FIRST UNITED CORP/MD/
Form 10-Q
May 10, 2011

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

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For quarterly period ended March 31, 2011

¨ TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT
For the transition period from _______________ to ________________

Commission file number 0-14237

First United Corporation
(Exact name of registrant as specified in its charter)

Maryland	52-1380770
(State or other jurisdiction of incorporation or organization)	(I. R. S. Employer Identification No.)

19 South Second Street, Oakland, Maryland	21550-0009
(Address of principal executive offices)	(Zip Code)

(800) 470-4356
(Registrant's telephone number, including area code)

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

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 ¨ No ¨ (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 definition of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 6,166,037 shares of common stock, par value $.01 per share, as of April 30, 2011.

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FIRST UNITED CORPORATION

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

FIRST UNITED CORPORATION
Consolidated Statements of Financial Condition
(In thousands, except per share and percentage data)

	March 31, 2011 (Unaudited)	December 31, 2010
Assets		
Cash and due from banks	$88,414	$ 184,830
Interest bearing deposits in banks	64,949	114,483
Cash and cash equivalents	153,363	299,313
Investment securities – available-for-sale (at fair value)	225,729	229,687
Restricted investment in bank stock, at cost	12,449	12,449
Loans Held for Sale	44,502	—
Loans	936,040	1,009,753
Allowance for loan losses	(21,409)	(22,138)
Net loans	914,631	987,615
Premises and equipment, net	32,367	32,945
Goodwill and other intangible assets, net	14,633	14,700
Bank owned life insurance	30,659	30,405
Deferred tax assets	27,229	26,400
Other real estate owned	18,032	18,072
Accrued interest receivable and other assets	42,957	44,859
Total Assets	$1,516,551	$ 1,696,445
Liabilities and Shareholders’ Equity		
Liabilities:		
Non-interest bearing deposits	$128,998	$ 121,142
Interest bearing deposits	998,582	1,180,504
Total deposits	1,127,580	1,301,646
Short-term borrowings	42,998	39,139
Long-term borrowings	232,836	243,100
Accrued interest payable and other liabilities	16,173	16,920
Total Liabilities	1,419,587	1,600,805
Shareholders’ Equity:		
Preferred stock – no par value; Authorized 2,000 shares of which 30 shares of Series A, $1,000 per share liquidation preference, 5% cumulative increasing to 9% cumulative on February 15, 2014, were issued and outstanding on March 31, 2011 and December 31, 2010 (discount of $187 and $202, respectively)	29,813	29,798
Common Stock – par value $.01 per share; Authorized 25,000 shares; issued and outstanding 6,166 shares at March 31, 2011 and 6,166 shares at December 31, 2010	62	62

Surplus	21,454	21,422
Retained earnings	64,742	64,179
Accumulated other comprehensive loss	(19,107)	(19,821)
Total Shareholders' Equity	96,964	95,640
Total Liabilities and Shareholders' Equity	$1,516,551	$ 1,696,445

See accompanying notes to the consolidated financial statements.

FIRST UNITED CORPORATION
Consolidated Statements of Operations
(In thousands, except per share data)

	Three Months Ended March 31, 2011	2010
	(Unaudited)	
Interest income		
Interest and fees on loans	$13,855	$15,854
Interest on investment securities		
Taxable	705	2,643
Exempt from federal income tax	862	932
Total investment income	1,567	3,575
Other	147	92
Total interest income	15,569	19,521
Interest expense		
Interest on deposits	3,671	4,615
Interest on short-term borrowings	61	66
Interest on long-term borrowings	2,426	2,847
Total interest expense	6,158	7,528
Net interest income	9,411	11,993
Provision for loan losses	1,344	3,555
Net interest income after provision for loan losses	8,067	8,438
Other operating income		
Changes in fair value on impaired securities	691	(11,217)
Portion of (gain)/loss recognized in other comprehensive income (before taxes)	(710)	3,703
Net securities impairment losses recognized in operations	(19)	(7,514)
Net gains/(losses) – other	101	(2,088)
Total net gains/(losses)	82	(9,602)
Service charges	925	1,118
Trust department	1,064	986
Insurance commissions	623	623
Debit card income	608	363
Bank owned life insurance	254	250
Other	347	243
Total other income	3,821	3,583
Total other operating income/(loss)	3,903	(6,019)
Other operating expenses		
Salaries and employee benefits	5,132	5,596
FDIC premiums	895	876
Equipment	815	830
Occupancy	738	736
Data processing	702	749
Other	2,631	2,358
Total other operating expenses	10,913	11,145
Income/(Loss) before income tax expense/(benefit)	1,057	(8,726)
Applicable income tax expense/(benefit)	100	(3,615)
Net Income/(Loss)	957	(5,111)
Accumulated preferred stock dividends and discount accretion	$(394)	$(390)

