FIRST NATIONAL COMMUNITY BANCORP INC
Form 10-Q/A
December 02, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q/A

Amendment No. 1

(Mark One)

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

For the quarterly period ended June 30, 2010

OR

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 No. 000-53869

FIRST NATIONAL COMMUNITY BANCORP, INC.

(Exact Name of Registrant as Specified in Its Charter)

Pennsylvania (State or Other Jurisdiction of Incorporation or Organization)	**23-2900790** (I.R.S. Employer Identification No.)
102 E. Drinker St., Dunmore, PA (Address of Principal Executive Offices)	**18512** (Zip Code)

Registrant s telephone number, including area code **(570) 346-7667**

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

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

Large Accelerated Filer o	Accelerated Filer x
Non-Accelerated Filer o	Smaller reporting company o

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of the latest practicable date:

Common Stock, $1.25 par value	**16,441,319 shares**
(Title of Class)	(Outstanding at November 29, 2011)

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EXPLANATORY NOTE

This Amendment No. 1 (Amendment) on Form 10-Q/A to the Quarterly Report on Form 10-Q of First National Community Bancorp, Inc. (the Company) for the quarterly period ended June 30, 2010, filed with the Securities and Exchange Commission (SEC) on August 9, 2010 (the Original Report) is being filed to revise and restate the Company s consolidated financial statements for the three and six month period ended June 30, 2010 that were filed with the Original Report to correct certain information and to address the impact of such changes on other disclosures included in the Original Report. The Company has previously advised that the financial statements for June 30, 2010 included in the Original Report should no longer be relied upon.

In particular, this Amendment:

- amends and restates in their entirety the consolidated financial statements of the Company, and the notes thereto, included in Item 1 hereof, to appropriately reflect (i) the accounting for and timing of charges related to other than temporary impairment (OTTI) of the collateralized debt obligations in the Company s securities investment portfolio, (ii) the determination of the Company s provision and allowance for loan and lease losses, (iii) the provision for off-balance sheet commitments, (iv) the accounting for deferred loan fees and costs, (v) the related effect on the Company s deferred tax assets and valuation allowance and (vi) other miscellaneous accounting issues;

- amends and revises Management s Discussion and Analysis of Financial Condition and Results of Operations to reflect the restated consolidated financial statements;

- revises the disclosures regarding, and management s assessment of, the Company s disclosure controls and procedures and internal control over financial reporting to reflect current management s determination that material weaknesses in such controls existed at June 30, 2010;

- provides additional disclosure regarding non-performing assets, including those loans extended to insiders or affiliates thereof;

- provides information relating to the Company s and Bank s regulatory orders entered into after the date of the Original Report to provide context for the amendments included in this document; and

- revises and corrects disclosure in response to comments from the SEC.

Other than as noted above, the Company is not required to and has not updated any forward-looking statements previously included in the Original Report. The Company has made no attempt in this Amendment to modify or update the disclosures presented in the Original Report other than as noted above. Other than as noted above or reflected in this Explanatory Note, this Amendment does not reflect events occurring after the filing of the Original Report except to the extent information learned after the Original Report was filed relates to periods prior to June 30, 2010. This Amendment is being filed in conjunction with amendments to the Company s annual report on Form 10-K/A for the annual period ended December 31, 2009 and to its quarterly report on Form 10-Q/A for the quarterly period ended March 31, 2010. The Company plans to file shortly its annual report on Form 10-K for the year ended December 31, 2010 and its quarterly reports on Form 10-Q for the quarterly periods ended September 30, 2010, March 31, 2010, June 30, 2011 and September 30, 2011. This Amendment should be read in conjunction with all such filings and all such filings should be read in their entirety.

As indicated above, the Company has restated its financial statements for the quarter ended June 30, 2010. The Company has also restated its financial statements for the year ended December 31, 2009 and for the quarter ended March 31, 2010. Unless otherwise indicated, the discussion in this Amendment gives effect to these restatements of the Company s financial statements.

In the first half of 2011, the Company received document subpoenas from the SEC. The information requested generally relates to disclosure and financial reporting by the Company and the restatement of the Company s financial statements for the year ended December 31, 2009, and the quarters ended March 31, 2010 and June 30, 2010. The Company is cooperating with the SEC in this matter.

Readers should review the risk factors described in other documents that the Company files or furnishes, from time to time, with the SEC, including Annual Reports to Shareholders, Annual Reports filed on Form 10-K, Form 10-Q and other current reports filed or furnished on Form 8-K and any amendments to such reports.

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PART I Financial Information

Item 1 Financial Statements

FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS (unaudited)

(in thousands, except for share data)	June 30, 2010 (as restated) (Unaudited)	December 31, 2009 (as restated)
Assets		
Cash and cash equivalents:		
Cash and due from banks	$ 21,795	$ 24,189
Federal funds sold	60,925	62,175
Total cash and cash equivalents	82,720	86,364
Securities:		
Available-for-sale, at fair value	253,006	252,946
Held-to-maturity, at cost (fair value $1,869 and $1,788)	1,946	1,899
Loans held for sale	119	
Loans, net of allowance for loan and lease losses of $27,378 and $22,458	862,327	917,516
Bank premises and equipment	20,619	20,667
Accrued interest receivable	3,907	4,245
Intangible assets	1,731	1,794
Other assets	79,830	80,901
Total Assets	$ 1,306,205	$ 1,366,332
Liabilities		
Deposits:		
Demand	$ 75,745	$ 85,370
Interest-bearing demand	340,516	352,631
Savings	95,682	86,455
Time ($100,000 and over)	227,300	238,839
Other time	282,539	308,313
Total deposits	1,021,782	1,071,608
FHLB advances	175,576	183,830
Subordinated debentures	25,000	23,100
Junior subordinated debentures	10,310	10,310
Other debt	206	227
Accrued interest payable	2,704	3,064
Other liabilities	10,385	11,109
Total liabilities	1,245,963	1,303,248
Shareholders Equity		
Common shares ($1.25 par)		
Authorized: 50,000,000 shares as of June 30, 2010 and December 31, 2009		
Issued and outstanding: 16,315,605 shares at June 30, 2010 and 16,289,970 shares at December 31, 2009	20,395	20,362
Additional paid-in capital	61,271	61,190
Retained earnings	(12,182)	(6,162)
Accumulated other comprehensive loss	(9,242)	(12,306)

Total shareholders equity		60,242		63,084
Total Liabilities and Shareholders Equity	$	1,306,205	$	1,366,332

The accompanying notes to consolidated financial statements are an integral part of these statements.

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FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)

	Three Months ended June 30, 2010 (as restated)	Three Months ended June 30, 2009	Six Months ended June 30, 2010 (as restated)	Six Months ended June 30, 2009
	(dollars in thousands, except share data)			
Interest income				
Interest and fees on loans	$ 11,486	$ 13,039	$ 23,618	26,397
Interest and dividends on securities:				
U.S. Treasury and government agencies	1,305	1,614	2,797	3,419
State and political subdivisions	1,391	1,253	2,791	2,473
Other securities	176	423	275	890
Total interest and dividends on securities	2,872	3,290	5,863	6,782
Interest on federal funds sold	31	13	67	13
Total interest income	14,389	16,342	29,548	33,192
Interest expense				
Interest-bearing demand	863	814	1,895	1,539
Savings	128	142	257	262
Time ($100,000 and over)	881	1,211	1,812	2,235
Other time	1,794	2,155	3,734	4,431
Interest on FHLB Advances	1,347	1,762	2,798	3,661
Interest on subordinated debentures	569		1,108	
Interest on junior subordinated debentures	51	75	101	166
Interest on other debt		4		52
Total interest expense	5,633	6,163	11,705	12,346
Net interest income before provision for loan and lease losses	8,756	10,179	17,843	20,846
Provision for loan and lease losses	4,574	7,250	9,682	9,710
Net interest income after provision for loan and lease losses	4,182	2,929	8,161	11,136
Other income (loss)				
Service charges	647	722	1,296	1,410
Net gain (loss) on the sale of securities	(21)	298	1,175	825
Gross other-than-temporary impairment (OTTI) losses	(10,265)	(11,722)	(11,173)	(11,722)
Portion of loss recognized in OCI (before taxes)	7,709	11,340	8,271	11,340
Net impairment losses recognized in earnings	(2,556)	(382)	(2,902)	(382)
Net gain on the sale of loans	155	462	403	1,007
Net loss on the sale of other real estate	48		48	
Net gain on the sale of other assets	28		28	
Other	827	584	1,661	1,247
Total other income	(872)	1,684	1,709	4,107
Other expenses				
Salaries and employee benefits	3,229	2,984	6,337	6,316
Occupancy expense	517	544	1,164	1,159
Equipment expense	454	467	886	922
Advertising expense	214	240	333	480
Data processing expense	495	430	982	866
FDIC assessment	502	1,192	971	1,432
Bank shares tax	255	215	510	432
Expenses of other real estate	1,224	42	1,359	42
Legal expense	133	123	281	170

Other operating expenses		1,482		1,106		3,067		2,201
Total other expenses		8,505		7,343		15,890		14,020
Income (loss) before income taxes		(5,195)		(2,730)		(6,020)		1,223
Provision (credit) for income taxes				(514)				201
Net income (loss)		(5,195)		(2,216)		(6,020)		1,022
Earnings (Loss) Per Share								
Basic	$	(0.32)	$	(0.14)	$	(0.37)	$	0.06
Diluted	$	(0.32)	$	(0.14)	$	(0.37)	$	0.06
Cash Dividends Declared per Common Share	$		$	0.02	$		$	0.13
Weighted average number of outstanding shares								
Basic		16,306,670		16,158,640		16,300,515		16,111,808
Diluted		16,306,670		16,158,640		16,300,515		16,155,745

The accompanying notes to consolidated financial statements are an integral part of these statements.

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FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

For The Six Months Ended June 30, (in thousands)	2010 (as restated)	2009
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS:		
CASH FLOWS FROM OPERATING ACTIVITIES:		
Interest received	$ 28,483	$ 32,195
Fees and commissions received	2,955	2,719
Interest paid	(12,065)	(13,414)
Cash paid to suppliers and employees	(14,027)	(16,000)
Income taxes (paid)/refunded	2,866	(1,861)
NET CASH PROVIDED BY OPERATING ACTIVITIES	8,212	3,639
CASH FLOWS FROM INVESTING ACTIVITIES:		
Securities available for sale:		
Proceeds from sales	25,548	12,378
Proceeds from calls, paydowns and maturities	17,502	22,531
Purchases	(39,105)	(11,371)
Net (decrease)/increase in loans to customers	40,916	(1,754)
Capital expenditures	(628)	(434)
NET CASH PROVIDED BY INVESTING ACTIVITIES	44,233	21,350
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net decrease in demand deposits, money market demand, NOW accounts and savings accounts	(12,514)	(4,562)
Net decrease in certificates of deposit	(37,313)	46,603
Proceeds from issuance of subordinated debentures	1,900	
Net decrease in borrowed funds	(8,274)	(24,386)
Proceeds from issuance of common shares, net of share issuance costs	112	1,106
Cash dividends paid		(2,087)
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	(56,089)	16,674
NET DECREASE IN CASH AND CASH EQUIVALENTS	(3,644)	41,663
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	86,364	18,171
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 82,720	$ 59,834
RECONCILIATION OF NET INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net income (loss)	$ (6,020)	$ 1,022
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization and accretion, net	(1,402)	(1,921)
Equity in trust	(2)	(3)
Depreciation and amortization	881	907
Provision for loan and lease loss	9,682	9,710
Provision for off balance sheet	30	
Provision/(benefit) for deferred taxes	2,137	(112)
Gain on sale of loan	(402)	(1,007)
Gain on sale of securities	(1,175)	(825)

Loss on sale of other assets		820		
Impairment losses on investment securities		2,902		382
Increase/(decrease) in taxes payable				(1,692)
Decrease in interest receivable		339		924
Increase/(decrease) in interest payable		(360)		(1,068)
Increase in prepaid expenses and other assets		1,310		(2,576)
Decrease in accrued expenses and other liabilities		(528)		(102)
Total adjustments		14,232		2,617
NET CASH PROVIDED BY OPERATING ACTIVITIES	$	8,212	$	3,639

The accompanying notes to consolidated financial statements are an integral part of these statements.

