity securities - banks			105	29	105	29
	$ 5,324	$ 30	$ 5,827	$ 3,921	$ 11,151	$ 3,951

The trust preferred securities that we hold in our securities portfolio are issued by other banks, bank holding companies, and insurance companies. Certain of these securities have experienced declines in value since acquisition. These declines have occurred due to changes in the market which has limited the demand for these securities and reduced their liquidity. We recorded net OTTI charges of $681,000 and $818,000 for the three and nine months ended September 30, 2011, respectively, and $816,000 and $1.2 million during the three and nine months ended September 30, 2010, respectively.

The following shows the activity in OTTI related to credit losses for the three and nine months ended September 30:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in thousands)	2011	2010	2011	2010
Balance at beginning of period	$ 8,029	$ 7,076	$ 7,892	$ 6,643
Additional OTTI taken for credit losses	681	816	818	1,249
Balance at end of period	$ 8,710	$ 7,892	$ 8,710	$ 7,892

All of the remaining securities that are temporarily impaired are impaired due to declines in fair values resulting from changes in interest rates or increased credit/liquidity spreads since the time they were purchased. We have the intent to hold these debt securities to maturity, and, for debt and equity securities in a loss position, for the foreseeable future and do not intend, nor do we believe it is more likely than not, that we will be required to sell the securities before anticipated recovery. We expect these securities will be repaid in full, with no losses realized. As such, management considers the impairments to be temporary.

We purchased securities of $2.0 million and $59.8 million during the three and nine months ended September 30, 2011, respectively, and sold securities of $26.8 million and $49.5 million during the three and nine months ended September 30, 2011, respectively. We purchased securities of $5.6 million and $8.1 million during the three and nine months ended September 30, 2010, respectively. We sold AFS securities of $8.0 million and trading securities of $10.1 million during the nine months ended September 30, 2010. We did not sell any securities during the three months ended September 30, 2010.

At September 30, 2011, we held securities with an aggregate carrying value (fair value) of $17.0 million that we have pledged as collateral for certain hedging activities, borrowings, government deposits, and customer deposits.

(4) Loans Receivable and Allowance for Loan Losses

Loans receivable are summarized as follows:

(dollars in thousands)	**September 30, 2011**	**December 31, 2010**
Commercial	$ 62,751	$ 78,607
Commercial mortgage	335,389	349,691
Commercial construction	54,112	58,742
Consumer construction	21,814	31,107
Residential mortgage	124,511	144,194
Consumer	137,124	148,166
Total loans	735,701	810,507
Unearned loan fees, net	971	1,180
	$ 736,672	$ 811,687

Included in consumer loan totals in the above table are overdrawn commercial and retail checking accounts totaling $143,000 as of September 30, 2011 and $186,000 as of December 31, 2010.

Transferred Loans

In accordance with the Financial Accounting Standards Board (FASB) guidance on mortgage-banking activities, any loan which is originally originated for sale into the secondary market and which we subsequently elect to transfer into the Company s loan portfolio is valued at fair value at the time of the transfer with any decline in value recorded as a charge against earnings.

Information on the activity in transferred loans and related accretable yield is as follows for the three months ended September 30:

	Loan Balance		**Accretable Yield**		**Total**	
(dollars in thousands)	**2011**	**2010**	**2011**	**2010**	**2011**	**2010**
Beginning balance	$ 26,783	$ 22,198	$ 110	$ 267	$ 26,673	$ 21,931
Loans transferred	1,053				1,053	
Charge-offs			(10)		10	
Payments/amortization	(10)	(382)	(10)	(48)		(334)
Ending balance	$ 27,826	$ 21,816	$ 90	$ 219	$ 27,736	$ 21,597

Information on the activity in transferred loans and related accretable yield is as follows for the nine months ended September 30:

	Loan Balance		**Accretable Yield**		**Total**	
(dollars in thousands)	**2011**	**2010**	**2011**	**2010**	**2011**	**2010**
Beginning balance	$ 26,219	$ 24,575	$ 178	$ 423	$ 26,041	$ 24,152
Loans transferred	2,031				2,031	
Loans moved to real estate acquired through foreclosure	(83)	(281)		(8)	(83)	(273)

Charge-offs	(302)	(962)	(16)	(33)	(286)	(929)
Payments/amortization	(39)	(1,516)	(72)	(163)	33	(1,353)
Ending balance	$ 27,826	$ 21,816	$ 90	$ 219	$ 27,736	$ 21,597

As of September 30, 2011 and December 31, 2010, we maintained servicing on mortgage loans sold to the Federal National Mortgage Association (FNMA) of approximately $2.6 million and $323.3 million, respectively. We sold the majority of our servicing rights to Next Generation Financial Services (NGFS) during the second quarter of 2011 in conjunction with the closing of that sales transaction in the third quarter of 2011.

At September 30, 2011, we have pledged loans with a carrying value of $116.7 million as collateral for Federal Home Loan Bank (FHLB) advances.

Credit Quality

Management has an established methodology to determine the adequacy of the allowance for loan losses that assesses the risks and losses inherent in the loan portfolio. For purposes of determining the allowance for loan losses, we have segmented our loan portfolio by product type. Our portfolio loan segments are commercial, commercial mortgage, commercial construction, consumer construction, residential mortgage, and consumer. We have looked at all segments to determine if subcategorization into classes is warranted based upon our credit review methodology. We have divided consumer loans into two classes, (1) home equity and second mortgage loans and (2) other consumer loans.

To establish the allowance for loan losses, loans are pooled by portfolio class and an historical loss percentage is applied to each class. The historical loss percentage is based upon a rolling 24 month history. This rolling history is utilized so that we have the most current and relevant charge-off trend data. These charge-offs are segregated by loan segment and compared to their respective loan segment average balances for the same period in order to calculate the charge-off percentage. That percentage is then applied to the current period loan balances to determine the required reserve. That calculation determines the required allowance for loan loss level. We then apply additional loss multipliers to the different classes of loans to reflect various environmental factors. This amount is considered our unallocated reserve. For individually evaluated loans (impaired loans), we do additional analyses to determine the impairment. In general, this impairment is included as part of the allowance for loan losses (specific reserve) for modified loans and is charged-off for all other impaired loans. These loss estimates are performed under multiple economic scenarios to establish a range of potential outcomes for each criterion. Management applies judgment to develop its own view of loss probability within that range, using external and internal parameters with the objective of establishing an allowance for loss inherent within these portfolios as of the reporting date.

The following table presents by portfolio segment, the changes in the allowance for loan losses, and the recorded investment in loans:

As of and for the three and nine months ended September 30, 2011:

	Three months ended September 30, 2011							
(dollars in thousands)	**Commercial**	**Commercial Mortgage**	**Commercial Construction**	**Consumer Construction**	**Residential Mortgage**	**Consumer**	**Unallocated**	**Total**
Beginning Balance	$ 233	$ 2,586	$ 1,782	$ 360	$ 2,895	$ 3,089	$ 3,170	$ 14,115
Charge-offs	(2,368)	(1,325)	(131)		(669)	(590)		(5,083)
Recoveries			24		23	33		80
Net charge-offs	(2,368)	(1,325)	(107)		(646)	(557)		(5,003)
Provision for (reversal of) loan losses	4,824	605	(7)	(125)	975	92	(1,364)	5,000
Ending Balance	$ 2,689	$ 1,866	$ 1,668	$ 235	$ 3,224	$ 2,624	$ 1,806	$ 14,112

	Nine months ended September 30, 2011							
(dollars in thousands)	**Commercial**	**Commercial Mortgage**	**Commercial Construction**	**Consumer Construction**	**Residential Mortgage**	**Consumer**	**Unallocated**	**Total**
Beginning Balance	$ 291	$ 2,542	$ 2,053	$ 817	$ 3,032	$ 2,417	$ 2,963	$ 14,115
Charge-offs	(5,240)	(1,834)	(728)	(24)	(2,209)	(2,021)		(12,056)
Recoveries		168	24		37	244		473
Net charge-offs	(5,240)	(1,666)	(704)	(24)	(2,172)	(1,777)		(11,583)
Provision for (reversal of) loan losses	7,638	990	319	(558)	2,364	1,984	(1,157)	11,580
Ending Balance	$ 2,689	$ 1,866	$ 1,668	$ 235	$ 3,224	$ 2,624	$ 1,806	$ 14,112
Ending balance - individually evaluated for impairment	$ 4	$ 89	$	$ 1	$ 352	$ 4	$	$ 450
Ending balance - collectively evaluated for impairment	$ 2,685	$ 1,777	$ 1,668	$ 234	$ 2,872	$ 2,620	$ 1,806	$ 13,662
Ending loan balance - individually evaluated for impairment	$ 4,400	$ 24,302	$ 11,701	$ 757	$ 19,742	$ 1,595		$ 62,497
Ending loan balance - collectively evaluated for impairment	58,375	310,804	42,375	20,836	104,836	136,949		674,175
	$ 62,775	$ 335,106	$ 54,076	$ 21,593	$ 124,578	$ 138,544		$ 736,672

As of and for the three and nine months ended September 30, 2010:

	Three months ended September 30, 2010							
(dollars in thousands)	**Commercial**	**Commercial Mortgage**	**Commercial Construction**	**Consumer Construction**	**Residential Mortgage**	**Consumer**	**Unallocated**	**Total**
Beginning Balance	$ 877	3,358	1,458	217	1,861	1,145	3,102	$ 12,018
Charge-offs	(1,904)		(3,103)	(12)	(431)	(1,568)		(7,018)
Recoveries			7		8	411		426
Net charge-offs	(1,904)		(3,096)	(12)	(423)	(1,157)		(6,592)
Provision for (reversal of) loan losses	1,515	(1,010)	3,691	747	1,869	2,361	577	9,750
Ending Balance	$ 488	$ 2,348	$ 2,053	$ 952	$ 3,307	$ 2,349	$ 3,679	$ 15,176

	Nine months ended September 30, 2010							
(dollars in thousands)	**Commercial**	**Commercial Mortgage**	**Commercial Construction**	**Consumer Construction**	**Residential Mortgage**	**Consumer**	**Unallocated**	**Total**
Beginning Balance	$ 817	3,336	1,647	293	2,062	882	2,602	$ 11,639
Charge-offs	(1,904)	(454)	(3,967)	(297)	(3,562)	(3,160)		(13,344)
Recoveries			7		97	487		591
Net charge-offs	(1,904)	(454)	(3,960)	(297)	(3,465)	(2,673)		(12,753)
Provision for (reversal of) loan losses	1,575	(534)	4,366	956	4,710	4,140	1,077	16,290
Ending Balance	$ 488	$ 2,348	$ 2,053	$ 952	$ 3,307	$ 2,349	$ 3,679	$ 15,176
Ending balance - individually evaluated for impairment	$	$ 70	$ 214	$	$ 291	$	$	$ 575
Ending balance - collectively evaluated for impairment	$ 488	$ 2,278	$ 1,839	$ 952	$ 3,016	$ 2,349	$ 3,679	$ 14,601
Ending loan balance - individually evaluated for impairment	$ 1,150	$ 24,609	$ 9,978	$ 1,600	$ 24,741	$ 2,618		$ 64,696
Ending loan balance -collectively evaluated for impairment	73,090	348,216	46,978	32,695	117,909	149,318		768,206
	$ 74,240	$ 372,825	$ 56,956	$ 34,295	$ 142,650	$ 151,936		$ 832,902

We use creditworthiness categories to grade commercial loans. Our internal grading system is based on experiences with similarly graded loans. Category ratings are reviewed each quarter. Our internal risk ratings are as follows:

Superior Credit Quality (RR1) This category includes credits that are secured by up to 95% advance against cash balances, municipal or corporate bonds carrying an A rating or better (subject to maturity), U.S. Government securities (subject to maturity), and fully marketable securities of companies with an A or better debt rating. In addition, the borrower must have a reasonable financial condition evidenced by complete financial statements.

High Credit Quality (RR2) This category includes credits that are secured by up to 70% advance against municipal or corporate bonds carrying an A rating or better, U.S. Government securities, and marketable securities of companies with an A or better debt rating. For individual credits, the credit must be secured by any of the aforementioned items or first deed of trust on residential owner-occupied property with a loan-to-value (LTV) ratio of 80% or less and adequate cash flow to service the debt. Permanent real estate loans on fully leased properties with A-rated tenants and a 70% or less LTV ratio with income coverage of 1.25 times or higher may qualify for this rating, with confirmation of tenants financial condition. No commercial construction loans may carry this rating at inception. At September 30, 2011 and December 31, 2010, none of our loans carried this risk rating.