Net Income Available to/(Loss Attributable to) Common Shareholders	$563	$(5,501)
Basic net income/(loss) per common share	$.09	$(.90)
Diluted net income/(loss) per common share	$.09	$(.90)
Dividends declared per common share	$—	$.01
Weighted average number of common and diluted shares outstanding	6,166	6,144

See accompanying notes to the consolidated financial statements.

FIRST UNITED CORPORATION
Consolidated Statements of Changes in Shareholders' Equity
(In thousands, except share and per share data)

	Preferred Stock	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
Balance at January 1, 2010	$ 29,739	$ 61	$ 21,305	$ 76,120	$ (26,659)	$ 100,566
Comprehensive loss:						
Net loss for the year				(10,197)		(10,197)
Unrealized gain on securities available-for-sale, net of reclassifications and income taxes of $4,052					5,987	5,987
Change in accumulated unrealized losses for pension and SERP obligations, net of income taxes of $887					1,311	1,311
Unrealized loss on derivatives, net of income taxes of $312					(460)	(460)
Comprehensive loss						(3,359)
Issuance of 9,924 shares of common stock under dividend reinvestment plan		1	47			48
Stock based compensation			70			70
Preferred stock discount accretion	59			(59)		—
Preferred stock dividends paid				(1,125)		(1,125)
Preferred stock dividends declared				(375)		(375)
Common stock dividends declared - $.03 per share				(185)		(185)
Balance at December 31, 2010	29,798	62	21,422	64,179	(19,821)	95,640
Comprehensive income:						
Net income for the period				957		957
Unrealized gain on securities available-for-sale, net of reclassifications and income taxes of $416					613	613
Unrealized gain on derivatives, net of income taxes of $68					101	101
Comprehensive income						1,671
Stock based compensation			32			32
Preferred stock discount accretion	15			(15)		—

Preferred stock dividends declared								(379)				(379)
Balance at March 31, 2011	$	29,813	$	62	$	21,454	$	64,742	$	(19,107)	$	96,964

See accompanying notes to the consolidated financial statements.

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FIRST UNITED CORPORATION
Consolidated Statements of Cash Flows
(In thousands)

	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010
	(Unaudited)	
Operating activities		
Net income/(loss)	$957	$(5,111)
Adjustments to reconcile net income/(loss) to net cash provided by operating activities:		
Provision for loan losses	1,344	3,555
Depreciation	640	649
Stock compensation	32	33
Amortization of intangible assets	67	209
Loss on sales of other real estate owned	7	63
Write-downs of other real estate owned	63	34
Loss on disposal of fixed assets	3	—
Net amortization of investment securities discounts and premiums	610	40
Other-than-temporary-impairment loss on securities	19	7,514
Proceeds from sales of investment securities trading	—	1
Gain on trading securities	—	(1)
Gain on sales of investment securities – available-for-sale	(155)	(262)
Loss on transfers of available-for-sale securities to trading	—	2,254
Decrease/(increase) in accrued interest receivable and other assets	2,071	(2,426)
Deferred tax benefit	(1,313)	(1,670)
(Decrease)/increase in accrued interest payable and other liabilities	(1,126)	518
Earnings on bank owned life insurance	(254)	(250)
Net cash (used in)/provided by operating activities	2,965	5,150
Investing activities		
Proceeds from maturities/calls of investment securities available-for-sale	20,230	29,356
Proceeds from sales of investment securities available-for-sale	22,048	2,268
Purchases of investment securities available-for-sale	(37,765)	(33,748)
Proceeds from sales of other real estate owned	532	362
Net decrease in loans	26,576	16,435
Purchases of premises and equipment	(65)	(160)
Net cash provided by investing activities	31,556	14,513
Financing activities		
Net (decrease)/ increase in deposits	(174,066)	52,998
Net increase/(decrease) in short-term borrowings	3,859	(5,815)
Proceeds from long-term borrowings	—	3,609
Payments on long-term borrowings	(10,264)	(10,263)
Cash dividends paid on common stock	—	(614)
Preferred stock dividends paid	—	(375)
Net cash (used in)/provided by financing activities	(180,471)	39,540
(Decrease)/increase in cash and cash equivalents	(145,950)	59,203
Cash and cash equivalents at beginning of the year	299,313	189,671

Cash and cash equivalents at end of period	$153,363	$248,874
Supplemental information		
Interest paid	$5,283	$7,896
Non-cash investing activities:		
Transfers from loans to other real estate owned	$562	$3,119
Transfers from loans to loans held-for-sale	$44,502	$—
Transfers from available-for-sale to trading	$—	$117,078

See accompanying notes to the consolidated financial statements.