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FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY (unaudited)

	COMPREHENSIVE INCOME (LOSS)	COMMON SHARES SHARES	COMMON SHARES AMOUNT	ADD L PAID-IN CAPITAL	RETAINED EARNINGS	ACCUMULATED OTHER COMPREHENSIVE INCOME/(LOSS)	TOTAL
Balances, December 31, 2008		16,047,928	$ 20,060	$ 59,591	$ 40,892	$ (20,201)	$ 100,342
Comprehensive income:							
Net income for the period	$ 1,022				1,022		1,022
Other comprehensive income, net of tax:							
Unrealized loss on securities available for sale, net of deferred tax benefit of $358	(666)						
Reclassification adjustment for gain or loss included in income (tax effect of $155)	288						
Total other comprehensive loss, net of tax	(378)					(378)	(378)
Comprehensive income	$ 644					(378)	644
Share-based compensation - Stock Option Plans				159			159
Issuance of common shares through dividend reinvestment		131,635	164	942			1,106
Cash dividends paid, $0.11 per share					(2,087)		(2,087)
Balances, June 30, 2009		16,179,563	$ 20,224	$ 60,692	$ 39,827	$ (20,579)	$ 100,164
Balances, December 31, 2009 (as restated)		16,289,970	$ 20,362	$ 61,190	$ (6,162)	$ (12,306)	$ 63,084
Comprehensive income:							
Net income for the period	$ (6,020)				(6,020)		(6,020)
Other comprehensive income, net of tax:							
Unrealized gain on securities available for sale net of deferred taxes of $10,886	20,220						
Noncredit related losses on securities not expected to be sold, net of deferred tax benefit of $9,649	(17,920)						
Reclassification adjustment for gain or loss included in income (tax effect of $411)	764						
Total other comprehensive income, net of tax	3,064					3,064	3,064
Comprehensive (Loss)	$ (2,956)					3,064	(2,956)
Proceeds from issuance of Common Shares through dividend reinvestment		25,635	33	81			114
Balances, June 30, 2010 (as restated)		16,315,605	$ 20,395	$ 61,271	$ (12,182)	$ (9,242)	$ 60,242

The accompanying notes to consolidated financial statements are an integral part of these statements.

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FIRST NATIONAL COMMUNITY BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Notes to Consolidated Financial Statements

Note 1. Basis of Presentation

The consolidated financial statements of the Company include the accounts of its bank subsidiary, First National Community Bank and its wholly-owned subsidiaries. All inter-company transactions and balances have been eliminated. The accounting and reporting policies of the Company conform to U.S. Generally Accepted Accounting Principles (GAAP) and general practices within the financial services industry. Certain prior period amounts have been reclassified to conform to the current presentation. In accordance with current accounting guidance, the Company has evaluated subsequent events for potential recognition and/or disclosure in the consolidated financial statements and accompanying notes included thereto through the date the financial statements were filed. In the opinion of management, all adjustments necessary to a fair statement of the results for the quarterly period ended June 30, 2010 have been included.

In preparing the consolidated financial statements, management has made estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated balance sheets and results of operations for the periods indicated. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to change are the allowance for loan and lease losses (ALLL), security valuations, the evaluation of deferred income taxes, and the evaluation of intangibles (which includes core deposits and loan servicing rights) and investment securities for impairment. The current economic environment has increased the degree of uncertainty inherent in these material estimates.

On July 1, 2009, the Accounting Standards Codification (ASC) became the Financial Accounting Standards Board s (the FASB) officially recognized source of authoritative U.S. GAAP applicable to all public and non-public non-governmental entities, superseding all existing FASB, American Institute of Certified Public Accountants (AICPA), Emerging Issues Task Force (EITF) and related literature. Rules and interpretive releases of the SEC under authority of federal securities laws are also sources of authoritative guidance for SEC registrants. All other accounting literature is considered non-authoritative. The issuance of the ASC affects the way companies refer to U.S. GAAP in financial statements and other disclosures. See the New Authoritative Accounting Guidance section below for a description of recent accounting pronouncements including the dates of adoption and the effect on the results of operations and financial condition.

Certain reclassifications have been made to the prior year s consolidated financial statements that conform to the current year s presentation. Such reclassifications had no impact on net income.

These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s December 31, 2009 audited financial statements filed on Form 10-K/A and the Company s March 31, 2010 unaudited financial statements filed on Form 10-Q/A. Additionally, the Company plans to file shortly its annual report on Form 10-K for the year ended December 31, 2010 and its quarterly reports on Form 10-Q for the quarterly periods ended September 30, 2010, March 31, 2011, June 30, 2011 and September 30, 2011. This Amendment should also be read in conjunction with all such filings and all such filings should be read in their entirety.

Note 2. Restatement of Consolidated Financial Statements

The Company concluded that it would revise its financial statements to properly account for its ALLL, the provision for off-balance sheet commitments, OTTI of the Company s securities portfolio, deferred loan fees and costs, goodwill impairment charge and the accounting for the deferred tax asset.

The Company has revised its financial statements from those included in the Original Report as follows:

- Impaired loans, previously reflected as an increase to the specific component of the ALLL, have been charged off and the reserve reduced, resulting in a reduction in the loan balance and an increase to the provision for loan and lease losses. The general reserve component of the ALLL, previously based on one aggregated pool of unimpaired loans, was increased after assigning these loans to one of the three pools of Pass, Special Mention or Accruing and Substandard and applying historical loss factors and varied qualitative factor basis point allocations based on the risk profile in each pool to determine the appropriate reserve related to those loans. The general reserve component of the ALLL also increased based on higher historical loss experience resulting from the increased loan charge offs for impaired loans.

- The reserve for off-balance sheet commitments was previously calculated using all commitments and assumed that these commitments would be fully funded. This methodology was revised to provide a reserve on letters of credit and construction commitments. In addition, individual analyses were performed on the aforementioned commitments to borrowers considered to be impaired. Based on these changes, the reserve for off-balance sheet commitments was reduced.

- OTTI with respect to our PreTSLs, previously calculated assuming that 50% of issuers who deferred would recover within two years and in reliance on one expected default rate for all issuers and on fair market value data obtained from two outside service providers, including a third party that had sold the Company the PreTSLs included in the securities portfolio, was recalculated using cash flow models assuming specific deferred issuers of securities default immediately, using default rates specific to each bank issuer based on an analysis of its financial trends, and employing certain assumptions in determining the fair value of the securities. The change in methodology resulted in an additional impairment charge through earnings for the six months ending June 30, 2010.

- The Company also reduced OTTI by $4.9 million on PreTSL and PLCMO securities, the issuers of which defaulted or deferred payments between January 1, 2010 and June 30, 2010, after the Company reviewed its subsequent events analysis and determined that these events reflected issuer credit impairments that existed as of the fourth quarter of 2009. As such, those charges were reflected in the restated financial statements for the year ended December 31, 2009 in the Amended 2009 For 10-K.

- Additional loan fees and costs were capitalized and amortized after the Company determined that it had not capitalized a sufficient portion of loan fees and costs and had not done so consistently by loan type.

- In response to the significant loss reported by the Company in 2009 and the reduction in the market capitalization of the Company s common shares, the Company s goodwill was evaluated for impairment as of December 31, 2009 and, as a result of the analysis, $8.1 million of goodwill that arose in connection with the Company s acquisition of its Honesdale, PA branch was charged off as of December 31, 2009.

- Recorded adjustments to the income tax benefit and the deferred tax asset and related reserve to reflect the changes to the financial statements.

The following tables set forth the consolidated restated financial statements for the quarterly period ended June 30, 2010 previously filed in its Original Report.

The following is a summary of the adjustments to the Company s previously filed consolidated balance sheets as of June 30, 2010:

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FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS (unaudited)

(in thousands)	June 30, 2010 As Reported	Adjustments Increase (Decrease)	Reclassifications Increase (Decrease)	June 30, 2010 As Restated
Assets				
Cash and cash equivalents:				
Cash and due from banks	$ 21,795			$ 21,795
Federal funds sold	60,925			60,925
Total cash and cash equivalents	82,720			82,720
Securities:				
Available-for-sale, at fair value (b) (c) (h)	260,266	$ (7,260)		253,006
Held-to-maturity, at cost (fair value $1,869 on June 30, 2010 and $1,788 on December 31, 2009) (q)	1,945	1		1,946
Federal Reserve Bank and FHLB Stock, at cost (i)	12,115		$ (12,115)	
Loans held for sale (r)		119		119
Loans, net of allowance for loan and lease losses of $27,378 and $22,458 (d) (e) (g) (f)	874,103	(11,776)		862,327
Accrued interest receivable (c) (n)		148	3,759	3,907
Bank premises and equipment (q)	20,620	(1)		20,619
Intangible assets (k)	9,865	(8,134)		1,731
Other assets (i) (j) (n)	77,904	(6,430)	8,356	79,830
Total Assets	$ 1,339,538	$ (33,333)	$	$ 1,306,205
Liabilities				
Deposits:				
Demand (q)	$ 75,743	$ 2		$ 75,745
Interest-bearing demand (q)	340,515	1		340,516
Savings	95,682			95,682
Time ($100,000 and over) (q)	227,302	(2)		227,300
Other time (q)	282,537	2		282,539
Total deposits	1,021,779	3		1,021,782
Borrowed funds (l)	186,093		(186,093)	
FHLB advances (l)			175,576	175,576
Subordinated debentures	25,000			25,000
Junior subordinated debentures (l)			10,310	10,310
Other debt (l) (q)		(1)	207	206
Accrued interest payable (o)			2,704	2,704
Other liabilities (o) (m) (a)	13,175	(86)	(2,704)	10,385
Total Liabilities	1,246,047	(84)		1,245,963
Shareholders Equity				
Common stock, ($1.25 par)				
Authorized 50,000,000 shares as of June 30, 2010 Issued and outstanding 16,315,605 shares at June 30, 2010 and 16,289,970 shares at December 31, 2009	20,395			20,395
Additional paid-in capital (q)	61,270	1		61,271
Retained earnings (p)	27,063	(39,245)		(12,182)
Accumulated other comprehensive loss (h)	(15,237)	5,995		(9,242)
Total Shareholders Equity	93,491	(33,249)		60,242
Total Liabilities and Shareholders Equity	$ 1,339,538	$ (33,333)	$	$ 1,306,205

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(a) Change in reserve for off-balance sheet commitments after change in methodology.

(b) Additional OTTI recorded on available-for-sale securities.

(c) Reversal of interest capitalized for payments in-kind.

(d) Allowance for impaired loan and lease losses recorded after change in methodology.

(e) Additional charge-offs recorded on loans.

(f) To record loan fees and costs in accordance with ASC 310 *Receivables*.

(g) Amortization of loan fees and costs in accordance with ASC 310 *Receivables*.

(h) Reversal of Other Comprehensive Income for those securities where additional OTTI was recognized.

(i) Reclassification of FHLB and FRB stock from Securities to Other Assets.

(j) Record benefit for income taxes.

(k) Adjust for the write-down of goodwill recorded in the restatement of 2009 results.

(l) Reclassification of FHLB advances, junior subordinated debentures and other debt from borrowed funds.

(m) Adjustment to accrued expenses.

(n) Reclassification of accrued interest receivable from other assets.