Above Average Credit Quality (RR3) This category includes business loans to publicly traded companies with a B rating or better, commercial construction loans with a contingent-free take-out or substantial pre-leasing (75% or more of leasable space) with a LTV ratio of 70% or less, residential construction loans with pre-sold units and a LTV ratio of 70% or less as long as sales are on a noncontingent basis and the overall project is progressing on schedule as originally determined, loans to individuals with liquid assets and strong net worth and the additional ability to service the debt from sources unrelated to the purpose of the credit extension, and monitored credits to borrowers of sound financial condition with approved advance rates providing adequate margin so that collateral can be easily liquidated within 90 days or less.

Average/Satisfactory Credit Quality (RR4) In general, this category includes small-to-medium sized companies with satisfactory financial condition, cash flow, profitability, and balance sheet and income statement ratios, term loans and revolving credits with annual clean-up requirements, the majority of retail commercial credits, loans to partnerships or small businesses, most wholesale sales finance lines, wholesale distributors whose capital position and profitability are at Robert Morris and Associates averages, and loans to individuals with acceptable financial condition and sufficient net cash flow to service the debt as long as the source of repayment is identifiable and sufficient to liquidate the debt within an acceptable period of time and a secondary source of repayment is evident.

Acceptable With Care (RR5) This category includes secured loans to small or medium sized companies which have suffered a financial setback where a convincing plan for correction demonstrates the deficiency is temporary in nature, loans with debt service coverage ratios below or LTV ratios above policy guidelines, most construction and development loans, permanent loans underwritten based on pro forma rents as opposed to historical or actual rents, real estate loans where the project is moderately off the original projections as to cost estimates or absorption, and loans where the interest reserve is no longer adequate, but the customer or guarantor has a proven ability to carry the interest expense out of pocket for an extended time period without undue financial strain. These credits require additional attention by the account officer and/or loan administration.

Watch Credits (RR6) This category includes loans to borrowers who have experienced a temporary setback or deterioration in financial condition that should correct itself during the next twelve months, companies whose financial condition has been marginally acceptable for a period of time and prospects for significant improvement are limited, loans to individuals with marginal financial condition, and most credits for start-up operations. Also included in this category are real estate loans where the project is moderately off original projections, interest reserve may be depleted, with the borrower or guarantor having a questionable or unproved ability to pay interest out of pocket. Such loans may have modest cost overruns that will cause a shortage in the budget, raising question as to how the project will be completed. These loans may have a good collateral position, additional collateral, or strong guarantors to mitigate the risk. These credits are considered marginally acceptable, and greater than usual attention is warranted by the account officer and/or loan operations.

Special Mention (RR7) special mention credits are characterized as adequately covered by collateral (if any) and/or the paying capacity of the borrower, but are subject to one or more deteriorating trends. These credits constitute an undue and unwarranted credit risk, but not to the point of justifying a classification of substandard. These credits have potential weaknesses which, if not examined and corrected, may weaken the asset or inadequately protect the Bank s credit position at some future date. This category should not be used to list assets that bear risks usually associated with the particular type of financing. Assets with this rating may have the potential for significant weakness. Loans where weaknesses are evident and significant must be considered for more serious criticism. Examples of credits carried in special mention may include the following:

Loans which are fully covered by collateral and cash flow, but where margins are inadequate;

Loans to borrowers with a strong capital base, who are experiencing modest losses;

Loans to borrowers with very strong cash flows, but experiencing modest losses;

Credits that are subject to manageable, but excessive, leverage;

Credits with material collateral documentation exceptions, but which appear to be strong credits. If the documentation exception results in an unperfected/under secured collateral position, the credit may be risk rated as if it were under secured until such time as the exception is corrected;

Credits to customers who have not provided the Bank with current or satisfactory financial data (unless the credit is secured by liquid marketable collateral or guaranteed by financially sound parties);

Credits that the account officer may be unable to supervise properly because of a lack of expertise or lack of control over the collateral and/or its condition;

Loans with deficient documentation or other deviations from prudent lending practices; and

Loans with strong guarantors and/or secondary sources of cash flow are the support for repayment.

Substandard (RR8) Substandard loans are inadequately protected by the current sound worth and paying capacity of the obligor or the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses, which jeopardize the orderly liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. The borrower s financial condition indicates an inability to repay, even if restructured. Prospects for improvement in the borrower s financial condition are poor. Primary repayment source appears to be shifting from cash flow to liquidation of collateral. Examples of substandard credits may include the following:

Credits adequately covered by collateral value, where repayment is dependent upon the sale of nonliquid collateral, nontrading assets, or from guarantors;

Loans secured by collateral greater than the amount of the credit, but where cash flow is inadequate to amortize the debt over a reasonable period of time;

Credits with negative financial trends coupled with material collateral documentation deficiencies or where there is a high potential for loss of principal;

Unsecured loans to borrowers whose financial condition does not warrant unsecured advances;

Credits where the borrower is in bankruptcy or the work out effort is proceeding toward legal remedies including foreclosure; and

All nonaccrual loans.

Doubtful (RR9) Doubtful classifications have all the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses make collection or liquidation in full on the basis of currently known facts, conditions, and values highly questionable and improbable. A doubtful classification may be appropriate in cases where significant risk exposures are perceived, but loss cannot be determined because of specific, reasonable, and pending factors which may strengthen and work to the advantage of the credit in the near term. Account officers attempt to identify any principal loss in the credit, where possible, thereby limiting the excessive use of the doubtful classification. The classification is a deferral of the estimated loss until its more exact status may be determined. Pending factors include proposed mergers, acquisition or liquidation procedures, new capital injection, perfecting liens on additional collateral, and refinancing plans. At September 30, 2011 and December 31, 2010, none of our loans carried this risk rating.

Loss (RR10) Losses must be taken as soon as they are realized. In some instances and on a temporary basis, a portion of a loan may receive this rating (split rating) when the actual loss cannot be currently identified. In these instances, additional facts or information is necessary to determine the final amount to be charged against the loan loss reserve. When applied for these purposes, this risk rating may be used for a period not to exceed nine months. Subsequent to the identification of this split rating, the remaining balance will be risk rated substandard. This category includes advances in excess of calculated current fair value which are considered uncollectible and do not warrant continuance as bankable assets. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may occur in the future. Credits to distressed borrowers lacking an identifiable and realistic source of repayment are generally charged-off. Loans where repayment is dependent upon events that are not predictable in terms of result or timing (such as protracted litigation) are generally charged-off. At September 30, 2011 and December 31, 2010, none of our loans carried this risk rating.

The following table shows the credit quality breakdown of our commercial loan portfolio by class as of September 30, 2011 and December 31, 2010:

	Commercial		Commercial Mortgage		Commercial Construction		Consumer Construction		Total	
	(dollars in thousands)									
	2011	2010	2011	2010	2011	2010	2011	2010	2011	2010
RR8	$ 6,268	$ 1,939	$ 29,947	$ 33,492	$ 12,245	$ 14,677	$	$ 1,150	$ 48,460	$ 51,258
RR7	9,174	7,241	16,202	10,921	18,275	6,686	136	136	43,787	24,984
RR6	8,016	9,174	37,135	23,097	8,734	15,081	1,025	98	54,910	47,450
RR5	11,815	22,417	116,442	126,297	10,075	13,811			138,332	162,525
RR4	26,483	36,257	133,792	155,336	4,747	8,509	20,432	29,408	185,454	229,510
RR3	1,000	1,000	1,588	268					2,588	1,268
RR1	19	773							19	773
	$ 62,775	$ 78,801	$ 335,106	$ 349,411	$ 54,076	$ 58,764	$ 21,593	$ 30,792	$ 473,550	$ 517,768

We do not individually grade residential mortgage or consumer loans. Such loans are classified as performing or nonperforming. Loan performance is reviewed each quarter. The following table shows performing and nonperforming (nonaccrual) residential mortgage and consumer loans by class as of September 30, 2011 and December 31, 2010

	Residential Mortgage		Home Equity & 2nd Mortgage		Other Consumer		Total	
(dollars in thousands)	2011	2010	2011	2010	2011	2010	2011	2010
Nonaccruing loans	$ 9,678	$ 11,877	$ 1,384	$ 946	$	$	$ 11,062	$ 12,823
Performing loans	114,900	132,332	112,537	119,874	24,623	28,890	252,060	281,096
	$ 124,578	$ 144,209	$ 113,921	$ 120,820	$ 24,623	$ 28,890	$ 263,122	$ 293,919

The following tables show the aging of our loans receivable by class. Also included are loans that are 90 days or more past due as to interest and principal and still accruing because they are well-secured and in the process of collection.

As of September 30, 2011:

(dollars in thousands)	31-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	90 Days or More and Accruing
Commercial	$ 97	$	$ 4,356	$ 4,453	$ 58,322	$ 62,775	$ 118
Commercial mortgage	14,022	2,243	21,406	37,671	297,435	335,106	1,281
Commercial construction	2,478	361	6,549	9,388	44,688	54,076	
Consumer construction	359	916	488	1,763	19,830	21,593	
Residential mortgage		6,289	11,293	17,582	106,996	124,578	1,615
Home equity and 2nd mortgage	2,342	777	1,693	4,812	109,109	113,921	309
Other consumer	394	155		549	24,074	24,623	
	$ 19,692	$ 10,741	$ 45,785	$ 76,218	$ 660,454	$ 736,672	$ 3,323

As of December 31, 2010:

(dollars in thousands)	**31-59 Days Past Due**	**60-89 Days Past Due**	**90 Days or More Past Due**	**Total Past Due**	**Current**	**Total Loans**	**90 Days or More and Accruing**
Commercial	$ 1,626	$ 169	$ 1,501	$ 3,296	$ 75,505	$ 78,801	$
Commercial mortgage	4,957	2,706	28,943	36,606	312,805	349,411	1,952
Commercial construction			8,237	8,237	50,527	58,764	250
Consumer construction	2,168	379	1,257	3,804	26,988	30,792	
Residential mortgage	10,919	7,789	12,653	31,361	112,848	144,209	776
Home equity and 2nd mortgage	3,221	390	946	4,557	116,263	120,820	
Other consumer	125	592		717	28,173	28,890	
	$ 23,016	$ 12,025	$ 53,537	$ 88,578	$ 723,109	$ 811,687	$ 2,978

Impaired loans include nonaccrual loans and troubled debt restructures (TDR or TDRs). The following tables show the breakout of impaired loans by class:

	September 30, 2011					
(dollars in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Charge-Offs
With no related allowance:						
Commercial	$ 4,239	$ 4,239	$	$ 2,197	$ 7	$ 5,240
Commercial mortgage	$ 19,553	$ 19,553	$	$ 20,948	$ 58	$ 1,706
Commercial construction	$ 11,701	$ 11,701	$	$ 12,376	$ 69	$ 728
Consumer construction	$ 351	$ 351	$	$ 874	$ 1	$ 24
Residential mortgage	$ 7,658	$ 7,658	$	$ 10,402	$ 85	$ 1,506
Home equity & 2nd mortgage	$ 1,520	$ 1,520	$	$ 915	$ 5	$ 2,021
Other consumer	$	$	$	$ 168	$	$
With a related allowance:						
Commercial	157	161	4	39	2	
Commercial mortgage	4,660	4,749	89	3,876	74	128
Commercial construction				333		
Consumer construction	405	406	1	140	16	
Residential mortgage	11,732	12,084	352	12,139	388	703
Home equity & 2nd mortgage	71	75	4	18	3	
Other consumer						
Totals:						
Commercial	$ 4,396	$ 4,400	$ 4	$ 2,236	$ 9	$ 5,240
Commercial mortgage	$ 24,213	$ 24,302	$ 89	$ 24,824	$ 132	$ 1,834
Commercial construction	$ 11,701	$ 11,701	$	$ 12,709	$ 69	$ 728
Consumer construction	$ 756	$ 757	$ 1	$ 1,014	$ 17	$ 24
Residential mortgage	$ 19,390	$ 19,742	$ 352	$ 22,541	$ 473	$ 2,209
Home equity & 2nd mortgage	$ 1,591	$ 1,595	$ 4	$ 933	$ 8	$ 2,021
Consumer	$	$	$	$ 168	$	$