FIRST UNITED CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
FOR THE QUARTER ENDED MARCH 31, 2011

Note A – Basis of Presentation

The accompanying unaudited consolidated financial statements of First United Corporation and its consolidated subsidiaries, including First United Bank & Trust (the "Bank"), have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information, as required by the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 270, Interim Reporting, and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all the information and footnotes required for annual financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation, consisting of normal recurring items, have been included. Operating results for the three-month period ended March 31, 2011 are not necessarily indicative of the results that may be expected for the full year or for any future interim period. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in First United Corporation's Annual Report on Form 10-K for the year ended December 31, 2010. For purposes of comparability, certain prior period amounts have been reclassified to conform to the 2011 presentation. Such reclassifications had no impact on net income/(loss) or equity.

First United Corporation has evaluated events and transactions occurring subsequent to the statement of financial condition date of March 31, 2011 for items that should potentially be recognized or disclosed in these financial statements as prescribed by ASC Topic 855, Subsequent Events.

As used in these notes to consolidated financial statements, First United Corporation and its consolidated subsidiaries are sometimes collectively referred to as the "Corporation".

Note B – Earnings/(Loss) Per Common Share

Basic earnings/(loss) per common share is derived by dividing net income available to/(loss attributable to) common shareholders by the weighted-average number of common shares outstanding during the period and does not include the effect of any potentially dilutive common stock equivalents. Diluted earnings/(loss) per share is derived by dividing net income available to/(loss attributable to) common shareholders by the weighted-average number of shares outstanding, adjusted for the dilutive effect of outstanding common stock equivalents. There were no common stock equivalents at March 31, 2011. There is no dilutive effect on the earnings per share during loss periods.

The following table sets forth the calculation of basic and diluted earnings/(loss) per common share for the three-month periods ended March 31, 2011 and 2010:

	For the three months ended March 31,					
	2011			2010		
(in thousands, except for per share amount)	Income	Average Shares	Per Share Amount	Loss	Average Shares	Per Share Amount
Basic and Diluted Earnings Per Share:						
Net income/(loss)	$ 957			$ (5,111)		
Preferred stock dividends paid	—			(375)		
Preferred stock dividends deferred	(379)			—		
Discount accretion on preferred stock	(15)			(15)		
	$ 563	6,166	$ .09	$ (5,501)	6,144	$ (.90)

Net income available to/(loss attributable to)
common shareholders

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Note C – Net Gains/(Losses)

The following table summarizes the gain/(loss) activity for the three-month periods ended March 31, 2011 and 2010:

	Three months ended March 31,	
(in thousands)	2011	2010
Other-than-temporary impairment charges:		
Available-for-sale securities	$ (19)	$ (7,514)
Net gains/(losses) – other:		
Available-for-sale securities:		
Realized gains	237	262
Realized losses	(82)	—
Transfers of available-for-sale securities to trading:		
Gains recognized in earnings	—	2,852
Losses recognized in earnings	—	(5,106)
Trading securities:		
Gross gains on sales	—	1
Loss on sales of other real estate owned	(7)	(63)
Write-down of other real estate owned	(63)	(34)
Gain on sale of mortgage loans	19	—
Loss on disposal of fixed assets	(3)	—
Net gains/(losses) – other	101	(2,088)
Net gains/(losses)	$ 82	$ (9,602)

Note D – Cash and Cash Equivalents

Cash and due from banks, which represents vault cash in the retail offices and invested cash balances at the Federal Reserve, is carried at fair value.

	March 31, 2011	December 31, 2010
Cash and due from banks, weighted average interest rate of 0.25% (at March 31, 2011)	$88,414	$ 184,830

Interest bearing deposits in banks, which represent funds invested at a correspondent bank, are carried at fair value and, as of March 31, 2011 and December 31, 2010, consisted of daily funds invested at the Federal Home Loan Bank (“FHLB”) of Atlanta, First Tennessee Bank (“FTN”), Merchants and Traders (“M&T”) and Community Bankers Bank (“CBB”).