(o) Reclassification of accrued interest payable from other liabilities.

(p) Reduction in retained earnings as a result of the net loss in the restated 2009 results as well as various adjustment entries booked as a result of the prior year and current quarter restatements.

(q) Adjustment for rounding.

(r) Reclassification of loans held for sale from other assets to properly present loans held for sale.

The following is a summary of the adjustments to our previously issued consolidated statements of operations for the three and six months ended June 30, 2010:

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FIRST NATIONAL COMMUNITY BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)

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	June 30, 2010 As Reported	Three months Ended Adjustments Increase/(Decrease)	Reclassifications Increase/(Decrease)	June 30, 2010 (As Restated)
		(dollars in thousands, except share data)		
Interest Income				
Interest and fees on loans (g) (h)	$ 11,542	$ (56)		$ 11,486
Interest and dividends on securities:				
US Treasury and government agencies	1,305			1,305
State and political subdivisions	1,391			1,391
Other securities (p)	180	(4)		176
Total interest and dividends on securities	2,876	(4)		2,872
Interest on federal funds sold	31			31
Total interest income	14,449	(60)		14,389
Interest Expense				
Interest bearing demand	863			863
Savings	128			128
Time ($100,000 and over)	881			881
Other time	1,794			1,794
Total deposits	3,666			3,666
Borrowed funds interest expense (l)	1,400		(1,400)	
Interest on FHLB advances (l)			1,347	1,347
Interest on subordinated debentures (e)	568		1	569
Interest on junior subordinated debentures (l)			51	51
Interest on other debt (l)				
Total interest expense	5,634		(1)	5,633
Net interest income before provision for loan and lease losses	8,815	(60)	1	8,756
Provision for loan and lease losses (d)	4,960	(386)		4,574
Net interest income (loss) after provision for loan and lease losses	3,855	326	1	4,182
Other income				
Service charges (e)	646	1		647
Net gain on the sale of securities	(21)			(21)
Gross other-than-temporary impairment (OTTI) losses (b)	(3,611)	(6,654)		(10,265)
Portion of loss recognized in OCI (before taxes) (b)	2,924	4,785		7,709
Net impairment losses recognized in earnings (b)	(687)	(1,869)		(2,556)
Net gain on the sale of loans (c) (q)	159	24	(28)	155
Net gain on the sale of other real estate (r)	(848)		896	48
Net gain on the sale of other assets (q)			28	28
Other (n) (f)	655	47	125	827
Total other income	(96)	(1,797)	1,021	(872)
Other expenses				
Salaries and employee benefits (f) (g)	3,283	(179)	125	3,229
Occupancy expense (i) (m)	1,013	(42)	(454)	517
Equipment expense (i)			454	454
Advertising expense (m)	225	(11)		214
Data processing expense (e)	496	(1)		495
FDIC assessment	502			502
Bank shares tax	255			255
Expense of other real estate owned (r) (m)	343	(15)	896	1,224
Legal expenses (k) (m)		(40)	173	133

Provision for off-balance sheet commitments (a)	(322)	322		
Other operating expenses (n) (o) (e) (k)	1,654	1	(173)	1,482
Total other expenses	7,449	35	1,021	8,505
Income (loss) before income taxes	(3,690)	(1,506)		(5,195)
Provision (credit) for income taxes (j)	(1,941)	1,941		
Net (loss)	$ (1,749)	$ (3,447)	$	$ (5,195)
LOSS PER SHARE:				
Basic	$ (0.11)	$ (0.21)		$ (0.32)
Diluted	$ (0.11)	$ (0.21)		$ (0.32)
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING:				
Basic	16,306,670			16,306,670
Diluted	16,306,670			16,306,670

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	Six Months Ended			
	June 30, 2010 As Reported	Adjustments Increase/(Decrease)	Reclassifications Increase/(Decrease)	June 30, 2010 (As Restated)
	(dollars in thousands, except share data)			
Interest Income				
Interest and fees on loans (g) (h)	$ 23,730	$ (112)		$ 23,618
Interest and dividends on securities:				
US Treasury and government agencies	2,797			2,797
State and political subdivisions	2,791			2,791
Other securities (p)	361	(86)		275
Total interest and dividends on securities	5,949	(86)		5,863
Interest on federal funds sold	67			67
Total interest income	29,746	(198)		29,548
Interest Expense				
Interest bearing demand	1,895			1,895
Savings	257			257
Time ($100,000 and over)	1,812			1,812
Other time	3,734			3,734
Total deposits	7,698			7,698
Borrowed funds interest expense (l)	2,901	(1)	(2,900)	
Interest on FHLB advances (l)			2,798	2,798
Interest on subordinated debentures (e)	1,107		1	1,108
Interest on junior subordinated debentures (l)			101	101
Interest on other debt (l)				
Total interest expense	11,706	(1)		11,705
Net interest income before provision for loan and lease losses	18,040	(197)		17,843
Provision for loan and lease losses (d)	7,762	1,920		9,682
Net interest income (loss) after provision for loan and lease losses	10,278	(2,117)		8,161
Other income				
Service charges (e)	1,296			1,296
Net gain on the sale of securities	1,175			1,175
Gross other-than-temporary impairment (OTTI) losses (b)	(28,504)	12,889		(15,615)
Portion of loss recognized in OCI (before taxes) (b)	26,902	(14,189)		12,713
Net impairment losses recognized in earnings (b)	(1,602)	(1,300)		(2,902)
Net gain on the sale of loans (c) (q)	432	(1)	(28)	403
Net gain on the sale of other real estate (r)	(848)		896	48
Net gain on the sale of other assets (q)		0	28	28
Other (f) (n)	1,311	95	255	1,661
Total other income	1,764	(1,206)	1,151	1,709
Other expenses				
Salaries and employee benefits (f) (g)	6,403	(322)	256	6,337
Occupancy expense (i) (m)	2,080	(30)	(886)	1,164
Equipment expense (i)			886	886
Advertising expense (m)	450	(117)		333
Data processing expense (e)	983	(1)		982
FDIC assessment	971			971
Bank shares tax	510			510
Expense of other real estate (r) (m)	463		896	1,359
Legal expenses (k) (m)		(15)	296	281
	(1,353)	1,353		

Provision for off-balance sheet commitments (a)								
Other operating expenses (n) (o) (e) (k)		3,324		38		(295)		3,067
Total other expenses		13,831		906		1,153		15,890
Income (loss) before income taxes		(1,789)		(4,229)		(2)		(6,020)
Provision (credit) for income taxes (j)		(1,998)		1,998				
Net income (loss)	$	209	$	(6,227)	$	(2)	$	(6,020)
LOSS PER SHARE:								
Basic	$	0.01	$	(0.38)			$	(0.37)
Diluted	$	0.01	$	(0.38)			$	(0.37)
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING								
Basic		16,300,515						16,300,515
Diluted		16,638,884		(338,369)				16,300,515

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(a) Change in reserve for off-balance sheet commitments after change in methodology.

(b) Adjustment to increase OTTI recorded on available-for-sale securities as a result of change in methodology.

(c) Adjustment related to the gain booked on Loans, held for sale.

(d) Provision for loan and lease losses adjusted after change in methodology.

(e) Adjustment for rounding.

(f) Reclassification of Bank Owned Life Insurance Income from expense to income.

(g) To record loan fees and costs in accordance with ASC 310 *Receivables*.

(h) Amortization of loan fees and costs in accordance with ASC 310 *Receivables*.

(i) Reclassification of Equipment expense from being included in Occupancy expense.

(j) Reverse income tax benefit.

(k) Reclassification of Legal expense from being included in other operating expenses.

(l) Reclassification of interest on borrowed funds to interest on FHLB advances, interest on junior subordinated debentures, and interest on other debt.

(m) To adjust and reduce expense related to an over accrual.

(n) Reclassification of mortgage servicing rights amortization expense from being netted against loan servicing fee income.

(o) Reclassification of provision for off balance sheet commitments to other operating expenses.

(p) Reversal of accrued interest on Pooled Trust Preferred Securities.

(q) Reclassification of Gain on sale of other assets from gain on sale of loans.

(r) Reclassification of OREO valuation write-downs.

Note 3. New Authoritative Accounting Guidance

On January 1, 2010, the Company adopted the provisions of the Accounting Standards Codification (ASC) Topic 860-10-50, *Transfers and Servicing - Overall-Disclosures* as updated by Accounting Standards Update (ASU) 2009-16, *Accounting for Transfers of Financial Assets*. The standard enhances the reporting for transfers of financial assets, including securitization transactions. It also requires companies to report where they have continuing exposure to the risks related to transferred financial assets and eliminates the concept of a qualifying special-purpose entity. In addition, it changes the requirements for derecognizing financial assets and requires additional disclosures about all continuing involvements with transferred financial assets, including information about gains and losses resulting from transfers during the period. This standard also requires additional year-end and interim disclosures. The standard must be applied to transfers that occurred before and after its effective date. The adoption of ASC Topic 860-10-50 had no impact on the Company s financial statements.

On January 1, 2010, the Company adopted ASC topic 810-10-50, *Consolidation-Overall-Disclosures* as amended by ASU 2009-17, *Consolidation Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities*, to change how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. The determination of whether a company is required to consolidate an entity is based on, among other things, an entity s purpose and design and a company s ability to direct the activities of the entity that most significantly impact the entity s economic performance. This standard also requires additional disclosures about the reporting entity s involvement with variable-interest entities and any significant changes in risk exposure due to that involvement as well as its effect on the entity s financial statements. The standard also requires additional year-end and interim disclosures. In February 2010, ASU 2010-10, *Consolidation: Amendments for Certain Investment Funds* was issued which provides an indefinite deferral of ASC topic 810-10 for certain entities. Entities that meet the criteria for deferral of consolidation guidance are still required to provide disclosures required by the topic. The update also clarifies how a related party s interests in an entity should be considered when evaluating the criteria for determining whether a decision maker or service provider fee represents a variable interest. It clarifies that a quantitative calculation should not be the only basis for evaluating whether a decision maker s or service provider s fee is a variable interest. The adoption of ASC Topic 810-10-50 had no impact on the Company s financial statements.

In January 2010, a clarification ASU 2010-06, *Fair Value and Disclosures, Improving Disclosures about Fair Value Measurements* was issued for ASC topic 820-10-50, *Fair Value Measurements and Disclosures*. The amendments in ASU 2010-06 require companies to provide a separate disclosure for transfers in and out of Levels 1 and 2, including a description of the reasons for the transfer. The amendments also require companies to report activity in Level 3 fair value measurements on a gross basis, including information about purchases, sales, issuances and settlements. The amendments also clarify existing disclosures related to disaggregated reporting, model inputs and valuation techniques. The new disclosures are effective for the first quarter of 2010, except for the gross reporting of Level 3 activity, which is effective beginning the first quarter of 2011. These amendments resulted in additional disclosures in our interim and annual reports. The applicable new disclosures have been included in Note 8.

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Note 4. Regulatory Matters

The Company is subject to various regulatory capital requirements administered by the federal banking agencies. 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 adverse effect on the Company s financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices must be met. 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 Company to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined).