	December 31, 2010					
(dollars in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Charge-Offs
With no related allowance:						
Commercial	$ 1,501	$ 1,501	$	$ 2,069	$ 40	$ 1,979
Commercial mortgage	$ 26,534	$ 26,534	$	$ 17,437	$ 811	$ 1,232
Commercial construction	$ 12,814	$ 12,814	$	$ 10,647	$ 310	$ 2,320
Consumer construction	$ 1,257	$ 1,257	$	$ 2,200	$ 35	$ 804
Residential mortgage	$ 11,877	$ 11,877	$	$ 11,973	$ 381	$ 3,757
Home equity & 2nd mortgage	$ 1,067	$ 1,067	$	$ 1,385	$ 15	$ 3,787
Other consumer	$	$	$	$ 13	$	$
With a related allowance:						
Commercial						
Commercial mortgage	3,226	3,314	88	2,864	73	163
Commercial construction	445	459	14	2,567	18	1,932
Consumer construction						
Residential mortgage	12,661	13,147	486	5,339	695	
Home equity & 2nd mortgage				2,065		
Other consumer				1		
Total:						
Commercial	$ 1,501	$ 1,501	$	$ 2,069	$ 40	$ 1,979
Commercial mortgage	$ 29,760	$ 29,848	$ 88	$ 20,301	$ 884	$ 1,395

Commercial construction	$	13,259	$	13,273	$	14	$	13,214	$	328	$	4,252
Consumer construction	$	1,257	$	1,257	$		$	2,200	$	35	$	804
Residential mortgage	$	24,538	$	25,024	$	486	$	17,312	$	1,076	$	3,757
Home equity & 2nd mortgage	$	1,067	$	1,067	$		$	3,450	$	15	$	3,787
Consumer	$		$		$		$	14	$		$	

The following table shows loans in nonaccrual status by class:

(dollars in thousands)	September 30, 2011	December 31, 2010	September 30, 2010
Commercial	$ 4,238	$ 1,501	$ 1,150
Commercial mortgage	20,125	26,991	22,610
Commercial construction	6,549	7,987	7,386
Consumer construction	488	1,257	1,600
Residential mortgage	9,678	11,877	13,237
Home equity and 2nd mortgage	1,384	946	1,146
Other consumer			1,472
	$ 42,462	$ 50,559	$ 48,601

The interest which would have been recorded on nonaccrual loans if those loans had been performing in accordance with their contractual terms for the nine months ended September 30, 2011 and 2010 was approximately $1.4 million and $2.2 million, respectively, and the actual interest income recorded on such loans for the nine months ended September 30, 2011 and 2010 was approximately $235,000 and $812,000, respectively.

The following table shows the breakdown of loans we modified during the three and nine months ended September 30:

	Three Months Ended September 30,					
	2011			2010		
(dollars in thousands)	Number of Modifications	Recorded Investment Prior to Modification	Recorded Investment After Modification	Number of Modifications	Recorded Investment Prior to Modification	Recorded Investment After Modification
Commercial	1	$ 297	$ 22		$	$
Residential mortgage				6	2,261	2,275
Home equity and 2nd mortgage				4	207	207
	1	$ 297	$ 22	10	$ 2,468	$ 2,482

	Nine Months Ended September 30,					
	2011			2010		
(dollars in thousands)	Number of Modifications	Recorded Investment Prior to Modification	Recorded Investment After Modification	Number of Modifications	Recorded Investment Prior to Modification	Recorded Investment After Modification
Commercial	2	$ 460	$ 185		$	$
Commercial mortgage	2	2,197	2,197	2	2,316	2,370
Commercial construction				6	5,177	5,508
Residential mortgage	1	566	579	16	9,027	9,033
Home equity and 2nd mortgage				10	1,148	1,148

5	$ 3,223	$ 2,961	34	$ 17,668	$ 18,059

The majority of our TDRs are the result of renewals where the only concession is that the interest rate is not considered to be a market rate. As such, the best illustration of the financial impact of the TDRs is the effect on the allowance for loan losses.

During the nine months ended September 30, 2011, a total of $65,000 ($4,000 for commercial, $40,000 for commercial mortgage, and $21,000 for residential mortgage) was added to the allowance for loan losses for TDRs. During the three months ended September 30, 2010, a total of $96,000 for residential mortgage loans was added to the allowance for loan losses for TDRs. During the nine months ended September 30, 2010, $226,000 ($15,000 for commercial mortgage loans and $211,000 for residential mortgage loans) was added to the allowance for loan losses for TDRs. There were no additional effects on the allowance for TDRs during the three months ended September 30, 2011. Additionally, during the three and nine months ended September 30, 2011, we charged-off approximately $275,000 of a TDR commercial loan.

There were no defaults in 2011 of modifications made during 2010. Additionally, there were no defaults during the three months ended September 30, 2010 of modifications made during 2009. The following table shows defaults during the nine months ended September 30, 2010 of modifications made during 2009:

(dollars in thousands)	**Number of Modifications**	**Recorded Investment**
Commercial	2	$ 2,850
Commercial mortgage		
Commercial construction		
Consumer construction		
Residential mortgage	3	857
Home equity and 2nd mortgage		
Other consumer		
	5	$ 3,707

Total TDRs as of September 30, 2011 and December 31, 2010 amounted to $24.7 million and $24.2 million, respectively, of which $4.6 million and $2.8 million, respectively, were also in nonaccrual status.

(5) Junior Subordinated Deferrable Interest Debentures

The following table shows the subordinated debt issued by First Mariner Bancorp and the related trust preferred securities (Trust Preferred Securities) issued at both September 30, 2011 and December 31, 2010:

Trust	Subordinated Debt Issued to Trust	Trust Preferred Securities Issued by Trust	Date of Original Issue	Optional Redemption Date	Stated Maturity
MCT II	$ 6,186	$ 6,000	December 10, 2002	December 15, 2007	December 10, 2032
MCT III	14,949	14,500	June 18, 2003	July 7, 2008	July 7, 2033
MCT IV	5,158	5,000	August 18, 2003	August 18, 2008	August 18, 2033
MCT V	10,310	10,000	September 25, 2003	October 8, 2008	October 8, 2033
MCT VI	10,310	10,000	October 21, 2004	January 7, 2010	January 7, 2035
MCT VII	5,155	5,000	August 18, 2005	September 15, 2010	September 15, 2035
	$ 52,068	$ 50,500			

First Mariner issued junior subordinated deferrable interest debentures to six statutory trust subsidiaries, Mariner Capital Trust (MCT) II, MCT III, MCT IV, MCT V, MCT VI, and MCT VII (collectively, the Trusts). The Trusts are Delaware business trusts for which all the common securities are owned by First Mariner and which were formed for the purpose of issuing trust preferred securities. In accordance with FASB guidance, we have deconsolidated the Trusts, and their financial position and results of operations are not included in our consolidated financial position and results of operations. The payment and redemption terms of the debentures and related Trust Preferred Securities are substantially identical.

The Trust Preferred Securities are mandatorily redeemable, in whole or in part, upon repayment of their underlying subordinated debt at their respective maturities or their earlier redemption. The junior subordinated deferrable interest debentures are redeemable prior to maturity at our option on or after their optional redemption dates.

As of September 30, 2011, all of the Trust Preferred Securities are Floating Rate Trust Preferred Securities, which accrue interest equal to the 3-month LIBOR rate plus varying basis points as follows: MCT II 335 basis points; MCT III 325 basis points; MCT IV 305 basis points; MCT V 310 basis points; MCT VI 205 basis points; and MCT VII 195 basis points.

The interest expense (including amortization of the cost of issuance) on junior subordinated deferrable interest debentures was $406,000 and $1.2 million, respectively, for the three and nine months ended September 30, 2011, and $436,000 and $1.5 million, respectively, for the three and nine months ended September 30, 2010. In 2009, we elected to defer interest payments on the debentures. This deferral is permitted by the terms of the debentures and does not constitute an event of default thereunder. Interest on the debentures and dividends on the related Trust Preferred Securities continue to accrue and will have to be paid in full prior to the expiration of the deferral period. The total deferral period may not exceed 20 consecutive quarters and expires with the last quarter of 2013.

The junior subordinated deferrable interest debentures are the sole assets of the Trusts. First Mariner has fully and unconditionally guaranteed all of the obligations of the Trusts.

Under applicable regulatory guidelines, a portion of the Trust Preferred Securities may qualify as Tier I capital, and the remaining portion may qualify as Tier II capital, with certain limitations. At September 30, 2011, none of our outstanding Trust Preferred Securities qualify as either Tier I or Tier II capital due to limitations.

During 2010, we executed Exchange agreements (the Exchanges) with our Chairman and Chief Executive Officer (CEO), Edwin F. Hale, Sr. and with an unaffiliated third party. The agreements exchanged trust preferred securities for shares of common stock and warrants of the Company. Upon completion of the Exchanges, the Company canceled the trust preferred securities and the related accrued interest on the

securities in exchanges for the common stock and warrants, eliminating the long term debt. The transaction with the unaffiliated third party resulted in a gain of $571,000, net of taxes of $387,000.

(6) Regulatory Matters, Capital Adequacy, and Liquidity

Regulatory matters and capital adequacy

Various regulatory capital requirements administered by the federal banking agencies apply to First Mariner and the Bank. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on our financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank s capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios of Total and Tier 1 capital to risk-weighted assets, and of Tier 1 capital to average quarterly assets. As of September 30, 2011 and December 31, 2010, the Bank was under capitalized under the regulatory framework for prompt corrective action.

Our regulatory capital amounts and ratios as of September 30, 2011 and December 31, 2010 were as follows:

			Minimum Requirements for Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provision	
(dollars in thousands)	**Actual Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
As of September 30, 2011						
Total capital (to risk-weighted assets):						
Consolidated	$ (18,455)	(2.1)%	$ 69,074	8.0%	$ 86,342	10.0%
Bank	50,091	5.8%	69,048	8.0%	86,310	10.0%
Tier 1 capital (to risk-weighted assets):						
Consolidated	(18,455)	(2.1)%	34,537	4.0%	51,805	6.0%
Bank	39,237	4.5%	34,524	4.0%	51,786	6.0%
Tier 1 capital (to average quarterly assets):						
Consolidated	(18,455)	(1.6)%	45,949	4.0%	57,436	5.0%
Bank	39,237	3.4%	45,932	4.0%	57,415	5.0%
As of December 31, 2010						
Total capital (to risk-weighted assets):						
Consolidated	$ 19,344	2.1%	$ 74,825	8.0%	$ 93,531	10.0%
Bank	75,277	8.0%	74,832	8.0%	93,540	10.0%
Tier 1 capital (to risk-weighted assets):						
Consolidated	9,672	1.0%	37,412	4.0%	56,119	6.0%
Bank	63,544	6.8%	37,416	4.0%	56,124	6.0%
Tier 1 capital (to average quarterly assets):						
Consolidated	9,672	0.7%	53,780	4.0%	67,226	5.0%
Bank	63,544	4.7%	53,926	4.0%	67,407	5.0%

The Federal Deposit Insurance Corporation (FDIC), through the Deposit Insurance Fund, insures deposits of accountholders up to $250,000, with the exception of noninterest-bearing transaction accounts, which are insured without limit through December 31, 2012. The Bank pays an annual premium to provide for this insurance.

The Bank is a member of the FHLB System and is required to maintain an investment in the stock of the FHLB based on specific percentages of outstanding mortgages, total assets, or FHLB advances. Purchases and sales of stock are made directly with the Bank at par value.

On September 18, 2009, the Bank entered into an Agreement with the FDIC and the Commissioner of Financial Regulation for the state of Maryland (the Commissioner), pursuant to which it consented to the entry of an Order to Cease and Desist (the September Order), which directs the Bank to (i) increase its capitalization, (ii) improve earnings, (iii) reduce nonperforming loans, (iv) strengthen management policies and practices, and (v) reduce reliance on noncore funding. The September Order required the Bank to adopt a plan to achieve and maintain a Tier I leverage capital ratio of at least 7.5% and a total risk-based capital ratio of at least 11% by June 30, 2010. We did not meet the requirements at June 30, 2010, December 31, 2010, or September 30, 2011. The failure to achieve these capital requirements could result in further action by our regulators.