	March 31, 2011	December 31, 2010
FHLB daily investments, interest rate of 0.01% (at March 31, 2011)	$27,546	$ 77,102
FTN daily investments, interest rate of 0.10% (at March 31, 2011)	1,350	1,350
M&T Fed Funds sold, interest rate of 0.30% (at March 31, 2011)	6,010	6,004
CBB Fed Funds sold, interest rate of 0.22% (at March 31, 2011)	30,043	30,027
	$64,949	$ 114,483

Note E – Investments

The investment portfolio is classified and accounted for based on the guidance of ASC Topic 320, Investments – Debt and Equity Securities.

The following table shows a comparison of amortized cost and fair values of investment securities available-for-sale at March 31, 2011 and December 31, 2010:

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	OTTI in AOCI
March 31, 2011					
U.S. government agencies	$24,420	$45	$280	$24,185	$—
Residential mortgage-backed agencies	108,532	1,700	229	110,003	—
Collateralized mortgage obligations	729	—	82	647	—
Obligations of states and political subdivisions	79,653	1,168	589	80,232	—
Collateralized debt obligations	36,147	—	25,485	10,662	17,441
Totals	$249,481	$2,913	$26,665	$225,729	$17,441
December 31, 2010					
U.S. government agencies	$24,813	$101	$64	$24,850	$—
Residential mortgage-backed agencies	98,109	1,703	199	99,613	—
Collateralized mortgage obligations	763	—	101	662	—
Obligations of states and political subdivisions	94,250	1,011	537	94,724	—
Collateralized debt obligations	36,533	—	26,695	9,838	18,151
Totals	$254,468	$2,815	$27,596	$229,687	$18,151

Proceeds from sales of securities and the realized gains and losses are as follows:

	Three Months Ended March 31,	
(in thousands)	2011	2010
Proceeds	$ 22,048	$ 2,268
Realized gains	237	262
Realized losses	82	—

The following table shows the Corporation's available-for-sale securities with gross unrealized losses and fair values, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at March 31, 2011 and December 31, 2010:

	Less than 12 months		12 months or more	
(in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
March 31, 2011				
U.S. government agencies	$ 12,440	$ 280	$ —	$ —
Residential mortgage-backed agencies	38,331	229	—	—
Collateralized mortgage obligations	—	—	647	82
Obligations of states and political subdivisions	25,313	589	—	—
Collateralized debt obligations	—	—	10,662	25,485
Totals	$ 76,084	$ 1,098	$ 11,309	$ 25,567
December 31, 2010				
U.S. government agencies	$ 13,044	$ 64	$ —	$ —
Residential mortgage-backed agencies	19,453	199	—	—
Collateralized mortgage obligations	—	—	662	101
Obligations of states and political subdivisions	26,887	537	—	—
Collateralized debt obligations	—	—	9,838	26,695
Totals	$ 59,384	$ 800	$ 10,500	$ 26,796

Management systematically evaluates securities for impairment on a quarterly basis. Management assesses whether (a) it has the intent to sell a security being evaluated and (b) it is more likely than not that the Corporation will be required to sell the security prior to its anticipated recovery. If neither applies, then declines in the fair values of securities below their cost that are considered other-than-temporary declines are split into two components. The first is the loss attributable to declining credit quality. Credit losses are recognized in earnings as realized losses in the period in which the impairment determination is made. The second component consists of all other losses, which are recognized in other comprehensive loss. In estimating other-than-temporary impairment ("OTTI") losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) adverse conditions specifically related to the security, an industry, or a geographic area, (3) the historic and implied volatility of the fair value of the security, (4) changes in the rating of the security by a rating agency, (5) recoveries or additional declines in fair value subsequent to the balance sheet date, (6) failure of the issuer of the security to make scheduled interest or principal payments, and (7) the payment structure of the debt security and the likelihood of the issuer being able to make payments that increase in the future. Management also monitors cash flow projections for securities that are considered beneficial interests under the guidance of ASC Subtopic 325-40, Investments – Other – Beneficial Interests in Securitized Financial Assets, (ASC Section 325-40-35). Further discussion about the evaluation of securities for impairment can be found in Item 2 of Part I of this report under the heading "Investment Securities".