Currently, the Company s and the Bank s actual capital positions and ratios as of June 30, 2010 and December 31, 2009 are presented in the following table:

CAPITAL ANALYSIS

(in thousands)

	June 30, 2010 (as restated)	**December 31, 2009 (as restated)**
Company		
Tier I Capital:		
Total Tier I Capital	$ 78,509	$ 84,365
Tier II Capital:		
Subordinated notes	25,000	23,100
Allowable portion of allowance for loan and lease losses	13,594	14,594
Total Tier II Capital	38,594	37,694
Total Risk-Based Capital	117,103	122,059
Total Risk-Weighted Assets	$ 1,072,189	$ 1,158,157
Bank		
Tier I Capital:		
Total Tier I Capital	$ 100,708	$ 103,453
Tier II Capital:		
Allowable portion of allowance for loan and lease losses	13,589	14,590
Total Tier II Capital	13,589	14,590
Total Risk-Based Capital	114,297	118,043
Total Risk-Weighted Assets	$ 1,071,842	$ 1,157,823

Actual

			For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provision	
As of June 30, 2010: (as restated)	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
Total Capital (to Risk Weighted Assets)						
Company	$ 117,103	10.92%	$ >85,775	>8.00%	N/A	N/A
Bank	$ 114,297	10.66%	$ >85,747	>8.00%	$ >107,184	>10.00%
Tier I Capital (to Risk Weighted Assets)						
Company	$ 78,509	7.32%	$ >42,888	>4.00%	N/A	N/A
Bank	$ 100,708	9.40%	$ >42,874	>4.00%	$ >64,311	>6.00%
Tier I Capital (to Average Assets)						
Company	$ 78,509	5.92%	$ >53,071	>4.00%	N/A	N/A
Bank	$ 100,708	7.59%	$ >53,097	>4.00%	$ >66,373	>5.00%

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	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provision	
As of December 31, 2009 (as restated)	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
Total Capital (to Risk Weighted Assets)						
Company	$ 122,059	10.54%	$ >92,653	>8.00%	N/A	N/A
Bank	$ 118,043	10.20%	$ >92,626	>8.00%	$ >115,782	>10.00%
Tier I Capital (to Risk Weighted Assets)						
Company	$ 84,365	7.28%	$ >46,326	>4.00%	N/A	N/A
Bank	$ 103,453	8.94%	$ 46,313	>4.00%	$ >69,469	>6.00%
Tier I Capital (to Average Assets)						
Company	$ 84,365	5.94%	$ >56,853	>4.00%	N/A	N/A
Bank	$ 103,453	7.28%	$ >56,853	>4.00%	$ >71,067	>5.00%

The Bank is under a Consent Order (the Order) from the Office of the Comptroller of the Currency (OCC) dated September 1, 2010. The material provisions of the Order are as follows:

(i) By October 31, 2010, the Board of Directors of the Bank (the   Board) is required to adopt and implement a three-year strategic plan which must be submitted to the OCC for review and prior determination of no supervisory objection; the strategic plan must establish objectives for the Bank s overall risk profile, earnings performance, growth, balance sheet mix, off-balance sheet activities, liability structure, capital adequacy, reduction in the volume of nonperforming assets, product line development, and market segments that the Bank intends to promote or develop, and is to include strategies to achieve those objectives; if the strategic plan involves the sale or merger of the Bank, it must address the timeline and steps to be followed to provide for a definitive agreement within 90 days after the receipt of a determination of no supervisory objection;

(ii) by October 31, 2010, the Board is required to adopt and implement a three year capital plan, which must be submitted to the OCC for review and prior determination of no supervisory objection;

(iii) by November 30, 2010, the Bank is required to achieve and thereafter maintain a total risk-based capital equal to at least 13% of risk-weighted assets and a tier 1 capital equal to at least 9% of adjusted total assets;

(iv) the Bank may not pay any dividend or capital distribution unless it is in compliance with the higher capital requirements required by the Order, the Capital Plan, applicable legal requirements and, then only after receiving a determination of no supervisory objection from the OCC;

(v) by November 15, 2010, the Committee must review the Board and the Board s committee structure; by November 30, 2010, the Board must prepare or cause to be prepared an assessment of the capabilities of the Bank s executive officers to perform their past and current duties, including those required to respond to the most recent examination report, and to perform annual performance appraisals of each officer;

(vi) by October 31, 2010, the Board must adopt, implement and thereafter ensure compliance with a comprehensive conflict of interest policy applicable to the Bank s and the Company s directors, executive officers, principal shareholders and their affiliates and such person s immediate family members and their related interests, employees, and by November 30, 2010, conduct a review of existing relationships with such persons to identify those, if any, not in compliance with the policy; and review all subsequent proposed transactions with such persons or modifications of transactions;

(vii) by October 31, 2010, the Board must develop, implement and ensure adherence to policies and procedures for Bank Secrecy Act (BSA) compliance; and account opening and monitoring procedures compliance;

(viii) by October 31, 2010, the Board shall ensure the BSA audit function is supported by an adequately staffed department or third party firm; adopt implement and ensure compliance with an independent BSA audit; and assess the capabilities of the BSA officer and supporting staff to perform present and anticipated duties;

(ix) by October 31, 2010, the Board is required to adopt, implement and ensure adherence to a written credit policy, including specified features, to improve the Bank s loan portfolio management;

(x) the Board is required to take certain actions to resolve certain credit and collateral exceptions;

(xi) by October 31, 2010, the Board is required to establish an effective, independent and ongoing loan review system to review, at least quarterly, the Bank s loan and lease portfolios to assure the timely identification and categorization of problem credits; by October 31, 2010, to adopt and adhere to a program for the maintenance of an adequate allowance for loan and lease losses (ALLL), and to review the adequacy of the Bank s ALLL at least quarterly;

(xii) by October 31, 2010, the Board must adopt and the Bank implement and adhere to a program to protect the Bank s interest in criticized assets; and the Bank may only extend additional credit (including renewals) to a borrower whose loans are criticized under specified circumstances;

(xiii) by October 31, 2010, the Board must adopt and ensure adherence to action plans for each piece of other real estate owned;

(xiv) by November 30, 2010, the Board is required to develop, implement and ensure adherence to a policy for effective monitoring and management of concentrations of credit;

(xv) by October 31, 2010, the Board must revise and implement the Bank s other-than-temporary impairment policy;

(xvi) by October 31, 2010, the Board must take action to maintain adequate sources of stable funding and liquidity and a contingency funding plan; by October 31, 2010, the Board is required to adopt, implement and ensure compliance with an independent, internal audit program; and

(xvii) take actions to correct cited violations of law; and adopt procedures to prevent future violations and address compliance management.

Federal Reserve Agreement On November 24, 2010, the Company entered into a written Agreement (the Agreement) with the Federal Reserve Bank of Philadelphia (the Reserve Bank). The Agreement requires the Company to undertake certain actions within designated timeframes, and to operate in compliance with the provisions thereof during its term. The material provisions of the Agreement include the following:

(i) the Company s Board must take appropriate steps to fully utilize the Company s financial and managerial resources to serve as a source of strength to the Bank, including taking steps to ensure that the Bank complies with its Consent Order entered into with the OCC;

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(ii) the Company may not declare or pay any dividends without the prior written approval of the Reserve Bank and the Director of the Division of Banking Supervision and Regulation (the Director) of the FRB;

(iii) the Company may not take dividends or other payments representing a reduction of the Bank s capital without the prior written approval of the Reserve Bank;

(iv) the Company and its nonbank subsidiary may not make any payment of interest, principal or other amounts on the Company s subordinated debentures or trust preferred securities without the prior written approval of the Reserve Bank and the Director;

(v) the Company may not make any payment of interest, principal or other amounts on debt owed to insiders of the Company without the prior written approval of the Reserve Bank and Director;

(vi) the Company and its nonbank subsidiary may not incur, increase or guarantee any debt without the prior written approval of the Reserve Bank;

(vii) the Company may not purchase or redeem any shares of its stock without the prior written approval of the Reserve Bank;

(viii) the Company must submit to the Reserve Bank, by January 23, 2011, an acceptable written plan to maintain sufficient capital at the Company on a consolidated basis. Thereafter, the Company must notify the Reserve Bank within 45 days of the end of any quarter in which the Company s capital ratios fall below the approved capital plan s minimum ratios, and submit an acceptable written plan to increase the Company s capital ratios above the capital plan s minimums;

(ix) the Company must immediately take all actions necessary to ensure that: (1) each regulatory report accurately reflects the Company s condition on the date for which it is filed and all material transactions between the Company and its subsidiaries; (2) each such report is prepared in accordance with its instructions; and (3) all records indicating how the report was prepared are maintained for supervisory review;

(x) the Company must submit to the Reserve Bank, by January 23, 2011, acceptable written procedures to strengthen and maintain internal controls to ensure all required regulatory reports and notices filed with the Board of Governors are accurate and filed in accordance with the instructions for preparation;

(xi) the Company must submit to the Reserve Bank, by January 8, 2011, a cash flow projection for 2011, reflecting the Company s planned sources and uses of cash, and submit a cash flow projection for each subsequent calendar year at least one month prior to the beginning of such year;

(xii) the Company must comply with: (1) the notice provisions of Section 32 of the FDI Act and Subpart H of Regulation Y in appointing any new director or senior executive officer or changing the duties of any senior executive officer; and (2) the restrictions on indemnification and severance payments of Section 18(k) of the FDI Act and Part 359 of the FDIC s regulations; and

(xiii) the Board must submit written progress reports within 30 days of the end of each calendar quarter;

Since entering into the Order and the Agreement, the Company has incurred expenses in an effort to comply with the terms of these agreements. In particular, the Company has incurred expenses in connection with developing and implementing policies and procedures and hiring additional personnel as required by the Order and the Agreement. During 2010 and the first nine months of 2011, the Company incurred approximately $1.4 million and $851 thousand, respectively, of expenses related to entering into and complying with these regulatory agreements, consisting primarily of professional and consulting fees. In addition, the Order and the Agreement place restrictions on the Company s ability to borrow funds and to pay interest and dividends to its security holders. In the future, the Company expects to continue to experience increased costs related to compliance with these regulatory agreements, primarily as a result of increased head count and also expects to face certain restrictions on its operations for as long as it continues to operate under the Order and the Agreement. The Company expects, however, that future compliance expenses will decrease significantly from the 2010 and 2011 levels, because the majority of the expenses incurred to date are related to development and implementation of processes and policies that, once those policies and processes are finalized and implemented, are not expected to recur.

The Order and the Agreement have not and are not expected to have an impact on the Company s ability to attract and maintain deposits or the Company s cost of funds. In order to meet the increased capital requirements imposed under the Order and the Agreement, however, unless the Company is able to raise additional capital, the Company could be limited in the aggregate amount of loans it can have outstanding, which may constrain loan growth. While it is not anticipated that the Order and the Agreement will have an immediate impact on the Company s net interest margin, the overall cost of compliance with the Order and the Agreement will continue to impact profitability at least through the end of 2012.

Note 5. Loans

Major classifications of loans are summarized as follows (in thousands):

	June 30, 2010 (as restated)	December 31, 2009 (as restated)
Residential real estate	$ 140,501	$ 137,520
Commercial real estate	300,517	317,408
Commercial and industrial loans	208,123	220,849
Construction Loans	83,281	98,383
Installment loans	117,308	128,392
Other loans	39,495	37,013
Gross loans	889,225	939,565
Less: Allowance for loan and lease losses	(27,378)	(22,458)
Unearned discount	(261)	(298)
Plus: Loan fees	741	707
Net loans	$ 862,327	$ 917,516

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Changes in the allowance for loan and lease losses were as follows (in thousands):

	Three months ended June 30, 2010 (as restated)	Three months ended June 30, 2009	Six months ended June 30, 2010 (as restated)	Six months ended June 30, 2009
Balance, beginning of period	$ 25,505	$ 11,278	$ 22,458	$ 9,150
Recoveries credited to allowance	43	43	103	87
Provision for loan and lease losses	4,574	7,250	9,682	9,710
Total	30,122	18,571	32,243	18,947
Losses charged to allowance	2,744	8,053	4,865	8,429
Balance, end of period	$ 27,378	$ 10,518	$ 27,378	$ 10,518

Non-performing loans consist of nonaccrual loans and loans past due 90 days or more and still accruing. At June 30, 2010 and December 31, 2009 the loans on nonaccrual totaled $36.5 million and $25.9 million, respectively. The total recorded investment in loans past due ninety days or more and still accruing interest amounted to $0 and $117 thousand at June 30, 2010 and December 31, 2009, respectively. OREO is included in other assets and totaled $15.0 million and $11.2 million at June 30,2010 and December 31, 2009, respectively. Troubled debt restructurings totaling $12.0 million were all performing in accordance with the restructured agreements as of June 30, 2010. The total recorded investment in impaired loans amounted to $48.5 million and $36.7 million at June 30, 2010 and December 31, 2009, respectively.