As part of the September Order, within 30 days after the end of each calendar year, the Bank must submit an annual budget and profit plan and a plan that takes into account the Bank s pricing structure, the Bank s cost of funds and how this can be reduced, and the level of provision expense for adversely classified loans. To address reliance on noncore funding, the Bank was required to submit a liquidity plan intended to reduce the Bank s reliance on noncore funding, wholesale funding sources, and high-cost rate-sensitive deposits. While the September Order is in

effect, the Bank may not pay dividends or management fees without the FDIC s prior consent, may not accept, renew, or roll over any brokered deposits, and is restricted in the yields that it may pay on deposits.

First Mariner Bancorp is also a party to agreements with the Federal Reserve Bank (FRB) (the FRB Agreements), which, together, require it to: (i) develop and implement a strategic business plan that includes (a) actions that will be taken to improve our operating performance and reduce the level of parent company leverage, (b) a comprehensive budget and an expanded budget review process, (c) a description of the operating assumptions that form the basis for major projected income and expense components and provisions needed to maintain an adequate loan loss reserve, and (d) a capital plan incorporating all capital needs, risks, and regulatory guidelines; and (ii) submit plans to improve enterprise-wide risk management and effectiveness of internal audit programs. First Mariner Bancorp has also agreed to provide the FRB with advance notice of any significant capital transactions. The FRB Agreements also prohibit First Mariner and the Bank from taking any of the following actions without the FRB s prior written approval: (i) declaring or paying any dividends; (ii) taking dividends from the Bank; (iii) making any distributions of interest, principal, or other sums on First Mariner s subordinated debentures or trust preferred securities; (iv) incurring, increasing, or guaranteeing any debt; or (v) repurchasing or redeeming any shares of its stock. To satisfy the FRB s minimum capital requirements, First Mariner s consolidated Tier I capital to average quarterly assets, Tier I capital to risk-weighted assets, and total capital to risk-weighted assets ratios at each quarter end must be at least 4.0%, 4.0%, and 8.0%, respectively. At September 30, 2011, those capital ratios were (1.6)%, (2.1)%, and (2.1)%, respectively, which were not in compliance with the minimum requirements. The failure to achieve these capital requirements could result in further action by our regulators.

The foregoing will subject us to increased regulatory scrutiny and may have an adverse impact on our business operations. Failure to comply with the provisions of these regulatory requirements may result in more restrictive actions from our regulators, including more severe and restrictive enforcement actions.

Management believes the ultimate successful satisfaction of the September Order s requirements and the requirements of the FRB Agreements will strengthen the financial condition of the Bank and Company for future periods.

Securities Purchase Agreement

On April 19, 2011, the Company and the Bank entered into a securities purchase agreement with Priam Capital Fund I, LP, which was subsequently amended on September 21, 2011 to, among other things, extend the agreement to November 30, 2011. For a description of the material terms of the securities purchase agreement, see the Company s Current Report on Form 8-K filed with the Securities and Exchange Commission on April 25, 2011. For additional information on the terms of the amendment, see Exhibit 10.1 to this Form 10-Q and the Company s Current Report on Form 8-K filed with the Securities and Exchange Commission on September 27, 2011.

Liquidity

The Bank s principal sources of liquidity are cash and cash equivalents (which are cash on hand and amounts due from financial institutions, federal funds sold, money market mutual funds, and interest bearing deposits), AFS securities, deposit accounts, and borrowings. The levels of such sources are dependent on the Bank s operating, financing, and investing activities at any given time. We attempt to primarily rely on core deposits from customers to provide stable and cost-effective sources of funding to support our loan growth. We also seek to augment such deposits with longer term and higher yielding certificates of deposit. Cash and cash equivalents, which totaled $186.7 million at September 30, 2011, have immediate availability to meet our short-term funding needs. Our entire investment portfolio is classified as AFS, is highly marketable (excluding our holdings of pooled trust preferred securities), and is available to meet our liquidity needs. Additional sources of liquidity include loans held for sale, which totaled $126.2 million at September 30, 2011, are committed to be sold into the secondary market, and generally are funded within 60 days and our residential real estate portfolio includes loans that are underwritten to secondary market criteria. Additionally, our residential construction loan portfolio provides a source of liquidity as construction periods generally range from 9-12 months, and these loans are subsequently refinanced with permanent first-lien mortgages and sold into the secondary market. Our loan to deposit ratio stood at 71.4% at September 30, 2011 and 72.4% at December 31, 2010.

(7) Employee Benefit Plans

Profit Sharing Plan

We established a defined contribution plan in 1997, covering our employees meeting certain age and service eligibility requirements. The Plan provides for cash deferrals qualifying under Section 401(k). In December 31, 2008, we suspended the company-match contributions.

Stock Options and Warrants

We have stock option plans, which provide for the granting of options to acquire First Mariner common stock to our directors and key employees. Option exercise prices are equal to or greater than the fair market value of the common stock on the date of the grant.

We account for stock options issued under our stockholder-approved Long-Term Incentive Plan (the Plan) in accordance with FASB guidance on share-based payments. The plan permits the granting of share options and shares to our directors and key employees. We recognized stock based compensation costs of $7,000 for the three months ended September 30, 2010 and $5,000 and $21,000 for the nine

months ended September 30, 2011 and 2010, respectively. We did not record any stock compensation expense during the third quarter of 2011. As of September 30, 2011, all compensation expense related to currently outstanding options and warrants has been recognized.

During 2010, we issued warrants to purchase 366,174 shares of common stock in Exchange transactions with Mr. Hale, the Company s CEO, and with an unaffiliated third party (see additional information in Note 5). The warrants vested immediately upon issuance.

As of September 30, 2011, all options and warrants to purchase shares of common stock were fully vested. All options expire 10 years after the date of grant. The warrants expire five years after date of issuance.

Information with respect to stock options and warrants is as follows for the nine months ended September 30, 2011 and 2010:

	2011						2010					
	Number of Shares	**Weighted-Average Exercise Price**		**Weighted-Average Remaining Contractual Term** *(in years)*	**Aggregate Intrinsic Value** *(in thousands)*		**Number of Shares**	**Weighted-Average Exercise Price**		**Weighted-Average Remaining Contractual Term** *(in years)*	**Aggregate Intrinsic Value** *(in thousands)*	
Outstanding at beginning of year	930,228	$	7.92				668,593	$	12.20			
Granted							366,174		1.15			
Forfeited/cancelled	(89,650)		2.65				(103,339)		11.63			
Oustanding at end of year	840,578		8.02	3.0	$		931,428		7.92	3.6	$	
Exercisable at end of year	840,578		8.02	3.0	$		926,428		7.93	3.6	$	

The weighted average fair value of the warrants issued for the nine months ended September 30, 2010 was $0.74. There were no options granted or warrants issued in 2011. The fair value of the warrants was calculated using the Black-Scholes-Merton option-pricing model with the following weighted average assumptions for the nine months ended September 30, 2010:

Dividend yield	
Expected volatility	92.87%
Risk-free interest rate	2.60%
Expected lives	5 years

There were no options or warrants exercised during 2011 or 2010.

Options and warrants outstanding are summarized as follows at September 30, 2011:

Exercise Price	**Options and Warrants Outstanding and Excersiable** *(shares)*	**Weighted Average Remaining Contractual Life** *(in years)*
$ 1.09	18,348	3.7
1.15	347,826	3.5
4.15	11,200	6.6
5.41	2,754	6.2
5.70	34,500	6.5
9.16	850	0.2
9.86	1,350	1.0
10.45	91,250	0.3
10.70	650	0.5
11.68	125,250	1.3
11.95	600	1.3
12.03	2,500	0.6
13.00	700	1.5
13.33	7,300	5.6
13.52	3,000	1.6
16.67	4,800	3.6
16.70	1,800	4.1
16.95	2,300	2.1
17.45	18,500	4.2
17.77	133,100	3.3
18.20	4,950	2.6
18.38	18,650	2.3
18.94	2,350	5.1
19.30	6,050	4.6
	840,578	

(8) Comprehensive Loss

Comprehensive loss is defined as net loss plus transactions and other occurrences which are the result of nonowner changes in equity. Our nonowner equity changes are comprised of unrealized gains or losses on AFS securities that are accumulated with net loss in determining comprehensive loss.

Components of our comprehensive loss are as follows for the three and nine months ended September 30:

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
(dollars in thousands)	**2011**	**2010**	**2011**	**2010**
Net loss	$ (7,960)	$ (4,608)	$ (26,269)	$ (12,705)
Other comprehensive income items:				
Unrealized holding (losses) gains on securities arising during the period (net of tax (benefit) expense of $(219), $73, $309, and $326, respectively)	(324)	108	457	481
Reclassification adjustment for net losses on securities (net of tax benefit of ($17, $329, $15, and $482, respectively) included in net loss	26	487	22	713

Total other comprehensive (loss) income	(298)	595	479	1,194
Total comprehensive loss	$ (8,258)	$ (4,013)	$ (25,790)	$ (11,511)

(9) Loss Per Share

Basic loss per share is computed by dividing loss available to common stockholders by the weighted-average number of common shares outstanding. Diluted loss per share is computed after adjusting the denominator of the basic loss per share computation for the effects of all dilutive potential common shares outstanding during the period. The dilutive effects of options, warrants and their equivalents are computed using the treasury stock method. For the three- and six-month periods ended September 30, 2011 and 2010, all options and warrants were antidilutive and excluded from the computations due to our realized net losses.

Information relating to the calculation of loss per common share is summarized as follows for the three and nine months ended September 30:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in thousands, except for per share data)	**2011**	**2010**	**2011**	**2010**
Weighted-average share outstanding - basic and dilutive	18,860,482	17,871,565	18,637,600	13,674,155
Net loss from continuing operations	$ (7,960)	$ (4,608)	$ (26,269)	$ (12,505)
Net loss from discontinued operations				(200)
Net loss	$ (7,960)	$ (4,608)	$ (26,269)	$ (12,705)
Basic:				
Net loss from continuing operations	$ (0.42)	$ (0.26)	$ (1.41)	$ (0.92)
Net loss from discontinued operations				(0.01)
Net loss	$ (0.42)	$ (0.26)	$ (1.41)	$ (0.93)
Diluted:				
Net loss from continuing operations	$ (0.42)	$ (0.26)	$ (1.41)	$ (0.92)
Net loss from discontinued operations				(0.01)
Net loss	$ (0.42)	$ (0.26)	$ (1.41)	$ (0.93)

(10) Fair Value of Financial Instruments

We group financial assets and financial liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 Valuations for assets and liabilities traded in active exchange markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third party pricing services for identical or comparable assets or liabilities which use observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Financial Instruments Measured on a Recurring Basis

The following table presents fair value measurements for assets, liabilities, and off-balance sheet items that are measured at fair value on a recurring basis:

	September 30, 2011				
(dollars in thousands)	**Carrying Value**	**Quoted Prices (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Total Changes In Fair Values Included In Period Losses**
Securities:					
Mortgage-backed securities	$ 1,963	$	$ 1,963	$	$
Trust preferred securities	10,218		9,517	701	(818)(1)
U.S. government agency notes	8,513		8,513		
U.S. Treasury securities	1,015		1,015		
Equity securities - banks	151		151		
Equity securities - mutual funds	786		786		
	$ 22,646	$	$ 21,945	$ 701	$ (818)
Warrants	$ 48	$	$	$ 48	$
LHFS	126,191		126,191		4,080
Interest rate lock commitments (IRLC or IRLCs) (notional amount of $183,564)	187,205		187,205		3,116
Forward contracts to sell mortgage-backed securities (notional amount of $146,500)	144,052		144,052		(7,922)

(1) Represents net OTTI charges taken on certain Level 3 securities

	December 31, 2010				
(dollars in thousands)	**Carrying Value**	**Quoted Prices (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Total Changes In Fair Values Included In Period Losses**
Securities:					
Mortgage-backed securities	$ 2,325	$	$ 2,325	$	$
Trust preferred securities	10,464		9,477	987	(1,249)(1)
U.S. government agency notes	12,071		12,071		
U.S. Treasury securities	1,001		1,001		
Corporate obligations	1,010		1,010		
Equity securities - banks	197		197		
Equity securities - mutual funds	758		758		
	$ 27,826	$	$ 26,839	$ 987	$ (1,249)
Mortgage servicing rights	$ 1,309	$	$	$ 1,309	$ (309)

Warrants	137		137	
LHFS	140,343	140,343		(655)
IRLCs (notional amount of $71,228)	71,753	71,753		479
Forward contracts to sell mortgage-backed securities (notional amount of $125,500)	127,424	127,424		(3,288)

(1) Represents net OTTI charges taken on certain Level 3 securities

Level 3 Financial Instruments

Financial instruments are considered Level 3 when their values are determined using pricing models, discounted cash flow methodologies, or similar techniques and at least one significant model assumption or input is unobservable. Level 3 financial instruments also include those for which the determination of fair value requires significant management judgment or estimation.