Management believes that the valuation of certain securities is a critical accounting policy that requires significant estimates in preparation of its consolidated financial statements. Management utilizes an independent third party to prepare both the impairment valuations and fair value determinations for its collateralized debt obligation ("CDO") portfolio consisting of pooled trust preferred securities. Management reviews the assumptions and results and does not believe that there were any material differences in the valuations between March 31, 2011 and December 31, 2010.

U.S. Government Agencies - Two U.S. government agencies have been in a slight unrealized loss position for less than 12 months as of March 31, 2011. The securities are of the highest investment grade and the Corporation does not intend to sell them, and it is not more likely than not that the Corporation will be required to sell them before recovery of their amortized cost basis, which may be at maturity. Therefore, no OTTI exists at March 31, 2011.

Residential Mortgage-Backed Agencies - Six residential mortgage-backed agencies have been in a slight unrealized loss position for less than 12 months as of March 31, 2011. The securities are of the highest investment grade and the Corporation does not intend to sell them, and it is not more likely than not that the Corporation will be required to sell them before recovery of their amortized cost basis, which may be at maturity. Therefore, no OTTI exists at March 31, 2011.

Collateralized Mortgage Obligations – The collateralized mortgage obligation portfolio, consisting of one security at March 31, 2011, has been in an unrealized loss position for 12 months or more. This security is a private label residential mortgage-backed security and is reviewed for factors such as loan to value ratio, credit support levels, borrower FICO scores, geographic concentration, prepayment speeds, delinquencies, coverage ratios and credit ratings. Management believes that this security continues to demonstrate collateral coverage ratios that are adequate to support the Corporation's investment. At the time of purchase, this security was of the highest investment grade and was purchased at a discount relative to its face amount. As of March 31, 2011, this security remains at investment grade and continues to perform as expected at the time of purchase. The Corporation does not intend to sell this security and it is not more likely than not that the Corporation will be required to sell the investment before recovery of its amortized cost basis, which may be at maturity. Accordingly, management does not consider this investment to be other-than-temporarily impaired at March 31, 2011.

Obligations of State and Political Subdivisions – The unrealized losses on the Corporation's investments in state and political subdivisions were $589,000 at March 31, 2011. Sixteen securities have been in an unrealized loss position for less than 12 months. All of these investments are of investment grade as determined by the major rating agencies and management reviews the ratings of the underlying issuers. Management believes that this portfolio is well-diversified throughout the United States, and all bonds continue to perform according to their contractual terms. The Corporation does not intend to sell these investments and it is not more likely than not that the Corporation will be required to sell the investments before recovery of their amortized cost basis, which may be at maturity. Accordingly, management does not consider these investments to be other-than-temporarily impaired at March 31, 2011.

Collateralized Debt Obligations - The $25.5 million in unrealized losses greater than 12 months at March 31, 2011 relates to 18 pooled trust preferred securities that comprise the CDO portfolio. See Note H for a discussion of the methodology used by management to determine the fair values of these securities. Based upon a review of credit quality and the cash flow tests performed by the independent third party, management determined that there was one security that had credit-related non-cash OTTI charges during the first quarter of 2011. As a result of this assessment, the Corporation recorded $19,000 in credit-related non-cash OTTI charges for the three-months ended March 31, 2011. The unrealized losses on the remaining securities in the portfolio are primarily attributable to continued depression in market interest rates, marketability, liquidity and the current economic environment.

The following tables present a cumulative roll-forward of the amount of non-cash OTTI charges related to credit losses which have been recognized in earnings for debt securities held and not intended to be sold for the three-month periods ended March 31, 2011 and 2010:

(in thousands)	March 31, 2011	March 31, 2010
Balance of credit-related OTTI at January 1	$14,653	$10,765
Additions for credit-related OTTI not previously recognized	—	1,402
Additional increases for credit-related OTTI previously recognized when there is no intent to sell and no requirement to sell before recovery of amortized cost basis	19	6,112
Decreases for previously recognized credit-related OTTI because there was an intent to sell	—	(4,369)
Reduction for increases in cash flows expected to be collected	(55)	—
Balance of credit-related OTTI at March 31	$14,617	$13,910

The amortized cost and estimated fair value of available-for-sale securities by contractual maturity at March 31, 2011 and December 31, 2010 are shown in the following table. Actual maturities will differ from contractual maturities because the issuers of the securities may have the right to call or prepay obligations with or without call or prepayment penalties.