The additional interest income that would have been earned on nonaccrual and restructured loans outstanding at June 30, 2010 and June 30, 2009 in accordance with their original terms approximated $1.3 million and $1.2 million, respectively. There was no interest income recognized on non-performing loans for cash payments received during the three and six months ended June 30, 2010 and June 30, 2009.

The following schedule reflects various non-performing lending categories as of the dates noted (in thousands):

	June 30, 2010 (as restated)	December 31, 2009 (as restated)
Nonaccrual loans	$ 36,483	$ 25,865
Loans past due 90 days or more and still accruing	0	117
Total Non-Performing Loans	36,483	$ 25,982
Other Real Estate Owned	15,022	$ 11,184
Total Non-Performing Assets	51,505	$ 37,166
Performing TDRs	11,998	$ 10,743
ALLL related to impaired loans	$ 8,688	$ 3,982

	June 30, 2010 (as restated)	December 31, 2009 (as restated)
Loans with no allocated allowance for loan and lease losses	$ 12,759	$ 11,348
Loans with allocated allowance for loan and lease losses	35,722	25,260
Total Balance of loans considered impaired	$ 48,481	$ 36,608

The average balance of impaired loans was $44.2 million and $49.4 million for the six months ended June 30, 2010 and year ended December

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31, 2009, respectively. The Company recorded $396 thousand and $448 thousand of interest income on impaired loans for the six months ended June 30, 2010 and six months ended June 30, 2009, respectively.

The Company attempts to limit its exposure to concentrations of credit risk by diversifying its loan portfolio and closely monitoring any concentrations of credit risk. The commercial real estate and commercial construction portfolios comprise $380.0 million (as restated) or 44.1% of net loans at June 30, 2010. In addition, the Company had commercial real estate and commercial construction loans of $46.3 million or 5.4% of net loans secured by properties outside of Pennsylvania. Geographic concentrations exist because the Company provides a full range of banking services, including commercial, consumer and mortgage loans to individuals and corporate customers in its market areas in Pennsylvania. Management believes underwriting guidelines and ongoing review by loan review mitigates these risks.

The Company has granted loans, letters of credit and lines of credit to certain executive officers and directors of the Company as well as to certain related parties of executive officers and directors. These loans, letters of credit and lines of credit were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated persons and, when made, did not involve more than normal risk of collectability. See note 11 for more information on related party transactions.

Note 6. Other Real Estate Owned

OREO totaled $15.0 million as of June 30, 2010, which is an increase of $3.8 million, from $11.2 million as of December 31, 2009 and is included in other assets. As of June 30, 2010, OREO consisted of sixteen properties as compared to fourteen properties as of December 31, 2009. Nine of the properties held in OREO as of June 30, 2010 totaled $14.3 million and represented approximately 96% of the total.

The following schedule reflects a breakdown of OREO for the periods reviewed.

	June 30, 2010 (as restated)	December 31, 2009
Land/Lots	$ 9,080	$ 5,887
Commercial Real Estate	5,374	4,852
Residential Real Estate	568	445
Total	$ 15,022	$ 11,184

The Company foreclosed on four properties during the six months ended June 30, 2010, two of which comprised substantially all of the $3.8 million in OREO (the other properties comprised $227 thousand of the increase). In connection with the transfer to OREO, the Company charged off $242 thousand of the loan balances against the ALLL to bring the properties down to their carrying value of $5.2 million.

The expenses related to maintaining OREO and the subsequent write down of the values related to declines in value since foreclosure amounted to $1.2 million and $1.5 million for the three and six months ended June 30, 2010, respectively compared to $42 thousand for the same periods in 2009.

Note 7. Securities

Securities have been classified in the consolidated financial statements according to management s intent. The amortized cost, gross unrealized gains or losses and the fair value of the Company s available-for-sale securities at June 30, 2010 and at December 31, 2009 as follows:

Available-for-sale securities (in thousands):

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June 30, 2010 (as restated)	Amortized cost	Gross unrealized holding gains	Gross unrealized holding losses	Fair value
U.S. Treasury securities and obligations of U.S. government agencies	$ 27,988	$ 389	$ 592	$ 27,785
Obligations of state and political subdivisions	120,061	2,536	5,808	116,789
Collateralized mortgage obligations:				
Government sponsored agency	70,348	1,484	169	71,663
Private label	14,872	101	2,196	12,777
Residential mortgage-backed securities	18,972	816		19,788
Pooled Trust Preferred Senior Class	3,855		2,546	1,309
Pooled Trust Preferred Mezzanine Class	9,619		8,136	1,483
Corporate debt securities	500		106	394
Equity securities	1,010	8		1,018
Total securities available for sale	$ 267,225	$ 5,334	$ 19,553	$ 253,006

December 31, 2009 (as restated)	Amortized cost	Gross unrealized holding gains	Gross unrealized holding losses	Fair value
U.S. Treasury securities and obligations of U.S. government agencies	$ 28,734	$ 78	$ 1,723	$ 27,089
Obligations of state and political subdivisions	122,052	2,591	5,973	118,670
Collateralized mortgage obligations:				
Government sponsored agency	52,968	897	370	53,495
Private label	24,154	17	3,112	21,059
Residential mortgage-backed securities	26,152	1,321	31	27,442
Pooled Trust Preferred Senior Class	3,848	0	2,457	1,391
Pooled Trust Preferred Mezzanine Class	12,459	0	10,040	2,419
Corporate debt securities	500	0	144	356
Equity securities	1,010	15	0	1,025
Total securities available for sale	$ 271,877	$ 4,919	$ 23,850	$ 252,946

The amortized cost, gross unrealized gains or losses and the fair value of the Company s securities held to maturity at June 30, 2010 and December 31, 2009 are as follows:

Held-to-maturity securities (in thousands):

	Amortized cost	Gross unrealized holding gains	Gross unrealized holding losses	Fair value
June 30, 2010				
Obligations of state and political subdivisions	$ 1,946	$ 0	$ 77	$ 1,869
December 31, 2009				
Obligations of state and political subdivisions	$ 1,899	$ 0	$ 111	$ 1,788

At June 30, 2010 and December 31, 2009, securities with a carrying amount of $201.9 million and $187.9 million, respectively, were pledged as collateral to secure public deposits and for other purposes.

The following table shows the approximate fair value of the Company s debt securities (in thousands) at June 30, 2010 using contractual maturities. Expected maturities will differ from contractual maturity because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

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	Available-for-sale				Held-to-maturity			
	Amortized Cost		Fair Value		Amortized Cost		Fair Value	
Amounts maturing in:								
One Year or Less	$		$		$		$	
One Year through Five Years		2,826		2,836				
After Five Years through Ten Years		6,438		6,505		470		456
After Ten Years		152,759		138,419		1,476		1,413
Collateralized mortgage obligations		85,220		84,440				
Mortgage-backed securities		18,972		19,788				
Total	$	266,215	$	251,988	$	1,946	$	1,869

Gross proceeds from the sale of securities for the three months ended June 30, 2010 and 2009 were $1.3 million and $6.6 million, respectively, with the gross realized gains being $33 thousand and $300 thousand, respectively, and gross realized losses being $0 and $0, respectively.

Gross proceeds from the sale of securities for the six months ended June 30, 2010 and 2009 were $27.8 million and $31.3 million, respectively, with the gross realized gains being $1.2 million and $0.8 million, respectively, and gross realized losses being $0 and $3 thousand, respectively.

The table below indicates the length of time that individual securities available for sale have been in a continuous unrealized loss position at June 30, 2010 (as restated):

	Less than 12 Months				12 Months or Greater				Total			
	Fair Value		Unrealized Losses		Fair Value		Unrealized Losses		Fair Value		Unrealized Losses	
U.S. Treasury securities and obligations of U.S. government agencies	$		$		$	10,841	$	592	$	10,841	$	592
Obligations of state and political subdivision		26,647		1,154		19,311		4,654		45,958		5,808
Collateralized mortgage obligations:												
Government sponsored agency		11,799		169						11,799		169
Private label						9,698		2,196		9,698		2,196
Residential mortgage-backed securities												
Pooled Trust Preferred Senior Class						1,310		2,546		1,310		2,546
Pooled Trust Preferred Mezzanine Class						1,482		8,136		1,482		8,136
Corporate debt securities						394		106		394		106
Equity securities												
	$	38,446	$	1,323	$	43,036	$	18,230	$	81,482	$	19,553

The table below indicates the length of time individual securities available for sale have been in a continuous unrealized loss position at December 31, 2009 (as restated):

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	Less than 12 Months		12 Months or Greater		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury securities and obligations of U.S. government agencies	$ 12,527	$ 215	$ 9,588	$ 1,508	$ 22,115	$ 1,723
Obligations of state and political subdivisions	30,266	1,274	16,904	4,699	47,170	5,973
Collateralized mortgage obligations:						
Government sponsored agency	31,733	370			31,733	370
Private label			13,591	3,112	13,591	3,112
Residential mortgage-backed securities	3,585	31			3,585	31
Pooled Trust Preferred Senior Class			1,391	2,457	1,391	2,457
Pooled Trust Preferred Mezzanine Class			2,419	10,040	2,419	10,040
Corporate debt securities			356	144	356	144
Equity securities						
	$ 78,111	$ 1,890	$ 44,249	$ 21,960	$ 122,360	$ 23,850

At June 30, 2010, the Company s investment portfolio was comprised of U.S. Government agency securities, tax-exempt obligations of states and political subdivisions, government sponsored agency obligations, private label collateralized mortgage obligations (PLCMOs), residential mortgage-backed securities, pooled trust preferred collateralized debt obligations securities (PreTSLs), and corporate debt securities.

At June 30, 2010, excluding PLCMOs and PreTSLs, 136 of the Company s debt securities holdings having unrealized losses have depreciated 8.82% from their amortized cost basis. These securities are guaranteed by either the U.S. Government, government sponsored agencies, other governments or corporations. Sixty six (66%) percent of the Company s investment in obligations of state and political subdivisions are also guaranteed by underlying insurance which further secures the safety of principal. These unrealized losses relate principally to current interest rates for similar types of securities. The Company does not intend to sell these securities and does not anticipate that it will be necessary to sell these securities before the full recovery of principal and interest due, which may be at maturity. Therefore, the Company did not consider the carrying value of these securities to be other-than-temporarily impaired at June 30, 2010.

At June 30, 2010, eight of the Company s PLCMOs have realized OTTI losses of $2.3 million, have unrealized losses of $2.0 million, and have depreciated 36.09% from their amortized cost basis.

At June 30, 2010, seven of the Company s PreTSLs have realized OTTI losses of $21.2 million, have unrealized losses of $10.7 million, and have depreciated 91.95% from their amortized cost basis.

Under ASC Topic 320, Investments Debt and Equity Securities, if management has no intent to sell the security and it is not more likely than not that the Company will be required to sell the security before recovery of its amortized cost, then other-than-temporary declines in the fair value of the debt security that are related to credit losses must be recognized in earnings as realized losses and those declines that are related to other factors are recognized in other comprehensive income. Numerous factors, including lack of liquidity for re-sales of certain investment securities, absence of reliable pricing information for investment securities, adverse changes in business climate, adverse actions by regulators, or unanticipated changes in the competitive environment could have a negative effect on our investment portfolio and may result in OTTI on the Company s investment securities in future periods.