Securities AFS

The fair value of AFS securities is based on bid quotations received from securities dealers, bid prices received from an external pricing service, or modeling utilizing estimated cash flows, depending on the circumstances of the individual security.

As of September 30, 2011, $701,000 ($10.9 million par value) of our AFS securities (four securities) were classified as Level 3, all of which are pooled trust preferred securities. The market environment has continued to be inactive for these security types and made fair value pricing more subjective. The amount of Level 3 securities will likely continue to be a function of market conditions and additional security transfers from Level 2 to Level 3 could result if further market inactivity occurs.

The following table details the four Level 3 securities:

(dollars in thousands)	**Class**	**Remaining Par Value**	**Current Rating/Outlook** (1) **Moody s**	**Fitch**	**Maturity**	(2) **Auction Call Date**	(3) **Index**
ALESCO Preferred Funding VII	C-1	$ 1,000	Ca	C	7/23/2035	MAR 2015	3ML + 1.5%
ALESCO Preferred Funding XI	C-1	4,938	C	C	12/23/2036	JUNE 2016	3ML + 1.2%
MM Community Funding	B	2,500	Ca	C	8/1/2031	N/A	6ML + 3.1%
MM Community Funding IX	B-1	2,500	Caa3	C	5/1/2033	N/A	3ML + 1.8%

(1) Ratings as of September 30, 2011.
(2) Under the terms of the offering, if the notes have not been redeemed in full prior to the indicated call date then an auction of the collateral debt securities will be conducted and the collateral will be sold and the notes redeemed. If the auction is not successful, the collateral manager will conduct auctions on a quarterly basis until the rated notes are redeemed in full.
(3) 3/6ML - 3 or 6 Month LIBOR; LIBOR (London Interbank Offered Rate) - daily reference rate based on the interest rates at which banks offer to lend unsecured funds to other banks in the London wholesale money market or interbank market.

Classification of Level 3 indicates that significant valuation assumptions are not consistently observable in the market and, as such, fair values are derived using the best available data. We calculated fair value for these four securities by using a present value of future cash flows model, which incorporated assumptions as follows as of September 30, 2011:

	Key Model Assumptions Used In Pricing				
	Cumulative Default (1)	**Deferrals Cured** (2)	**Credit MTM** (3) (6)	**Liquidity Premium** (4)	**Liquidity MTM Adj** (5) (6)
ALESCO Preferred Funding VII	45.0%	2.0%	$ 46.60	12.00%	$ 37.78
ALESCO Preferred Funding XI	36.0%	3.6%	46.95	12.00%	38.14
MM Community Funding	72.0%	10.1%	8.67	12.00%	5.51
MM Community Funding IX	60.0%	8.9%	34.62	12.00%	30.67

(1) The anticipated level of total defaults from the issuers within the pool of performing collateral as of September 30, 2011. There are no recoveries assumed on any default.
(2) Deferrals that are cured occur 60 months after the initial deferral starts.
(3) The credit mark to market represents the discounted value of future cash flows after the assumption of current and future defaults discounted at the book rate of interest on the security.
(4) The risk of being unable to sell the instrument for cash at short notice without significant costs, usually indicative of the level of trading activity for a specific security or class of securities.
(5)

The liquidity mark to market adjustment on the security represents the difference between the value of the discounted cash flows based on the book interest rate and the value discounted at the liquidity premium. The credit MTM less the liquidity MTM equals the estimated fair value price of the security.

(6) Price per $100

	September 30, 2011		December 31, 2010	
	Model Result (1)	**Fair Value** *(in thousands)*	**Model Result** (1)(2)	**Fair Value** *(in thousands)*
ALESCO Preferred Funding VII	$ 8.82	$ 88	$ 9.38	$ 94
ALESCO Preferred Funding XI	8.81	435	7.81	386
MM Community Funding	3.16	79	9.88	247
MM Community Funding IX	3.95	99	10.41	260
		$ 701		$ 987

(1) Price per $100
(2) Based on December 31, 2010 assumptions

During 2011 and 2010, we determined that OTTI had occurred in our pooled trust preferred security portfolio. The amount of OTTI that is recognized through earnings is determined by comparing the present value of the expected cash flows to the amortized cost of the security. The discount rate used to determine the credit loss is the expected book yield on the security. The credit loss estimated under the aforementioned method that was charged to operating earnings totaled $681,000 and $818,000 for the three and nine months ended September 30, 2011, respectively, and $816,000 and $1.2 million for the three and nine months ended September 30, 2010, respectively.

Warrants

As of September 31, 2011, certain warrants were classified as Level 3. See Note 7 for information related to the calculation of fair value of the warrants.

The table below presents a reconciliation of financial instruments measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the three months ended September 30, 2011 and 2010:

	2011		2010		
(dollars in thousands)	**Securities**	**Warrants**	**Securities**	**MSRs**	**Warrants**
Balance at beginning of period	$ 959	$ 162	$ 1,125	$ 1,009	$ 251
Originated mortgage servicing rights (MSR or MSRs)				1	
MSR amortization				(63)	
Change in fair value included in additional paid-in capital		(114)			(52)
Total realized losses included in other comprehensive income	(681)		(816)	(5)	
Total unrealized gains included in other comprehensive income	423		576		
Balance at end of period	$ 701	$ 48	$ 885	$ 942	$ 199

The table below presents a reconciliation of financial instruments measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the nine months ended September 30, 2011 and 2010:

	2011			2010		
(dollars in thousands)	**Securities**	**MSRs**	**Warrants**	**Securities**	**MSRs**	**Warrants**
Balance at beginning of period	$ 987	$ 1,309	$ 137	$ 1,432	$ 1,176	$
Warrants issued						251
Originated MSRs					1	
MSR amortization		(135)			(218)	
Change in fair value included in additional paid-in capital			(89)			(52)
Total realized losses included in other comprehensive income	(818)			(1,249)	(17)	
Reduction due to transfer of servicing rights to NGFS		(1,174)				
Total unrealized gains included in other comprehensive income	532			702		
Balance at end of period	$ 701	$	$ 48	$ 885	$ 942	$ 199

There were no transfers between any of Levels 1, 2, and 3 during either the three or nine months ended September 30, 2011 or September 30, 2010. During the second quarter of 2011, we sold our MSRs to NGFS in conjunction with the imminent closing of that sales transaction, which occurred during the third quarter of 2011.

Other Financial Instruments Measured on a Recurring Basis

Loans Held for Sale

Loans held for sale are carried at fair value, which is determined based on outstanding investor commitments or, in the absence of such commitments, based on current investor yield requirements or third party pricing models.

IRLCs

We engage an experienced independent third party to estimate the fair market value of our IRLC. IRLCs are valued based upon mandatory pricing quotes from correspondent lenders less estimated costs to process and settle the loan. Fair value is adjusted for the estimated probability of the loan closing with the borrower.

Forward Contracts to Sell Mortgage-Backed Securities

Fair value of these commitments is determined based upon the quoted market values of the securities.

Financial Instruments Measured on a Nonrecurring Basis

We may be required, from time to time, to measure certain other financial assets and liabilities at fair value on a nonrecurring basis. These adjustments to fair value usually result from application of lower-of-cost-or-market accounting or write-downs of individual assets. For assets measured at fair value on a nonrecurring basis, the following tables provide the level of valuation assumptions used to determine each adjustment and the carrying value of the assets:

	September 30, 2011			
(dollars in thousands)	**Carrying Value**	**Quoted Prices (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Impaired loans	$ 62,497	$	$	$ 62,497
Real estate acquired through foreclosure	24,739			24,739

	December 31, 2010			
(dollars in thousands)	**Carrying Value**	**Quoted Prices (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Impaired loans	$ 71,970	$	$	$ 71,970
Real estate acquired through foreclosure	21,185			21,185

Impaired Loans

Allowable methods for estimating fair value for impaired loans include using the fair value of the collateral for collateral dependent loans or, where a loan is determined not to be collateral dependent, using the discounted cash flow method.

If the impaired loan is identified as collateral dependent, then the fair value method of measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal or utilizing some other method of valuation for the collateral and applying a discount factor to the value based on our loan review policy and procedures.

If the impaired loan is determined not to be collateral dependent, then the discounted cash flow method is used. This method requires the impaired loan to be recorded at the present value of expected future cash flows discounted at the loan s effective interest rate. The effective interest rate of a loan is the contractual interest rate adjusted for any net deferred loan fees or costs, premiums, or discounts existing at origination or acquisition of the loan.

For all loans other than TDRs, a partial charge-off is recorded to reduce the carrying amount of the loan to its fair value. For TDRs that have an estimated fair value that is below the carrying value, a specific reserve is established and remains part of the allowance until such time that it is determined the loan will proceed to foreclosure. Total impaired loans had a carrying value of $62.5 million and $72.0 million as of September 30, 2011 and December 31, 2010, respectively, with specific reserves of $450,000 and $588,000 as of September 30, 2011 and December 31, 2010, respectively.

Real Estate Acquired Through Foreclosure

We record foreclosed real estate assets at the lower of cost or estimated fair value (LCM) on their acquisition dates and at the lower of such initial amount or estimated fair value less estimated selling costs thereafter. Estimated fair value is generally based upon independent appraisal of the collateral or listing prices supported by broker recommendation. We consider these collateral values to be estimated using Level 3 inputs. We held real estate acquired through foreclosure of $24.7 million as of September 30, 2011 and $21.2 million as of December 31, 2010. During 2011, we added $16.1 million to real estate acquired through foreclosure and recorded write-downs and losses on sales, included in noninterest expense, of $5.7 million. We disposed of $8.6 million of foreclosed properties during 2011.

Other Financial Instruments

The carrying value and estimated fair value of financial instruments are summarized in the following table. Certain financial instruments disclosed previously in this footnote are excluded from this table.

(dollars in thousands)	September 30, 2011 Carrying Value	September 30, 2011 Estimated Fair Value	December 31, 2010 Carrying Value	December 31, 2010 Estimated Fair Value
Assets:				
Cash and cash equivalents	$ 186,664	$ 186,664	$ 217,961	$ 217,961
Loans receivable	736,672	738,225	811,687	812,417
Restricted stock investments	6,969	6,969	7,095	7,095
Liabilities:				
Deposits	1,031,878	1,045,956	1,121,889	1,141,321
Long- and short-term borrowings	117,808	119,244	118,287	120,150
Junior subordinated deferrable interest debentures	52,068	35,390	52,068	32,060

Pricing or valuation models are applied using current market information to estimate fair value. In some cases considerable judgment is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange. The use of different market assumptions and/or estimation methods may have a material effect on the estimated fair value amounts.

Cash and Cash Equivalents

The carrying amount for cash and cash equivalents approximates fair value due to the short maturity of these instruments.

Loans Receivable

Loans were segmented into portfolios with similar financial characteristics. Loans were also segmented by loan class. Each loan class was further segmented by fixed and adjustable rate interest terms and performing and nonperforming categories. The fair value of each loan class was calculated by discounting anticipated cash flows based on weighted-average contractual maturity, weighted-average coupon, and discount rate.

The fair value for nonperforming loans was determined utilizing FASB guidance on loan impairment.

Restricted Stock Investments

The carrying value of restricted stock investments is a reasonable estimate of fair value as these investments do not have a readily available market.

Deposits

The fair value of deposits with no stated maturity, such as noninterest-bearing deposits, interest-bearing NOW accounts, money market, and savings accounts, is deemed to be equal to the carrying amounts. The fair value of certificates of deposit is based on the discounted value of contractual cash flows. The discount rate for certificates of deposit was estimated using the rate currently offered for deposits of similar remaining maturities.

Long- and Short-Term Borrowings and Junior Subordinated Deferrable Interest Debentures

Long- and short-term borrowings and junior subordinated notes were segmented into categories with similar financial characteristics. Carrying values were discounted using a cash flow approach based on market rates.