(in thousands)	March 31, 2011 Amortized Cost	March 31, 2011 Fair Value	December 31, 2010 Amortized Cost	December 31, 2010 Fair Value
Contractual Maturity				
Due in one year or less	$—	$—	$2,500	$2,421
Due after one year through five years	11,700	11,745	16,470	16,573
Due after five years through ten years	33,911	33,499	19,293	19,492
Due after ten years	94,609	69,835	117,333	90,926
	140,220	115,079	155,596	129,412
Residential mortgage-backed agencies	108,532	110,003	98,109	99,613
Collateralized mortgage obligations	729	647	763	662
	$249,481	$225,729	$254,468	$229,687

Note F - Restricted Investment in Bank Stock

Restricted stock, which represents required investments in the common stock of the FHLB of Atlanta, Atlantic Central Bankers Bank ("ACBB") and CBB, is carried at cost and is considered a long-term investment.

Management evaluates the restricted stock for impairment in accordance with ASC Industry Topic 942, Financial Services – Depository and Lending, (ASC Section 942-325-35). Management's evaluation of potential impairment is based on management's assessment of the ultimate recoverability of the cost of the restricted stock rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability is influenced by criteria such as (a) the significance of the decline in net assets of the issuing bank as compared to the capital stock amount for that bank and the length of time this situation has persisted, (b) commitments by the issuing bank to make payments required by law or regulation and the level of such payments in relation to the operating performance of that bank, and (c) the impact of legislative and regulatory changes on institutions and, accordingly, on the customer base of the issuing bank.

The Corporation recognizes dividends on a cash basis. For the three months ended March 31, 2011, dividends of $25,040 were recognized in earnings. For the comparable period of 2010, dividends of $9,400 were recognized in earnings.

Management has evaluated the restricted stock for impairment and believes that no impairment charge is necessary as of March 31, 2011.

Note G – Loans and Related Allowance for Loan Losses

The following table summarizes the primary segments of the loan portfolio as of March 31, 2011 and December 31, 2010:

(in thousands)	Commercial Real Estate	Acquisition and Development	Commercial and Industrial	Residential Mortgage	Consumer	Total
March 31, 2011						
Total loans	$ 327,380	$ 155,476	$ 72,362	$ 353,617	$ 27,205	$ 936,040
Individually evaluated for impairment	24,204	31,072	13,771	7,991	39	77,077
	303,176	124,404	58,591	345,626	27,166	858,963

Collectively evaluated for impairment						
December 31, 2010						
Total loans	$ 348,584	$ 156,892	$ 69,992	$ 356,742	$ 77,543	$ 1,009,753
Individually evaluated for impairment	16,270	31,196	5,131	9,854	152	62,603
Collectively evaluated for impairment	332,314	125,696	64,861	346,888	77,391	947,150

The segments of the Bank's loan portfolio are disaggregated to a level that allows management to monitor risk and performance. The commercial real estate ("CRE") loan segment is further disaggregated into two classes. Non-owner occupied CRE loans, which include loans secured by non-owner occupied nonfarm nonresidential properties, generally have a greater risk profile than all other CRE loans, which include loans secured by farmland, multifamily structures and owner-occupied commercial structures. The acquisition and development ("A&D") loan segment is further disaggregated into two classes. One-to-four family residential construction loans are generally made to individuals for the acquisition of and/or construction on a lot or lots on which a residential dwelling is to be built. All other A&D loans are generally made to developers or investors for the purpose of acquiring, developing and constructing residential or commercial structures. These loans have a higher risk profile because the ultimate buyer, once development is completed, is generally not known at the time of the A&D loan. The commercial and industrial ("C&I") loan segment consists of loans made for the purpose of financing the activities of commercial customers. The residential mortgage loan segment is further disaggregated into two classes: amortizing term loans, which are primarily first liens, and home equity lines of credit, which are generally second liens. The consumer loan segment consists primarily of installment loans (direct and indirect) and overdraft lines of credit connected with customer deposit accounts.

Management evaluates individual loans in all of the commercial segments for possible impairment if the loan is greater than $500,000 or is part of a relationship that is greater than $750,000, and if the loan either is in nonaccrual status, or is risk rated Substandard and is greater than 60 days past due. Loans are considered to be impaired when, based on current information and events, it is probable that the Corporation will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in evaluating impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. The Corporation does not separately evaluate individual consumer and residential mortgage loans for impairment, unless such loans are part of larger relationship that is impaired, or are classified as a troubled debt restructuring agreement.