On a quarterly basis, the Company evaluates its investment securities for OTTI. Unrealized losses on securities are considered to be OTTI when the Company believes the security s impairment is due to factors that could include the security issuers inability to pay interest or dividends, the security issuers potential for default, and/or other factors. When a held to maturity or available for sale debt security is assessed for OTTI, the Company must first consider (a) whether management intends to sell the security, and (b) whether it is more likely than not that the Company will be required to sell the security prior to recovery of its amortized cost basis. If one of these circumstances applies to a security, an OTTI loss is recognized in the statement of operations equal to the full amount of the decline in fair value below amortized cost. If neither of these circumstances applies to a security, but the Company does not expect to recover the entire amortized cost basis, an OTTI loss has occurred that must be separated into two categories: (a) the amount related to credit loss, and (b) the amount related to other factors. In assessing the level of OTTI attributable to credit loss, the Company compares the present value of cash flows expected to be collected with the amortized cost basis of the security. As discussed above, the portion of the total OTTI related to credit loss is recognized in earnings, while the amount related to other factors is recognized in other comprehensive income. The total OTTI loss is presented in the statement of operations, less the portion recognized in other comprehensive income.

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When a debt security becomes other than temporarily impaired, its amortized cost basis is reduced to reflect the portion of the total impairment related to credit loss.

To determine whether a security s impairment is other-than-temporary, the Company considers factors that include:

- the causes of the decline in fair value, such as credit problems, interest rate fluctuations, or market volatility;

- the severity and duration of the decline;

- the Company s ability and intent to hold equity security investments until they recover in value, as well as the likelihood of such a recovery in the near term;

- the Company s intent to sell security investments, or if it is more likely than not that the Company will be required to sell such securities before recovery of their individual amortized cost basis less any current period credit loss.

For debt securities, the primary consideration in determining whether impairment is other-than-temporary is whether or not it is probable that current or future contractual cash flows have or may be impaired.

Based on the Company s evaluation at June 30, 2010, the Company has determined that the decreases in estimated fair value are temporary with the exception of eight PLCMOs and seven PreTSLs. The Company s discounted estimate of projected cash flows it expects to receive was less than the securities carrying value resulting in a credit-related impairment charge to earnings for the six months ended June 30, 2010 of $2.9 million.

OTTI of Private Label CMOs:

The following PLCMOs held as of June 30, 2010 (in thousands as restated) were determined to be credit impaired either in the current or previous year resulting in a charge to earnings.

Description	**Book Value**	**Fair Value**	**Unrealized gain/loss**	**S&P credit rating**	**Collateral type**	**Credit Impairment Quarter to Date**	**Credit Impairment Year to Date**	**Cumulative Credit Impairment**

RAST 2006-A10 A5	$ 934	$ 654	$ (280)	D	ALT-A30	$	$ 5	$ 283
RAST 2006-A8 2A2	781	735	(46)	D	ALT-A30		7	421
CWALT 2007-7T2 A12	1,833	1,607	(226)	CC	ALT-A30			282
RALI 2006-QS 16 A10	867	711	(156)	D	ALT-A30		2	356
RALI 2006-QS4 A2	1,305	1,047	(258)	CC	ALT-A30	5	11	389
HALO 2007-1 3A6	1,392	610	(782)	CCC	WH-30			79
WMALT 2006-2 2CB	775	851	76	CCC	ALT-A30		33	467
PRIME 2006-1 1A1	1,854	1,495	(359)	CC	WH-30	4	4	45
Total	$ 9,741	$ 7,710	$ (2,031)			$ 9	$ 62	$ 2,322

The OTTI analysis relies on a review of the individual loans that provide the collateral for each security. This information is then used to develop default and severity assumptions over a future horizon for each security. The factors involved in constructing these assumptions are:

- MSA (Metropolitan statistical area), Geographic location
- HPI (Home Price Index) of specific MSAs
- Loan Balance
- Rate Premium
- LTV (both individual and combined if there are other loans)
- FICO
- Loan Purpose (cash-out versus purchase)
- Documentation
- Loan Structure
- Occupancy Status
- Property Type
- Borrower Payment History
- Historical delinquency and roll/curve rates

Adjustments are made to the default/severity vectors that may be warranted given the current environment. The Company then applies

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a fairness check to each vector to review whether future default/severity assumptions are in line with current observable performance. The data used to perform this analysis is provided by a third party provider and the individual loan performance.

Once the Company has default/severity assumptions for the underlying collateral (on a deal specific basis), the Company then has to understand how the timing of losses impacts each specific bond/tranche and how each cash flow changes over time. The default and severity vectors are modeled using a third party cash flow model and both total collateral and tranche specific cash flows are established. The Company then computes various metrics based on the resulting tranche cash flows:

- Total Collateral Principal Loss
- Total Tranche Loss
- Lifetime Tranche Yield
- Tranche Loss Timing

A security is considered to be other-than-temporarily impaired if the analysis results in a change of cash flow from the original expectation which indicates that there is the potential that all principal and/or interest may not be received. Information affecting cash flows and the impact on the collectability of principal and interest are evaluated on a monthly basis as received from service providers. The results are recognized through earnings as they become available. Information discovered subsequent to the balance sheet date but prior to the filing date is included in the OTTI analysis. As a result of this analysis, the Company recorded a charge of $9 thousand and $62 thousand, respectively, against the three and six month periods ended June 30, 2010 for credit losses on its PLCMOs.

The table below illustrates the percentage of the current balance of each PLCMO that was delinquent, in foreclosure, in OREO and the trailing 3 month loss severity that was used in our June 30, 2010 OTTI calculations.

Description	**60-89 Days delinquent**	**90+ Days delinquent**	**Foreclosure**	**OREO**	**3 Month Severity**	**Projected Default Severity**
RAST 2006-A10 A5	4.08%	9.03%	13.91%	2.30%	57.24%	36.52%
RAST 2006-A8 2A2	3.10%	6.89%	14.32%	3.05%	64.96%	58.00%
CWALT 2007-7T2 A12	3.04%	19.52%	15.00%	2.54%	22.67%	57.94%
RALI 2006-QS 16 A10	2.78%	7.77%	17.22%	2.11%	57.64%	63.67%
RALI 2006-QS4 A2	3.10%	5.63%	11.54%	1.49%	52.98%	46.99%
HALO 2007-1 3A6	1.71%	10.69%	7.09%	0.85%	57.45%	48.10%
WMALT 2006-2 2CB	1.74%	8.69%	11.57%	1.90%	72.27%	72.10%
PRIME 2006-1 1A1	1.05%	7.84%	5.42%	1.99%	28.75%	40.00%

OTTI of Pooled Trust Preferred Collateralized Debt Obligations:

As of June 30, 2010, the book value of our PreTSLs totaled $13.5 million with an estimated fair value of $2.8 million and is comprised of seven securities each of which are collateralized by debt issued by bank holding companies and insurance companies. The Company holds one senior tranche and six mezzanine tranches. All of the securities have been downgraded below investment grade. At the time of initial issue, no more than 5% of any pooled security consisted of a security issued by any one institution. As of June 30, 2010, six of these securities had no excess subordination and one had excess subordination of 8.04% of the current performing collateral. Excess subordination is the amount by which the underlying performing collateral exceeds the outstanding bonds in the current class plus all senior classes. It can also be referred to as credit enhancement. As deferrals and defaults of underlying issuers occur, the excess subordination is reduced or eliminated, increasing the risk of the security experiencing principal or interest shortfalls. Conversely, subordination can be increased as collateral transitions from non-performing to performing. The coverage ratio, or overcollateralization, of a specific security measures the rate of performing collateral to a given class of notes. It is calculated by dividing the performing collateral in a transaction by the current balance of the class of notes plus all classes senior to that class.

The following table presents information about the Company s collateral and subordination for its PreTSLs as of June 30, 2010 (as restated):

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(In thousands) Deal	Performing collateral	Bonds outstanding	Excess/ insufficient collateral	Coverage ratio	Excess subordination	Credit Impairment Quarter to Date	Credit Impairment Year to Date	Cumulative Credit Impairment
PreTSL VIII	$ 235,300	$ 394,861	$ (159,561)	59.59%	N/A	$ 44	$ 44	$ 2,964
PreTSL IX	313,520	337,880	(24,360)	92.79%	N/A			1,680
PreTSL X	282,750	383,171	(100,421)	73.79%	N/A	133	137	2,782
PreTSL XI	426,995	479,847	(52,852)	88.99%	N/A	544	544	3,330
PreTSL XIX	540,135	550,574	(10,439)	98.10%	N/A	1,036	1,203	2,268
PreTSL XXVI	689,200	637,920	51,280	108.04%	8.04%			251
PreTSL XXVIII	281,850	308,278	(26,428)	91.43%	N/A	790	912	7,954
Total						$ 2,547	$ 2,840	$ 21,229

The following list details information for each of the Company s PreTSLs as of June 30, 2010:

Deal		Book value	Fair value	Unrealized gain/loss	Moody s / Fitch ratings	Current number of performing issuers	Actual deferrals / defaults as a % of current collateral	Expected future default rate
PreTSL VIII	Mezzanine	$ 36	$ 1	$ (35)	C / C	23	44.60%	3.16%
PreTSL IX	Mezzanine	1,320	275	(1,045)	Ca / C	36	30.30%	1.60%
PreTSL X	Mezzanine	218	5	(213)	C / C	37	43.50%	2.34%
PreTSL XI	Mezzanine	1,670	216	(1,454)	Ca / C	48	29.00%	2.57%
PreTSL XIX	Senior	4,907	970	(3,937)	B3 / B	87	22.90%	2.19%
PreTSL XXVI	Mezzanine	3,855	1,310	(2,545)	B1 / B	55	28.50%	1.87%
PreTSL XXVIII	Mezzanine	1,468	15	(1,453)	Ca / CC	44	21.90%	1.90%
Total		$ 13,474	$ 2,792	$ (10,682)				

The Company s PreTSLs are measured for OTTI within the scope of ASC Topic 325 by determining whether an adverse change in estimated cash flows has occurred. Determining whether there has been an adverse change in estimated cash flows from the cash flows previously projected involves comparing the present value of remaining cash flows previously projected against the present value of the cash flows estimated at June 30, 2010. The Company considers the discounted cash flow analysis to be our primary evidence when determining whether credit related OTTI exists.

Results of a discounted cash flow test are significantly affected by variables such as the estimate of the probability of default, estimates of future cash flows, discount rates, prepayment rates and the creditworthiness of the underlying issuers. The following provides additional information for each of these variables:

- Probability of Default An issuer level approach is used to analyze each security and default and recovery assumptions are based on the credit quality of the underlying issuers (generally, bank holding companies or insurance companies). Each bank issuer is evaluated based upon an examination of the trends in its earnings, net interest margin, operating efficiency, liquidity, capital position, level of nonperforming loans to total loans, apparent sufficiency of loan loss reserves, Texas ratio and whether the bank received TARP monies. From this information, each issuer bank that is currently performing is assigned a category of Good, Average, Weak, or Troubled. Default rates are then assigned based upon the historical performance of each category. Additionally, because the information available to the Company regarding the underlying insurance company issuers is more limited than for bank issuers, rather than performing an analysis of each such issuer s results and assigning insurance company issuers to these same categories, the Company uses the Moody s one year long-term default rate assumption for insurance companies. The historical default rates used in this analysis are:

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Default Rate

Category	Year 1	Year 2	Year 3	Thereafter
Good	0.50%	0.60%	0.60%	0.40%
Average	1.80%	2.30%	2.30%	1.50%
Insurance	1.00%	1.20%	1.20%	0.80%
Weak	5.80%	7.20%	7.20%	4.80%
Troubled	9.70%	12.20%	12.20%	8.10%

Each issuer in the collateral pool is assigned a probability of default for each year until maturity. Banks currently in default or deferring interest payments thus far are assumed to default immediately. A zero percent projected recovery rate is applied to both deferring and defaulted issuers. The probability of default is updated quarterly based upon changes in the creditworthiness of each underlying issuer. Timing of defaults and deferrals has a substantial impact on each valuation. As a result of this analysis, each issuer is assigned an expected default rate specific to that issuer.