Other Off-Balance Sheet Financial Instruments

The disclosure of fair value amounts does not include the fair values of any intangibles, including core deposit intangibles. Core deposit intangibles represent the value attributable to total deposits based on an expected duration of customer relationships.

Limitations

Fair value estimates are made at a specific point in time, based on relevant market information and information about financial instruments. These estimates do not reflect any premium or discount that could result from a one-time sale of our total holdings of a particular financial instrument. Because no market exists for a significant portion of our financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect estimates.

(11) Segment Information

We are in the business of providing financial services, and we operate in two business segments commercial and consumer banking and mortgage-banking. Commercial and consumer banking is conducted through the Bank and involves delivering a broad range of financial services, including lending and deposit taking, to individuals and commercial enterprises. This segment also includes our treasury and administrative functions. Mortgage-banking is conducted through First Mariner Mortgage, a division of the Bank, and involves originating first- and second-lien residential mortgages for sale in the secondary market and to the Bank.

The following tables present certain information regarding our business segments:

For the nine month period ended September 30, 2011:

(dollars in thousands)	**Commercial and Consumer Banking**	**Mortgage-Banking**	**Total**
Interest income	$ 33,309	$ 2,209	$ 35,518
Interest expense	14,042	883	14,925
Net interest income	19,267	1,326	20,593
Provision for loan losses	11,580		11,580
Net interest income after provision for loan losses	7,687	1,326	9,013
Noninterest income	7,585	7,942	15,527
Noninterest expense	44,321	6,488	50,809
Net intersegment income	1,674	(1,674)	
Net (loss) income before income taxes	$ (27,375)	$ 1,106	$ (26,269)
Total assets	$ 1,071,470	$ 126,191	$ 1,197,661

For the nine month period ended September 30, 2010:

(dollars in thousands)	**Commercial and Consumer Banking**	**Mortgage-Banking**	**Total**
Interest income	$ 38,328	$ 3,148	$ 41,476
Interest expense	17,567	2,205	19,772
Net interest income	20,761	943	21,704
Provision for loan losses	16,290		16,290
Net interest income after provision for loan losses	4,471	943	5,414
Noninterest income	9,040	13,499	22,539
Noninterest expense	44,417	6,789	51,206
Net intersegment income	1,775	(1,775)	
Net (loss) income before income taxes	$ (29,131)	$ 5,878	$ (23,253)
Total assets	$ 1,181,716	$ 151,623	$ 1,333,339

(12) Recent Accounting Pronouncements

Pronouncements Adopted

In July, 2010, the FASB issued Accounting Standards Update (ASU) No. 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, which requires companies to improve their disclosures about the credit quality of their financing receivables and the credit reserves held against them. The standard is effective for interim and annual reporting periods ending after December 15, 2010. In January of 2011, this standard was updated by ASU No. 2011-01, *Receivables (Topic 310) Deferral of the Effective Date of Disclosure about Troubled Debt Restructurings in Update No. 2010-20,* which temporarily delays the provisions of ASU No. 2010-20 for troubled debt restructurings until the FASB clarifies the guidance for determining what constitutes a troubled debt restructuring in order to ensure more consistent disclosures about troubled debt restructurings. The effective date for the new TDR guidance is for interim and annual periods ending after June 15, 2011. We began providing the aforementioned disclosures in the Consolidated Financial Statements as of and for the three years ended December 31, 2010.

In April 2011, the FASB issued Accounting Standards Update (ASU) No. 2011-02, *A Creditor s Determination of Whether a Restructuring Is a Troubled Debt Restructuring*. ASU No. 2011-02 provides additional guidance and clarification to help creditors in determining whether a creditor

has granted a concession and whether a debtor is experiencing financial difficulties for purposes of determining whether a restructuring constitutes a troubled debt restructuring. The provisions of ASU No. 2011-02 were effective for the Company s reporting period ended September 30, 2011 and were applied retrospectively to January 1, 2011. The adoption of this ASU did not have a material impact on the Company s statements of operations or financial condition.

Pronouncements Issued

In June 2011, the FASB issued guidance on the reporting and presentation of comprehensive income. This guidance eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders equity and requires an entity to present items of net income, other comprehensive income and total comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The guidance also requires companies to display reclassification adjustments for each component of other comprehensive income in both net income and other comprehensive income. The amendments in this guidance do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. The new guidance was originally proposed to be effective for fiscal years, and interim periods within those years, beginning after December 15, 2011 and applied retrospectively. In October 2011, the FASB proposed to defer the effective date of certain provisions in the guidance related to the presentation of reclassification adjustments. No effective date has been announced. As the new guidance requires additional presentation only, there will be no impact to the Company s consolidated results of operations or financial position.

Item 2 - Management s Discussion and Analysis of Financial Condition and Results of Operations

When used in this report, the terms the Company, we, us, and our refer to First Mariner Bancorp and, unless the context requires otherwise, it s consolidated subsidiary. The following discussion should be read and reviewed in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations set forth in First Mariner Bancorp s Annual Report on Form 10-K for the year ended December 31, 2010.

Recent Developments

NASDAQ Delisting

On August 30, 2011, we received a letter from NASDAQ notifying us that NASDAQ had determined to deny our request for continued listing on NASDAQ. NASDAQ indicated that it would suspend the trading of the shares of Company common stock effective at the open of business on September 1, 2011. The Company s common stock was quoted on the Over-the-Counter Bulletin Board (OTCBB) starting on September 1. NASDAQ s determination was based on the Company s failure to comply with: (1) NASDAQ Listing Rule 5450(b), which requires maintenance of a minimum of $2.5 million in shareholders equity; and (2) NASDAQ Listing Rule 5450(a)(1), which requires maintenance of a minimum bid price of $1.00 per share.

Securities Purchase Agreement

On April 19, 2011, the Company and the Bank entered into a securities purchase agreement with Priam Capital Fund I, LP, which was subsequently amended on September 21, 2011 to, among other things, extend the agreement to November 30, 2011. For a description of the material terms of the securities purchase agreement, see the Company s Current Report on Form 8-K filed with the Securities and Exchange Commission on April 25, 2011. For additional information on the terms of the amendment, see Exhibit 10.1 to this Form 10-Q and the Company s Current Report on Form 8-K filed with the Securities and Exchange Commission on September 27, 2011.

The Company

First Mariner Bancorp is a bank holding company incorporated under the laws of Maryland and registered under the federal Bank Holding Company Act of 1956, as amended. First Mariner Bancorp s business is conducted primarily through its wholly-owned subsidiary, First Mariner Bank (the Bank). The Company had over 520 employees (approximately 508 full-time equivalent employees) as of September 30, 2011.

The Bank, with assets exceeding $1.1 billion as of September 30, 2011, is engaged in the general commercial banking business, with particular attention and emphasis on the needs of individuals and small to mid-sized businesses, and delivers a wide range of financial products and services that are offered by many larger competitors. The Bank s primary market area for its core banking operations, which consist of traditional commercial and consumer lending, as well as retail and commercial deposit operations, is central Maryland and portions of Maryland s eastern shore. Products and services of the Bank include traditional deposit products, a variety of consumer and commercial loans, residential and commercial mortgage and construction loans, wire transfer services, nondeposit investment products, and Internet banking and similar services. Most importantly, the Bank provides customers with access to local Bank officers who are empowered to act with flexibility to meet customers needs in an effort to foster and develop long-term loan and deposit relationships. The Bank is an independent community bank and its deposits are insured by the Federal Deposit Insurance Corporation (the FDIC).

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First Mariner Mortgage, a division of the Bank, engages in mortgage-banking activities, providing mortgages and associated products to customers and selling most of those mortgages into the secondary market. First Mariner Mortgage had assets of $126.2 million and $140.3 million as of September 30, 2011 and December 31, 2010, respectively, and generated revenue of $10.2 million and $16.6 million, respectively, for the nine months ended September 30, 2011 and 2010. They recognized income before income taxes of $1.1 million and $5.9 million during the nine months ended September 30, 2011 and 2010, respectively. Origination volume during the nine months ended September 30, 2011 and 2010 was $691.8 million and $915.8 million, respectively. During 2011, 69% of the originations were made in the state of Maryland, 12% in the immediately surrounding states and Washington, DC., and the remaining 19% in other states throughout the country. First Mariner Mortgage has offices in Maryland, Delaware, Virginia, and North Carolina. See Note 11 to the Consolidated Financial Statements for more detailed information on the results of our mortgage-banking operations.

Next Generation Financial Services (NGFS), a former division of the Bank, engages in the origination of reverse and conventional mortgage loans, providing these products directly through commission based loan officers throughout the United States. The final settlement of sale on this division occurred during the third quarter of 2011. We transferred all Mortgage Servicing Rights (MSR or MSRs) to the buyer of NGFS during the second quarter of 2011 and finalized the sale during the third quarter of 2011. We have not realized any significant benefit or loss from the sale of NGFS.

Critical Accounting Policies

The Company s consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and follow general practices within the industry in which it operates. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the consolidated financial statements and accompanying notes. These estimates, assumptions, and judgments are based on information available as of the date of the consolidated financial statements; accordingly, as this information changes, the consolidated financial statements could reflect different estimates, assumptions, and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions, and judgments and, as such, have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions, and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the consolidated financial statements at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. When applying accounting policies in such areas that are subjective in nature, management must use its best judgment to arrive at the carrying value of certain assets and liabilities. Below is a discussion of our critical accounting policies.

Allowance for loan losses

Our allowance for loan losses represents an estimated amount that, in management s judgment, will be adequate to absorb probable incurred losses on existing loans. The allowance for loan losses consists of an allocated component and an unallocated component. Management uses a disciplined process and methodology to establish the allowance for losses each quarter. To determine the total allowance for loan losses, we estimate the reserves needed for each class of the portfolio, including loans analyzed individually and loans analyzed on a pooled basis. The allowance for loan losses consists of amounts applicable to: (1) the commercial loan portfolio; (2) the commercial mortgage loan portfolio; (3) the construction loan portfolios (both commercial and consumer); (4) the residential mortgage loan portfolio; (5) the home equity and second mortgage loan portfolio; and (6) the other consumer loan portfolio.

To determine the balance of the allowance account, loans are pooled by portfolio class and losses are modeled using historical experience, quantitative analysis, and other mathematical techniques over the loss emergence period. For each class of loan, significant judgment is exercised to determine the estimation method that fits the credit risk characteristics of its portfolio segment. We use internally developed models in this process. Management must use judgment in establishing additional input metrics for the modeling processes. The models and assumptions used to determine the allowance are validated and reviewed to ensure that their theoretical foundation, assumptions, data integrity, computational processes, reporting practices, and end-user controls are appropriate and properly documented.

The establishment of the allowance for loan losses relies on a consistent process that requires multiple layers of management review and judgment and responds timely to changes in economic conditions and other influences. From time to time, events or economic factors may affect the loan portfolio, causing management to provide additional amounts to or release balances from the allowance for loan losses.

Management monitors differences between estimated and actual incurred loan losses, utilizing charge-off history. Loans deemed uncollectible are charged against, while recoveries are credited to, the allowance. Management adjusts the level of the allowance through the provision for loan losses, which is recorded as a current period operating expense.

Commercial (including commercial mortgages) and construction loans (including both commercial and consumer) are generally evaluated for impairment when the loan becomes 90 days past due and/or is rated as substandard. The difference between the fair value of the collateral, less estimated selling costs and the carrying value of the loan is charged-off at that time. Residential mortgage loans are generally charged down to their fair value when the loan becomes 120 days past due or is placed in nonaccrual status, whichever is earlier. Consumer loans are generally charged-off when the loan becomes 120 days past due or when it is determined that the amounts due are uncollectible (whichever is earlier). The above charge-off guidelines may not apply if the loan is both well secured and in the process of collection. These charge-off policies have not changed in the last three years.

As an additional portion of the allowance for loan losses, we also estimate probable losses related to unfunded loan commitments. These commitments are subject to individual review and are analyzed for impairment the same as a correspondent loan would be.

Securities available for sale (AFS)

We designate securities into one of three categories at the time of purchase. Debt securities that we have the intent and ability to hold to maturity are classified as held to maturity and recorded at amortized cost. Debt and equity securities are classified as trading if bought and held principally for the purpose of sale in the near term. Trading securities are reported at estimated fair value, with unrealized gains and losses included in earnings. Debt securities not classified as held to maturity and debt and equity securities not classified as trading securities are considered AFS and are reported at estimated fair value, with unrealized gains and losses reported as a separate component of stockholders equity, net of tax effects, in accumulated other comprehensive loss.