Once the determination has been made that a loan is impaired, the determination of whether a specific allocation of the allowance is necessary is measured by comparing the recorded investment in the loan to the fair value of the loan using one of three methods: (a) the present value of expected future cash flows discounted at the loan's effective interest rate; (b) the loan's observable market price; or (c) the fair value of the collateral less selling costs. The method is selected on a loan-by loan basis, with management primarily utilizing the fair value of collateral method. The evaluation of the need and amount of a specific allocation of the allowance and whether a loan can be removed from impairment status is made on a quarterly basis. The Corporation's policy for recognizing interest income on impaired loans does not differ from its overall policy for interest recognition.

The following table presents impaired loans by class, segregated by those for which a specific allowance was required and those for which a specific allowance was not necessary as of March 31, 2011 and December 31, 2010:

	Impaired Loans with Specific Allowance		Impaired Loans with No Specific Allowance	Total Impaired Loans	
(in thousands)	Recorded Investment	Related Allowance	Recorded Investment	Recorded Investment	Unpaid Principal Balance
March 31, 2011					

Commercial real estate					
Non owner-occupied	$13,568	$2,636	$3,950	$17,518	$17,518
All other CRE	—	—	6,686	6,686	6,711
Acquisition and development					
1-4 family residential construction	2,915	889	139	3,054	3,054
All other A&D	7,492	1,283	20,526	28,018	30,679
Commercial and industrial	9,400	940	4,371	13,771	15,180
Residential mortgage					
Residential mortgage - term	576	18	6,634	7,210	7,387
Residential mortgage – home equity	—	—	781	781	781
Consumer	—	—	39	39	39
Total impaired loans	$33,951	$5,766	$43,126	$77,077	$81,349
December 31, 2010					
Commercial real estate					
Non owner-occupied	$8,183	$2,768	$4,635	$12,818	$12,818
All other CRE	713	80	2,740	3,453	3,478
Acquisition and development					
1-4 family residential construction	2,823	334	622	3,445	3,491
All other A&D	7,269	1,141	20,482	27,751	31,284
Commercial and industrial	—	—	5,131	5,131	6,540
Residential mortgage					
Residential mortgage - term	725	43	8,606	9,331	10,086
Residential mortgage – home equity	—	—	522	522	522
Consumer	—	—	152	152	153
Total impaired loans	$19,713	$4,366	$42,890	$62,603	$68,372

The following table presents the average recorded investment in impaired loans by class and related interest income recognized for the periods indicated:

(in thousands)	Three months ended March 31, 2011 Average investment	Interest income recognized on an accrual basis	Interest income recognized on a cash basis	Three months ended March 31, 2010 Average investment	Interest income recognized on an accrual basis	Interest income recognized on a cash basis
Commercial real estate						
Non owner-occupied	$15,168	$19	$—	$10,912	$117	$—
All other CRE	5,070	69	—	20,518	277	—
Acquisition and development						
1-4 family residential construction	3,250	27	—	364	—	—
All other A&D	27,885	145	—	68,721	398	—
Commercial and industrial	9,451	38	—	11,775	143	—
Residential mortgage						
Residential mortgage - term	8,271	43	—	8,892	119	—
Residential mortgage – home equity	652	4	—	3,892	34	—
Consumer	99	—	—	—	—	—
Total	$69,846	$345	$—	$125,074	$1,088	$—

Management uses a 10 point internal risk rating system to monitor the credit quality of the overall loan portfolio. The first six categories are considered not criticized, and are aggregated as "Pass" rated. The criticized rating categories utilized by management generally follow bank regulatory definitions. The Special Mention category includes assets that are currently protected but are potentially weak, resulting in an undue and unwarranted credit risk, but not to the point of justifying a Substandard classification. Loans in the Substandard category have well-defined weaknesses that jeopardize the liquidation of the debt, and have a distinct possibility that some loss will be sustained if the weaknesses are not corrected. All loans greater than 90 days past due are considered Substandard. The portion of any loan that represents a specific allocation of the allowance for loan losses is placed in the Doubtful category. Any portion of a loan that has been charged off is placed in the Loss category.