- Estimates of Future Cash Flows While understanding the composition and characteristics of each bank issuer is important in evaluating the security, certain issuers have a disproportionate impact (both positive and negative) based upon other attributes, such as the interest rate payable by each issuer. Each credit is assessed independently, and the timing and nature of each issuer s performance is assessed. Once assessed, the expected performance of each issuer is applied to a structural cash flow model. Due to the complexity of these transactions, the expected performance of each unique issuer requires an adherence to the governing documents of the securitization to derive a cash flow. A model produced by a third party is utilized to assist in determining cash flows. Utilization of third party cash flow modeling to derive cash flows from assumptions is a market convention for these types of securities.

- Discount Rate The Company is discounting projected cash flows based upon its discount margin defined at the time of purchase, which constitutes a spread over 3-month LIBOR plus credit premium, consistent with our pre-purchase yield.

- Prepayment Rate Lack of liquidity in the market for PreTSL securities, credit rating downgrades and market uncertainties related to the financial industry are factors contributing to the impairment of these securities. During the early years of PreTSL securities, prepayments were common as issuers were able to refinance into lower cost borrowings. Since the middle of 2007, however, this option has all but disappeared and the Company is operating in an environment which makes early redemption of these instruments unlikely. Accordingly, the Company has assumed zero prepayments when modeling the cash flows of these securities. The Company performed a sensitivity analysis using 1% and 3% prepayment assumptions. As a result of this analysis, the Company determined that employing a 1% and a 3% prepayment assumption rather than assuming zero prepayments would have resulted in an additional credit loss of approximately $859 thousand and $894 thousand, respectively, to the $2.9 million impairment charge taken during the first six months of 2010. Credit losses would increase as a result of an increase in the prepayment assumption because prepayments reduce the amount of excess subordination that would be available to absorb expected losses.

- Credit Analysis A quarterly credit evaluation is performed for each of the securities. While the underlying core component of these securities are the credit characteristics of the underlying issuers , typically banks, other characteristics of the securities and, issuers are evaluated and stressed to determine cash flow. These include but are not limited to interest rate payable by each issuer, certain derivative contracts, default timing, and interest rate volatility. Issuer level credit considers all evidence available to us and includes the nature of the issuer s business, its years of operating history, corporate structure, loan composition, loan concentrations, deposit mix, asset growth rates, geographic footprint and local environment. Depending upon the security, and its place in the capital structure, certain analytical assumptions are isolated with greater scrutiny. The core analysis for each specific issuer focuses on profitability, return on assets, shareholders equity, net interest margin, credit quality ratios, operating efficiency, capital adequacy and liquidity.

The Company has evaluated its PreTSLs and PLCMOs considering all available evidence, including information received after the balance sheet date but before the filing date, and determined that the discounted estimated projected cash flows are less than the securities carrying value, resulting in an impairment charge to earnings for the three and six months ended June 30, 2010 of $2.5 million and $2.9 million, respectively.

The table below provides a cumulative roll forward of credit losses recognized (dollars in thousands):

Other-Than-Temporarily Impaired Securities

Beginning Balance January 1, 2010	$	20,649
Credit losses on debt securities for which OTTI was not previously recognized		
Additional credit losses on debt securities for which OTTI was previously recognized		2,902
Ending Balance, June 30, 2010	$	23,551

Investments in FHLB and FRB stock, which have limited marketability, are carried at cost in Other Assets and totaled $12.1 million and $11.8 million at June 30, 2010 and December 31, 2009, respectively. Management noted no indicators of impairment for the

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FHLB of Pittsburgh at June 30, 2010.

Note 8. Fair Value Measurements

In determining fair value, the Company uses various valuation approaches, including market, income and cost approaches. ASC Topic 820 establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability, which are developed based on market data obtained from sources independent of the Company. Unobservable inputs reflects the Company s assumptions about the assumptions the market participants would use in pricing an asset or liability, which are developed based on the best information available in the circumstances.

The fair value hierarchy gives the highest priority to unadjusted quoted market prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). The fair value hierarchy is broken down into three levels based on the reliability of inputs as follows:

- Level 1 valuation is based upon unadjusted quoted market prices for identical instruments traded in active markets.

- Level 2 valuation is based upon quoted market prices for similar instruments traded in active markets, quoted market prices for identical or similar instruments traded in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by market data.

- Level 3 valuation is derived from other valuation methodologies including discounted cash flow models and similar techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in determining fair value.

An asset or liability s level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

A description of the valuation methodologies used for assets recorded at fair value, and for estimating the fair value of assets for financial instruments not recorded at fair value, is set forth below.

Cash, Short-term Investments, Accrued Interest Receivable and Accrued Interest Payable

For these short-term instruments, the carrying amount is a reasonable estimate of fair value.

Securities

The estimated fair values of available for sale equity securities are determined by obtaining quoted prices on nationally recognized exchanges (Level 1 inputs). The estimated fair values for the Company s investments in obligations of U.S. government agencies, obligations of state and political subdivisions, government sponsored agency collateralized mortgage obligations, private label collateralized mortgage obligations, residential mortgage backed securities, and corporate debt securities are obtained by the Company from a nationally-recognized pricing service. This pricing service develops estimated fair values by analyzing like securities and applying available market information through processes such as benchmark curves, benchmarking of like securities, sector groupings and matrix pricing (Level 2 inputs), to prepare valuations. Matrix pricing is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities relationship to other benchmark quoted securities. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond s terms and conditions, among other things and are based on data obtained from sources independent from the Company. The Level 2 investments in the Company s portfolio are priced using those inputs that, based on the analysis prepared by the pricing service, reflect the assumptions that market participants would use to price the assets. The Company has determined that the Level 2 designation is appropriate for these securities because, as with most fixed-income securities, those in the Company s portfolio are not exchange-traded, and non-exchange-traded fixed income securities are typically priced by correlation to observed market data. The Company has reviewed the pricing service s methodology to confirm its understanding that such methodology results in a valuation based on quoted market prices for similar instruments traded in active markets, quoted markets for identical or similar instruments traded in markets that are not active and model-based valuation techniques for which the significant assumptions can be corroborated by market data as appropriate to a Level 2 designation.

In accordance with the Company s adoption of the new authoritative accounting guidance under ASC Topic 820, the Company reviewed the volume and level of activity for all classes of securities and attempted to identify transactions which may not be orderly or reflective of a significant level of activity and volume. For securities meeting these criteria, the quoted prices received from either market participants or an independent pricing service may be adjusted, as necessary, to estimate fair value (fair values based on Level 3 inputs). If applicable, the adjustment to fair value was derived based on present value cash flow model projections prepared by the Company or obtained from third party providers utilizing assumptions similar to those incorporated by market participants. The estimated fair value of the PreTSLs in the Company s securities portfolio are obtained from a third-party service provider that prepared the valuation using a discounted cash flow approach with inputs derived from unobservable market information (Level 3 inputs). The valuation of PreTSLs is further described below and in Note 7.

As of June 30, 2010, the Company owned PreTSLs having a book value of $13.5 million. The market for these securities at June 30, 2010 is not active and markets for similar securities are also not active. PreTSLs were historically priced using Level 2 inputs. However, the decline in the level of observable inputs and market activity in this class of investments by the measurement date has been significant and resulted in unreliable external pricing. Broker pricing and bid/ask spreads, when available, vary widely. The once active market has become comparatively inactive. As such, the valuation of these investments is now determined using Level 3 inputs. The Company obtained the valuations from a third-party service provider that prepared the valuations using a discounted cash flows approach. The Company takes measures to validate the service provider s analysis and is actively involved in the valuation process, including reviewing and verifying the assumptions used in the valuation calculations.

Results of a discounted cash flow test are significantly affected by variables such as the estimate of the probability of default, estimates of future cash flows, discount rates, prepayment rates and the creditworthiness of the underlying issuers. Refer to the discussion of these variables in Note 7. The Company considers these inputs to be unobservable Level 3 inputs because they are based on the Company s estimates about the assumptions market participants would use in pricing this type of asset and developed based on the best information available in the circumstances rather than on observable inputs. The Company continues to monitor the market for PreTSLs to assess the market activity and the availability of observable inputs and will continue to apply these controls and procedures to the valuations received from its third party service provider for the period it continues to use an outside valuation service. As it relates to fair value measurements, once each issuer is categorized and the forecasted default rates have been applied, the expected cash flows are modeled using the variables described above. The Company then applies a 15% discount rate to PreTSL XIX and PreTSL XXVI and a 20% discount rate for the remaining PreTSLs to the expected cash flows to estimate fair value.

Loans

For non-impaired loans, fair values are estimated by discounting the projected future cash flows using market discount rates that reflect the credit and interest rate risk inherent in the loan. Projected future cash flows are calculated based upon contractual maturity or call dates, projected repayments and prepayments of principal. Impaired loans are measured on a loan-by-loan basis based upon the present value of expected future cash flows at the loan s effective interest rate or, for collateral dependent loans, the fair value of the impaired loan balance is based on the appraised loan value or other reasonable offers less estimated costs to sell. See also, Note 5 Loans.

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Deposits

The fair value of demand deposits, savings deposits, and certain money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities.

Borrowed funds

Rates currently available to the Bank for debt with similar terms and remaining maturities are used to estimate fair value of existing debt.

Commitments to extend credit and standby letters of credit

The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties.

Assets and Liabilities Measured on a Recurring Basis

The following tables detail the financial asset amounts carried at fair value that are measured for fair value on a recurring basis at June 30, 2010 and December 31, 2009 and indicate the assets classifications within the fair value hierarchy (dollars in thousands):

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Fair Value Measurements at June 30, 2010 (as restated)

	Fair value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant other unobservable inputs (Level 3)
Available for sale securities:				
U.S. Treasury securities and obligations of U.S. Government agencies	$ 27,785		$ 27,785	
Obligations of political and state subdivisions	116,789		116,789	
Government sponsored agency CMOs	71,663		71,663	
Private label CMOs	12,777		12,777	
Residential mortgage backed securities	19,788		19,788	
Pooled trust preferred Senior Class	1,309			1,309
Pooled trust preferred Mezzanine Class	1,483			1,483
Class				
Corporate debt securities	394		394	
Equity securities	1,018	1,018		
Total securities available for sale	$ 253,006	$ 1,018	$ 249,196	$ 2,792

Fair Value Measurements at December 31, 2009 (as restated)

	Fair value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant other unobservable inputs (Level 3)
Available for sale securities:				
U.S. Treasury securities and obligations of U.S. Government agencies	$ 27,089		$ 27,089	
Obligations of political and state subdivisions	118,670		118,670	
Government sponsored agency CMOs	53,495		53,495	
Private label CMOs	21,059		21,059	
Residential mortgage backed securities	27,442		27,442	
Pooled trust preferred Senior Class	1,391			1,391
Pooled trust preferred Mezzanine Class	2,419			2,419
Corporate debt securities	356		356	
Equity securities	1,025	1,025		
Total securities available for sale	$ 252,946	$ 1,025	$ 248,111	$ 3,810

The table below presents reconciliation and statement of operations classifications of gains and losses for all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the six month period ended June 30, 2010 and year ended December 31, 2009 (in thousands):

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Fair Value Measurements Using Significant Unobservable Inputs (Level 3)

	Available for Sale Securities For the six months ended June 30, 2010 (as restated)		2,009	
Balance, beginning of the period	$	3,810	$	17,652
Accretion of discount		7		8
Payments received				
Increase in amortized cost				
Change in unrealized gains (losses) on securities not deemed other-than-temporarily impaired during the period		(66)		413
Other-than-temporary impairment included in other comprehensive income		1,881		(1,298)
Other-than-temporary impairment included in earnings		(2,840)		(242)
Transfers in and out of Level 3				
Balance, end of period	$	2,792	$	16,533

The net unrealized (losses) gains for the six months ended June 30, 2010 included in other comprehensive income attributable to the change in unrealized gains or losses relating to assets still held at the reporting date was $1.82 million.