Securities AFS are evaluated periodically to determine whether a decline in their value is other than temporary. The term other than temporary is not intended to indicate a permanent decline in value. Rather, it means that the prospects for near term recovery of value are not necessarily favorable, or that there is a lack of evidence to support fair values equal to, or greater than, the carrying value of the security.

The initial indications of other-than-temporary impairment (OTTI) for both debt and equity securities are a decline in the market value below the amount recorded for an investment and the severity and duration of the decline. In determining whether an impairment is other than temporary, we consider the length of time and the extent to which the market value has been below cost, recent events specific to the issuer, including investment downgrades by rating agencies and economic conditions of its industry, our intent to sell the security, and if it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis. For marketable equity securities, we also consider the issuer s financial condition, capital strength, and near-term prospects. For debt securities and for perpetual preferred securities that are treated as debt securities for the purpose of OTTI analysis, we also consider the cause of the price decline (general level of interest rates and industry- and issuer-specific factors), the issuer s financial condition, near-term prospects and current ability to make future payments in a timely manner, the issuer s ability to service debt, and any change in agencies ratings at evaluation date from acquisition date and any likely imminent action. Once a decline in value is determined to be other than temporary, the security is segmented into credit- and noncredit-related components. Any impairment adjustment due to identified credit-related components is recorded as an adjustment to current period earnings, while noncredit-related fair value adjustments are recorded through accumulated other comprehensive loss. In situations where we intend to sell or it is more likely than not that we will be required to sell the security, the entire OTTI loss must be recognized in earnings.

Gains or losses on the sales of securities are calculated using a specific-identification basis and are determined on a trade-date basis. Premiums and discounts on securities are amortized (accreted) over the term of the security using methods that approximate the interest method. Gains and losses on trading securities are recognized regularly in income as the fair value of those securities changes.

Income Taxes

Deferred income taxes are recognized for the tax consequences of temporary differences between financial statement carrying amounts and the tax bases of assets and liabilities. Deferred income taxes are provided on income and expense items when they are reported for financial statement purposes in periods different from the periods in which these items are recognized in the income tax returns. Deferred tax assets are recognized only to the extent that it is more likely than not that such amounts will be realized based upon consideration of available evidence, including tax planning strategies and other factors.

We recognize a tax position as a benefit only if it is more likely than not that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely to be realized on examination. For tax positions not meeting the more likely than not test, no tax benefit is recorded. As of September 30, 2011 and December 31, 2010, we maintained a valuation allowance against the full amount of our deferred tax assets.

The calculation of tax liabilities is complex and requires the use of estimates and judgment since it involves the application of complex tax laws that are subject to different interpretations by us and the various tax authorities. These interpretations are subject to challenge by the tax authorities upon audit or to reinterpretation based on management s ongoing assessment of facts and evolving case law.

Periodically and in the ordinary course of business, we are involved in inquiries and reviews by tax authorities that normally require management to provide supplemental information to support certain tax positions we take in our tax returns. Uncertain tax positions are initially recognized in the financial statements when it is more likely than not the position will be sustained upon examination by the tax authorities. Such tax positions are initially and subsequently measured as the largest amount of tax benefit that is greater than 50% likely of being realized upon ultimate settlement with the tax authority assuming full knowledge of the position and all relevant facts. Management believes it has taken appropriate positions on its tax returns, although the ultimate outcome of any tax review cannot be predicted with certainty. No assurance can be given that the final outcome of these matters will not be different than what is reflected in the current and historical financial statements.

We recognize interest and penalties related to income tax matters in income tax (benefit) expense.

Loan income recognition

Interest income on loans is accrued at the contractual rate based on the principal outstanding. Loan origination fees and certain direct loan origination costs are deferred and amortized as a yield adjustment over the contractual loan terms or until the date of sale or disposition. Accrual of interest is discontinued when its receipt is in doubt, which typically occurs when a loan becomes impaired. Any interest accrued to income in the year when interest accruals are discontinued is generally reversed. Management may elect to continue the accrual of interest when a loan is in the process of collection and the estimated fair value of the collateral is sufficient to satisfy the principal balance and accrued interest. Loans are returned to accrual status once the doubt concerning collectability has been removed and the borrower has demonstrated the ability to pay and remain current. Payments on nonaccrual loans are applied to principal.

Real Estate Acquired Through Foreclosure

We record foreclosed real estate assets at the lower of cost or estimated fair value (LCM) on the acquisition date and at the lower of such initial amount or estimated fair value less estimated selling costs thereafter. Estimated fair value is based upon many subjective factors, including location and condition of the property and current economic conditions, among other things. Because the calculation of fair value relies on estimates and judgments relating to inherently uncertain events, results may differ from our estimates.

Write-downs at time of transfer are made through the allowance for loan losses. Write-downs subsequent to transfer are included in our noninterest expenses, along with operating income, net of related expenses of such properties and gains or losses realized upon disposition.

Financial Condition

At September 30, 2011, our total assets were $1.2 billion compared to the $1.3 billion at December 31, 2010. Earning assets decreased $108.4 million, or 10.5%, to $926.9 million at September 30, 2011 from $1.0 billion at December 31, 2010. We experienced decreases in all of our interest-earning asset categories. Deposits and capital decreased $90.0 million and $25.3 million, respectively.

Securities

We utilize the securities portfolio as part of our overall asset/liability management practices to enhance interest revenue while providing necessary liquidity for the funding of loan growth or deposit withdrawals. We continually monitor the credit risk associated with investments and diversify the risk in the securities portfolios. We held $22.6 million and $27.8 million, respectively, in securities classified as AFS as of September 30, 2011 and December 31, 2010. During the nine months ended September 30, 2011, we purchased $59.8 million in U.S. Agency and mortgage-backed securities in order to utilize some of our excess liquidity.

We recorded $818,000 and $1.2 million in net OTTI charges during the nine months ended September 30, 2011 and 2010, respectively, related to pooled trust preferred securities. Overall market values of securities have improved as evidenced by a net unrealized loss on securities classified as AFS of $3.1 million at September 30, 2011 compared to a net unrealized loss of $3.6 million at December 31, 2010.

The trust preferred securities we hold in our securities portfolio were issued by other banks, bank holding companies, and insurance companies. Certain of these securities have experienced declines in credit ratings from credit rating firms, which have devalued these specific securities. While some of these issuers have reported weaker financial performance since acquisition of these securities, in management s opinion, they continue to possess acceptable credit risk. We monitor the actual default rates and interest deferrals for possible losses and contractual shortfalls of interest or principal, which could warrant further recognition of impairment.

All of the remaining securities that are temporarily impaired are impaired due to declines in fair values resulting from changes in interest rates or increased credit/liquidity spreads compared to the time they were purchased. We have the intent to hold these securities to maturity and it is more likely than not that we will not be required to sell the securities before recovery of value. As such, management considers the impairments to be temporary.

Our securities AFS portfolio composition is as follows:

(dollars in thousands)	**September 30, 2011**	**December 31, 2010**
Mortgage-backed securities	$ 1,963	$ 2,325
Trust preferred securities	10,218	10,464
U.S. government agency notes	8,513	12,071
U.S. Treasury securities	1,015	1,001
Corporate obligations		1,010
Equity securities - banks	151	197
Equity securities - mutual funds	786	758
	$ 22,646	$ 27,826

Loans Held for Sale (LHFS)

We originate residential mortgage loans for sale on the secondary market. At September 30, 2011 and December 31, 2010, such loans held for sale amounted to $126.2 million and $140.3 million, respectively.

When we sell mortgage loans we make certain representations to the purchaser related to loan ownership, loan compliance and legality, and accurate documentation, among other things. If a loan is found to be out of compliance with any of the representations subsequent to the date of purchase, we may be required to repurchase the loan or indemnify the purchaser for losses related to the loan, depending on the agreement with the purchaser. In addition other factors may cause us to be required to repurchase or make-whole a loan previously sold.

Prior to January 1, 2008, we used investor contracts that required us to repurchase and make-whole requests on loans sold prior to that date. We experienced losses on loans closed prior to 2008 due to borrower loan payment default. After January 1, 2008, we revised our contract and terms process to include the elimination of early payment default as a risk factor in the majority of our investor contracts and resulting loan sales. The most common reason for a loan repurchase for loans sold since January 1, 2008 is due to a documentation error or disagreement with an investor or on rare occasions for fraud. Repurchase requests are negotiated with each investor at the time we are notified of the demand and an appropriate reserve is taken at that time. Repurchase and or make-whole requests are initially negotiated by the secondary marketing department and monitored by the secondary marketing committee where most disagreements are resolved with no reserve requirement or loss to the Company. In the event there is an unresolved repurchase or make-whole request, the loan is managed by the secondary marketing committee and is elevated to be monitored by the mortgage overview committee to determine the final settlement terms with the investor. Repurchases amounted to $435,000 and $1.2 million during the nine months ended September 30, 2011 and 2010, respectively. Our reserve for potential repurchases was $647,000 and $127,000 as of September 30, 2011 and December 31, 2010, respectively. These reserves were calculated based upon an analysis of the specific loans in question. We do not foresee increases in repurchases to be a growing trend nor do we see it having a significant impact on our financial results.

Loans

Our loan portfolio is expected to produce higher yields than investment securities and other interest-earning assets; the absolute volume and mix of loans and the volume and mix of loans as a percentage of total earning assets is an important determinant of our net interest margin.

The following table sets forth the composition of our loan portfolio:

(dollars in thousands)	**September 30, 2011**	**Percent of Total**	**December 31, 2010**	**Percent of Total**
Commercial	$ 62,775	8.5%	$ 78,801	9.7%
Commercial mortgage	335,106	45.5%	349,411	43.0%
Commercial construction	54,076	7.4%	58,764	7.2%
Consumer construction	21,593	2.9%	30,792	3.8%
Residential mortgage	124,578	16.9%	144,209	17.8%
Consumer	138,544	18.8%	149,710	18.5%
Total loans	$ 736,672	100.0%	$ 811,687	100.0%

Total loans decreased $75.0 million during the first nine months of 2011. We experienced lower balances in all loan types: commercial (-$16.0 million), commercial mortgage (-$14.3 million), commercial construction (-$4.7 million), consumer construction (-$9.2 million), residential mortgage (-$19.6 million), and consumer (-$11.2 million). During the first nine months of 2011, we were less aggressive in our loan origination activity, as we focused on improving asset quality and controlling our growth of assets to improve our capital ratios.

Commercial Construction Portfolio

Our commercial construction portfolio consists of construction and development loans for commercial purposes and includes loans made to builders and developers of residential real estate projects. Of the September 30, 2011 total included above, $23.1 million represents loans made to borrowers for the development of residential real estate. This segment of the portfolio has exhibited greater weakness (relative to our other loan portfolios) during 2010 and 2011 due to overall weakness in the residential housing sector.

The breakdown of the portion of the commercial construction portfolio made to borrowers for residential real estate developments is as follows as of September 30, 2011 and December 31, 2010:

(dollars in thousands)	**September 30, 2011**	**December 31, 2010**
Raw residential land	$ 5,949	$ 6,617
Residential subdivisions	4,261	5,653
Single residential lots	3,068	3,589
Single family construction	4,481	4,949
Townhome construction	668	912
Multi-family unit construction	4,685	6,135
	$ 23,112	$ 27,855

Transferred Loans

In accordance with the Financial Accounting Standards Board (FASB) guidance on accounting for certain mortgage-banking activities, any loans which are originally originated for sale into the secondary market and which we subsequently transfer into the Company s loan portfolio are valued at fair value at the time of the transfer with any decline in value recorded as a charge to operating expense. We maintained $26.6 million in first-lien mortgage loans and $1.1 million in second-lien mortgage loans that were transferred from loans held for sale to our mortgage and consumer loan portfolios at September 30, 2011.

Credit Risk Management

Credit risk is the risk of loss arising from the inability of a borrower to meet its obligations and entails both general risks, which are inherent in the process of lending, and risks specific to individual borrowers. Our credit risk is mitigated through portfolio diversification, which limits exposure to any single customer, industry, or collateral type.