To help ensure that risk ratings are accurate and reflect the present and future capacity of borrowers to repay a loan as agreed, the Bank has a structured loan rating process with several layers of internal and external oversight. Generally, consumer and residential mortgage loans are included in the Pass categories unless a specific action, such as bankruptcy, repossession, or death occurs to raise awareness of a possible credit event. The Bank's Commercial Loan Officers are responsible for the timely and accurate risk rating of the loans in their portfolios at origination and on an ongoing basis. The Credit Quality Department performs an annual review of all commercial relationships $500,000 or greater. Confirmation of the appropriate risk grade is included in the review on an ongoing basis. The Bank has an experienced Loan Review Department that continually reviews and assesses loans within the portfolio. The Bank engages an external consultant to conduct loan reviews on at least an annual basis. Generally, the external consultant reviews commercial relationships greater than $750,000 and/or criticized relationships greater than $500,000. Detailed reviews, including plans for resolution, are performed on loans classified as Substandard on a quarterly basis. Loans in the Special Mention and Substandard categories that are collectively evaluated for impairment are given separate consideration in the determination of the allowance.

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The following table presents the classes of the loan portfolio summarized by the aggregate Pass and the criticized categories of Special Mention, Substandard and Doubtful within the internal risk rating system as of March 31, 2011 and December 31, 2010:

(in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
March 31, 2011					
Commercial real estate					
Non owner-occupied	$118,892	$9,266	$28,080	$2,636	$158,874
All other CRE	110,506	8,168	49,832	—	168,506
Acquisition and development					
1-4 family residential construction	8,080	—	5,977	889	14,946
All other A&D	85,612	3,765	49,870	1,283	140,530
Commercial and industrial	51,603	2,125	17,694	940	72,362
Residential mortgage					
Residential mortgage - term	253,670	2,532	17,957	18	274,177
Residential mortgage – home equity	75,398	—	4,042	—	79,440
Consumer	26,563	36	606	—	27,205
Total	$730,324	$25,892	$174,058	$5,766	$936,040
December 31, 2010					
Commercial real estate					
Non owner-occupied	$121,144	$9,541	$33,914	$2,768	$167,367
All other CRE	123,115	8,995	49,027	80	181,217
Acquisition and development					
1-4 family residential construction	7,038	—	6,876	334	14,248
All other A&D	86,352	4,664	50,487	1,141	142,644
Commercial and industrial	46,760	2,933	20,299	—	69,992
Residential mortgage					
Residential mortgage - term	255,916	2,634	18,576	43	277,169
Residential mortgage – home equity	76,828	—	2,745	—	79,573
Consumer	76,736	23	784	—	77,543
Total	$793,889	$28,790	$182,708	$4,366	$1,009,753

Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by the length of time a recorded payment is past due. The following table presents the classes of the loan portfolio summarized by the aging categories of performing loans and non-accrual loans as of March 31, 2011 and December 31, 2010:

(in thousands)	Current	30-59 Days Past Due	60-89 Days Past Due	90 Days+ Past Due	Total Past Due and still accruing	Non-Accrual	Total Loans
March 31, 2011							
Commercial real estate							
Non owner-occupied	$ 140,853	$ 1,032	$ 450	$ —	$ 1,482	$ 16,539	$ 158,874
All other CRE	166,875	941	—	—	941	690	168,506
Acquisition and development							
1-4 family residential construction	14,724	83	—	—	83	139	14,946
All other A&D	115,703	8,609	—	—	8,609	16,218	140,530
Commercial and industrial	71,335	195	263	—	458	569	72,362
Residential mortgage							
Residential mortgage - term	257,998	10,566	1,407	324	12,297	3,882	274,177
Residential mortgage – home equity	78,483	66	359	—	425	532	79,440
Consumer	25,313	1,300	528	26	1,854	38	27,205
Total	$ 871,284	$ 22,792	$ 3,007	$ 350	$ 26,149	$ 38,607	$ 936,040
December 31, 2010							
Commercial real estate							
Non owner-occupied	$ 146,470	$ 892	$ 8,801	$ —	$ 9,693	$ 11,204	$ 167,367
All other CRE	179,661	581	286	—	867	689	181,217
Acquisition and development							
1-4 family residential construction	13,626	—	—	—	—	622	14,248
All other A&D	124,731	1,950	188	128	2,266	15,647	142,644
Commercial and industrial	67,688	883	22	44	949	1,355	69,992
Residential mortgage							
Residential mortgage - term	253,225	12,168	4,455	2,359	18,982	4,962	277,169
Residential mortgage – home equity	78,533	559	129	78	766	274	79,573
Consumer	74,392	2,116	700	183	2,999	152	77,543
Total	$ 938,326	$ 19,149	$ 14,581				