We manage credit risk by evaluating the risk profile of the borrower, repayment sources, the nature of the underlying collateral, and other support given current events, conditions, and expectations. We attempt to manage the risk characteristics of our loan portfolio through various control processes, such as credit evaluation of borrowers, establishment of lending limits, and application of lending procedures, including the holding of adequate collateral and the maintenance of compensating balances. However, we seek to rely primarily on the cash flow of our borrowers as the principal source of repayment. Although credit policies and evaluation processes are designed to minimize our risk, management recognizes that loan losses will occur and the amount of these losses will fluctuate depending on the risk characteristics of our loan portfolio, as well as general and regional economic conditions.

Management has an established methodology to determine the adequacy of the allowance for loan losses that assesses the risks and losses inherent in the loan portfolio. Our allowance methodology employs management s assessment as to the level of future losses on existing loans based on our internal review of the loan portfolio, including an analysis of the borrowers current financial position, and the consideration of current and anticipated economic conditions and their potential effects on specific borrowers and/or lines of business. In determining our ability to collect certain loans, we also consider the fair value of any underlying collateral. In addition, we evaluate credit risk concentrations, including trends in large dollar exposures to related borrowers, industry and geographic concentrations, and economic and environmental factors.

For purposes of determining the allowance for loan losses, we have segmented our loan portfolio by product type. Our loan segments are commercial, commercial mortgage, commercial construction, consumer construction, residential mortgage, and consumer. We have looked at all segments to determine if subcategorization into classes is warranted based upon our credit review methodology. As of September 30, 2011, we divided consumer loans into two classes, (1) home equity and second mortgage loans and (2) other consumer loans. For each class of loan, significant judgment is exercised to determine the estimation method that fits the credit risk characteristics of its portfolio segment. We use internally developed models in this process. Management must use judgment in establishing additional input metrics for the modeling processes. The models and assumptions used to determine the allowance are independently validated and reviewed to ensure that their theoretical foundation, assumptions, data integrity, computational processes, reporting practices, and end-user controls are appropriate and properly documented.

The establishment of the allowance for loan losses relies on a consistent process that requires multiple layers of management review and judgment and responds timely to changes in economic conditions and other influences. From time to time, events or economic factors may affect the loan portfolio, causing management to provide additional amounts to or release balances from the allowance for loan losses.

To establish the allowance for loan losses, which we do on a quarterly basis, loans are pooled by portfolio class and an historical loss percentage is applied to each class. The historical loss percentage is based upon a rolling 24 month history, which gives us the most current and relevant charge-off data. The result of that calculation for each loan class is then applied to the current loan portfolio balances to determine the required allowance for loan loss level per loan class. We then apply additional loss multipliers to the different classes of loans to reflect various environmental factors. This amount is considered our unallocated reserve. These factors capture any changes in economic trends, portfolio composition, real estate trends, as well as other factors and are meant to supplement the required reserves. For individually evaluated loans (impaired loans), we do additional analyses to determine the impairment amount (see below for more detail on these calculations). In general, this impairment amount is included as part of the allowance for loan losses for troubled debt restructures (TDR or TDRs) and is charged-off for all other impaired loans. These loss estimates are performed under multiple economic scenarios to establish a range of potential outcomes for each criterion. Management applies judgment to develop its own view of loss probability within that range, using external and internal parameters with the objective of establishing an allowance for loss inherent within these portfolios as of the reporting date.

See our charge-off policies under Critical Accounting Policies Allowance for loan losses above.

See information on partial charge-offs later in this section.

Commercial

Credit risk in commercial lending, which includes commercial, commercial mortgage, commercial construction, and consumer construction loans, can vary significantly, as losses as a percentage of outstanding loans can shift widely during economic cycles and are particularly sensitive to changing economic conditions.

The risks associated with each portfolio class are as follows:

Commercial and Commercial Mortgage - The primary loan-specific risks in commercial and commercial mortgage loans are: deterioration of the business and/or collateral values, deterioration of the financial condition of the borrowers and/or guarantors, which creates a risk of default, and real estate collateral value determined through appraisals are not reflective of the true property values.

Portfolio risk includes condition of the economy, changing demand for these types of loans, large concentration of these types of loans, and geographic concentrations of these types of loans.

Commercial Construction loan-specific and portfolio risks related to commercial construction loans also carry the loan-specific and portfolio risks of commercial and commercial mortgage loans as described above. Additional loan-specific risks include budget overruns and performance variables related to the contractor and subcontractors.

Consumer Construction loan-specific and portfolio risks related to consumer construction loans to builders also carry the loan-specific and portfolio risks of commercial and commercial mortgage loans as described above. An additional loan-specific risk is the risk that the builder has a geographical concentration of developments. The risks related to consumer construction loans to ultimate homeowners carry the same risks as commercial construction loans as described above.

In general, improving economic conditions result in improved operating results on the part of commercial customers, enhancing their ability to meet debt service requirements. However, any improvements in operating cash flows can be offset by the impact of rising interest rates that could occur during improved economic times. Declining economic conditions have an adverse affect on the operating results of commercial customers, reducing their ability to meet debt service obligations.

Our commercial loans are generally reviewed individually, in accordance with FASB guidance on accounting for loan impairment, to determine impairment, accrual status, and the need for specific reserves. We use creditworthiness categories to grade commercial loans. Our internal grading system is based on experiences with similarly graded loans and incorporates a variety of risk considerations, both qualitative and quantitative (see definitions of our various grades and the composition of our loan portfolio within those grades in Note 4 to the Consolidated Financial Statements). Quantitative factors include collateral values, financial condition of borrowers, and other factors. Qualitative factors include judgments concerning general economic conditions that may affect credit quality, credit concentrations, the pace of portfolio growth, and delinquency levels; these qualitative factors are evaluated in connection with the unallocated portion of our allowance for loan losses. We periodically engage outside firms and experts to independently assess our methodology and perform various loan review functions. Commercial loans are generally evaluated for impairment when the loan becomes 90 day past due and/or is placed on nonaccrual status. The difference between that fair value of the collateral and the carrying value of the loan is charged-off at that time.

Consumer

Our consumer portfolio includes first- and second-lien mortgage loans and other loans to individuals. The risks associated with each portfolio class are as follows:

Residential Mortgage, Home Equities, and 2nd Mortgages The primary loan-specific risks related to residential mortgage, home equity, and 2nd mortgage lending include: unemployment, deterioration in real estate values, our ability to assess the creditworthiness of the customer, deterioration in the borrowers financial condition, whether the result of personal issues or a general economic downturn, and property values determined through appraisals are not reflective of the true property values. The portfolio risks for these types of loans are the same as for commercial and commercial mortgages as described above.

Other Consumer - The primary loan-specific risks of consumer loans are: unemployment, deterioration of the borrower s financial condition, whether the result of personal issues or a general economic downturn, and for certain consumer loans such as auto loans and boat loans, there is also a risk of deterioration in the value of the collateral. The portfolio risks for these types of loans are the same as for commercial and commercial mortgages as described above.

Generally, consumer loans are segregated into homogeneous pools with similar risk characteristics. We do not individually grade residential mortgage or consumer loans. Such loans are classified as performing or nonperforming. Trends such as delinquency and loss and current economic conditions in consumer loan pools are analyzed and historical loss experience is adjusted accordingly. Quantitative and qualitative adjustment factors for the different consumer portfolios are consistent with those for the commercial portfolios. Residential mortgage loans are generally charged down to their fair value when the loan becomes 120 days past due or is placed in nonaccrual status, whichever is earlier. Consumer loans are generally charged-off when the loan becomes 120 days past due or when it is determined that the amounts due are uncollectible (whichever is earlier). These charge-off guidelines may not apply if the loan is both well secured and in the process of collection or is a TDR (see discussion on TDRs later in this section).

Unallocated

The unallocated portion of the allowance is intended to provide for losses that are not identified when establishing the required portion of the allowance and is based upon management s evaluation of various conditions that are not directly measured in the determination of the formula and specific allowances. Such conditions include general economic and business conditions affecting key lending areas, credit quality trends (including trends in delinquencies and nonperforming loans expected to result from existing conditions), loan volumes, loan concentrations by class and geography and any changes in such concentrations, specific industry conditions within portfolio categories, duration of the current business cycle, bank regulatory examination results, and management s judgment with respect to various other conditions including changes in management, including credit, loan administration, and origination staff, changes in underwriting standards, lending policies, and procedures, the impact of any new or modified lines of business, level and trends in nonaccrual and delinquent loans and charge-offs, changes in underlying collateral for collateral dependent loans, and management and the quality of risk identification systems. Executive management reviews these conditions quarterly. Economic factors are an important consideration in determining the adequacy of the loan loss reserve. A strong regional and national economy will reduce the probability of losses. Weaker regional and national economies will usually result in

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higher unemployment, higher vacancies in commercial real estate, and declining values on both commercial and residential properties, which will gradually increase the probably of losses. Key measures of economic strength or weakness are unemployment levels, interest rates, and economic growth and confidence.

The following basis points have been added to the respective portfolios for environmental factors as follows:

September 30, 2011:

	Commercial	Commercial Mortgage	Commercial Construction	Consumer Construction	Residential Mortgage	Consumer
Concentration of credit and changes in level of concentration		5	5	8	10	
Nature and volume of portfolio		25	25	4	4	
Trends of past due and classified loans	1	10	10	10	10	
Economic factors	25	25	25	11	11	45
Value of underlying collateral for collateral dependent loans		20	20	20	20	
	26	85	85	53	55	45

December 31, 2010:

	Commercial	Commercial Mortgage	Commercial Construction	Consumer Construction	Residential Mortgage	Consumer
Concentration of credit and changes in level of concentration		5	5	8	10	
Nature and volume of portfolio		25	25	4	4	
Trends of past due and classified loans	1	10	10	10	10	
Economic factors	25	25	25	6	6	40
Value of underlying collateral for collateral dependent loans		15	15	15	15	
	26	80	80	43	45	40

Each of the above factors is evaluated quarterly. The factors applied to commercial mortgage and commercial and consumer construction loans were increased in 2011 due to a trend of decreasing appraised values and the general weak economy. The factors applied to residential mortgage and consumer loans were increased in 2011 as a result of increased unemployment rates and the general economic downturn. The factors for the commercial portfolio were unchanged from December 31, 2010 to September 30, 2011.

We have risk management practices designed to ensure timely identification of changes in loan risk profiles; however, undetected losses may exist inherently within the loan portfolio. The assessments aspects involved in analyzing the quality of individual loans and assessing collateral values can also contribute to undetected, but probable, losses.

See additional detail on our allowance methodology and risk rating system in Note 4 to the Consolidated Financial Statements.

The changes in the allowance are presented in the following table for the three and nine months ended September 30:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in thousands)	**2011**	**2010**	**2011**	**2010**
Allowance for loan losses, beginning of period	$ 14,115	$ 12,018	$ 14,115	$ 11,639
Charge-offs:				
Commercial	(2,368)	(1,904)	(5,240)	(1,904)
Commercial mortgage	(1,325)		(1,834)	(454)
Commercial construction	(131)	(3,103)	(728)	(3,967)
Consumer construction		(12)	(24)	(297)
Residential mortgage	(669)	(431)	(2,209)	(3,562)
Consumer	(590)	(1,568)	(2,021)	(3,160)
Total charge-offs	(5,083)	(7,018)	(12,056)	(13,344)
Recoveries:				
Commercial				
Commercial mortgage			168	
Commercial construction	24	7	24	7
Consumer construction				
Residential mortgage	23	8	37	97
Consumer	33	411	244	487
Total recoveries	80	426	473	591
Net charge-offs	(5,003)	(6,592)	(11,583)	(12,753)
Provision for loan losses	5,000	9,750	11,580	16,290
Allowance for loan losses, end of period	$ 14,112	$ 15,176	$ 14,112	$ 15,176
Loans (net of premiums and discounts):				
Period-end balance	$ 736,672	$ 832,902	$ 736,672	$ 832,902
Average balance during period	742,173	845,485	762,895	863,619
Allowance as a percentage of period-end loan balance	1.92%	1.82%	1.92%	1.82%
Percent of average loans:				
Provision for loan losses	2.67%	4.58%	2.03%	2.52%
Net charge-offs	2.67%	3.09%	2.03%	1.97%

The following table summarizes our allocation of allowance by loan type:

September 30, 2011	December 31, 2010