The net unrealized (losses) gains for the six months ended June 30, 2009 included in other comprehensive income attributable to the change in unrealized gains or losses relating to assets still held at the reporting date was $(885) thousand.

Gains and losses (realized and unrealized) included in earnings or comprehensive income are as follows (dollars in thousands):

June 30, 2010		
Total gains or losses included in earnings for the period	$	(2,840)
Change in unrealized gains or losses relating to assets still held the end of the period	$	1,815
June 30, 2009		
Total gains or losses included in earning for the period	$	(242)
Change in unrealized gains or losses relating to assets still held at the end of the period	$	(885)

As of June 30, 2010, the Company owned PreTSLs having a book value of $13.5 million. The market for these and other similar securities at June 30, 2010 was not active. PreTSLs were historically priced using Level 2 inputs. However, the decline in the level of observable inputs and market activity in this class of investments by the measurement date has been significant and resulted in unreliable external pricing. Broker pricing and bid/ask spreads, when available, vary widely. The once active market has become comparatively inactive. As such, the valuation of these investments is now determined using Level 3 inputs. The Company obtained the pricing for these securities from a third party service provider that prepared the valuations using the discounted cash flows approach discussed in Note 7.

Results of a discounted cash flow test are significantly affected by variables such as the estimate of the probability of default, estimates of future cash flows, discount rates, prepayment rates and the creditworthiness of the underlying banks. Refer to the discussion of these variables in Note 7. As it relates to fair value measurements, once each issuer is categorized and the forecasted default rates have been applied, the expected cash flows are modeled using the variables described above. The Company then applies a 15% discount rate to PreTSL XIX and PreTSL XXVI and a 20% discount rate for the remaining PreTSLs to the expected cash flows to estimate fair value.

As of June 30, 2010, the Company owned PLCMOs having a book value of $14.8 million. The market for these securities was minimally active and severely stressed. The Company performed an OTTI analysis on its PLCMOs. The OTTI analysis relies on a review of the individual loans that provide the collateral for each security. This information is then used to develop default and severity assumptions over a future horizon for each security. The factors involved in constructing these assumptions are:

- MSA (Metropolitan statistical area), Geographic location
- HPI (Home Price Index) of specific MSAs
- Loan Balance
- Rate Premium
- LTV (both individual and combined if there are other loans)
- FICO

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- Loan Purpose (cash-out versus purchase)
- Documentation
- Loan Structure
- Occupancy Status
- Property Type
- Borrower Payment History
- Historical delinquency and roll/curve rates

Adjustments are made to the default/severity vectors that may be warranted given the current environment. The Company then applies a fairness check to each vector to review whether future default/severity assumptions are in line with current observable performance. The data used to perform this analysis is provided by a third party provider and the individual loan performance.

Once the Company has default/severity assumptions for the underlying collateral (on a deal specific basis), the Company then has to understand how the timing of losses impacts each specific bond/tranche and how each cash flow changes over time. The default and severity vectors are modeled using a third party cash flow model and both total collateral and tranche specific cash flows are established. The Company then computes various metrics based on the resulting tranche cash flows:

- Total Collateral Principal Loss
- Total Tranche Loss
- Lifetime Tranche Yield
- Tranche Loss Timing

Assets and Liabilities Measured on a Non-Recurring Basis

The following tables detail the assets measured at fair value on a non-recurring basis at June 30, 2010 and December 31, 2009 and indicate the assets classifications within the fair value hierarchy (dollars in thousands):

	Fair Value Measurements at June 30, 2010			Fair Value Measurements at December 31, 2009		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
			(in thousands)			
Impaired loans			$ 48,481			$ 36,608
Other real estate owned			$ 15,022			$ 11,184

Collateral-dependent impaired loans consist of nonaccrual loans and troubled debt restructured loans that are classified as Level 3 assets. Impaired loans are measured at fair value based on the present value of expected future cash flows discounted at the loan s effective interest rate, or at the loan s observable market price or fair value of its collateral, if the loan is collateral dependent. When the measure of the impaired loan is less than the recorded investment in the loan, the impairment is recorded through a valuation allowance. The amount shown is the balance of impaired loans, net of any charge-offs and the related allowance for loan losses.

Other real estate owned properties are recorded at the fair value less the estimated cost to sell at the date of foreclosure. It is the Company s policy to obtain certified external appraisals of real estate collateral underlying impaired loans, including OREO, and it estimates fair value using those appraisals. Other valuation sources may be used, including broker price opinions, letters of intent and executed sale agreements.

The following estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies. However, management judgment is required to interpret data and develop fair value estimates. Accordingly, the estimates below 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 methodologies may have a material effect on the estimated fair value amounts.

The estimated fair values of the Company s financial instruments (in thousands) are as follows:

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	June 30, 2010		December 31, 2009	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial Assets				
Cash and short term investments	$ 82,720	$ 82,720	$ 86,364	$ 86,364
Securities	254,952	254,875	254,845	254,031
Gross Loans	889,225	845,406	939,565	871,732
Accrued interest receivable	3,907	3,907	4,245	4,245
Financial Liabilities				
Deposits	1,021,782	1,026,221	$ 1,071,608	$ 1,076,700
Borrowed funds	211,092	213,606	217,467	220,434
Accrued interest payable	2,704	2,704	3,064	3,064
Off-Balance Sheet Financial Instruments				
Commitments to extend credit and standby letters of credit	$ 149	$ 149	$ 189	$ 189

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Note 9. Earnings per Share

Basic earnings per common share is the net income (loss) divided by the weighted average number of common shares outstanding during the period. The shares in the denominator were 16,306,670 and 16,158,640 for the three months ended June 30, 2010 and 2009, respectively. Diluted earnings per share includes the dilutive effect of additional potential common shares for stock options outstanding. The shares in the denominator were 16,300,515 and 16,155,745 for the six months ended June 30, 2010 and 2009, respectively.

The calculation for basic earnings per common share is the net income (loss) divided by the weighted average number of common shares outstanding during the period. Diluted earnings per share includes the dilutive effect of additional potential common shares for stock options outstanding.

(In thousands except for share data)	three months ended June 30, 2010 (as restated)	three months ended June 30, 2009	six months ended June 30, 2010 (as restated)	six months ended June 30, 2009
Net income available to common shareholders	$ (5,195)	$ (2,216)	$ (6,020)	$ 1,022
Weighted average shares outstanding - basic	16,306,670	16,158,640	16,300,515	16,111,808
Plus: Common share equivalents				43,937
Weighted average shares outstanding - diluted	16,306,670	16,158,640	16,300,515	16,155,745
Earnings per share - basic	$ (0.32)	$ (0.14)	$ (0.37)	$ 0.06
Earnings per share - diluted	$ (0.32)	$ (0.14)	$ (0.37)	$ 0.06

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Note 10. Bank Premises and Equipment

Bank premises and equipment are summarized as follows (in thousands):

	June 30, 2010	December 31, 2009
Land	$ 5,169	$ 4,765
Buildings	13,206	13,266
Furniture, fixtures and equipment	10,996	10,828
Leasehold improvements	4,957	4,892
Total	34,328	33,751
Less accumulated depreciation	13,709	13,084
Net	$ 20,619	$ 20,667

Depreciation and amortization expense amounted to $373 thousand and $725 thousand for the three and six months ended June 30, 2010 compared to $373 thousand and $759 thousand for the same periods in the previous year.

Note 11. Related Party Transactions

The Company and the Bank have engaged in and intend to continue to engage in banking and financial transactions in the conduct of its business with directors, executive officers and their related parties.

The Bank has granted loans, letters of credit and lines of credit to directors, executive officers and their related parties. The following table summarizes the changes in the total amounts of such loans and advances under lines of credit during the six months ended June 30, 2010:

	June 30, 2010 (in thousands)
Opening balance	$ 102,705
Advances	43,984
Principal repayments/reductions	(37,872)
Ending balance	$ 108,817
Ending balance December 31, 2009	$ 105,698
Less loans removed - resignations	(2,993)
Adjusted opening balance	$ 102,705

At June 30, 2010 loans in the amount of $2.0 million to directors, executive officers and their related parties were not performing in accordance with the terms of the loan agreements, representing a $2.2 million decrease compared to December 31, 2009. The decrease is primarily attributable to the resignation of a director during 2009 and the charge-down of other loans. Also, as of June 30, 2010 additional loans in the amount of $13.3 million to directors, executive officers and their related parties were categorized as criticized loans within the Bank s risk rating system, meaning they are considered to present a higher risk of collection than other loans.

As of June 30, 2011, $7.0 million of the loans described above were subsequently charged-off, $5.6 million in loans were non-performing and $1.2 million in loans to directors, executive officers and their related parties were criticized. The remaining $1.5 million has been reclassified to a non-criticized risk rating. For further description of loans with related parties see Note 14 to the Company s financial statements included in the Company s annual report on Form 10-K/A for the period ended December 31, 2009.

Deposits from directors, executive officers and their related parties amounted to $139.3 million and $136.5 million at June 30, 2010 and December 31, 2009, respectively.

Note 12. Stock Option Plans

On August 30, 2000, the Company s Board adopted an Employee Stock Incentive Plan in which options may be granted to key officers and other employees of the Company. The aggregate number of shares which may be issued upon exercise of the options under the plan cannot exceed 1,100,000 shares. Options and rights granted under the plan become exercisable six months after the

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date the options are awarded and expire ten years after the award date. Upon exercise, the shares are issued from the Company s authorized but unissued stock.

The Board also adopted on August 30, 2000, the Independent Directors Stock Option Plan for directors who are not officers or employees of the Company. The aggregate number of shares issuable under the plan cannot exceed 550,000 shares and are exercisable six months from the date the awards are granted and expire three years after the award date. Upon exercise, the shares are issued from the Company s authorized but unissued shares. There was no compensation expense related to option plans during the three and six months ended June 30, 2010 and 2009.

In accordance with current accounting guidance, all options are charged against income at their fair value. Awards granted under the plans vest immediately and the entire expense of the award is recognized in the year of grant.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model average assumptions:

	June 30, 2010	**December 31, 2009**
Dividend yield	N/A	3.87%
Expected life	N/A	10 years
Expected volatility	N/A	27.8%
Risk-free interest rate	N/A	2.99%

A summary of the status of the Company s stock option plans is presented below:

	Six months ended June 30,					
	2010			**2009**		
	Shares		**Weighted Average Exercise Price**	**Shares**		**Weighted Average Exercise Price**
Outstanding at the beginning of the period	366,248	$	12.18	325,134	$	12.36
Granted				74,600	$	10.81
Exercised						
Forfeited	(133,721)	$	12.55	(3,061)		18.80
Outstanding at the end of the period	232,527			396,673	$	12.02
Options exercisable at June 30,	232,527			396,673	$	12.30
Weighted average fair value of options granted during the year					$	2.13

Stock-Based Compensation Expense

There were no options exercised during these periods. As of June 30, 2010, there was no unrecognized compensation expense.

Information pertaining to options outstanding at June 30, 2010 is as follows:

	Options Outstanding			Options Exercisable	
Range of Exercise Price	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
$5.19-$23.13	232,527	5.1 years	$ 12.55	232,527	$ 12.55

As of June 30, 2010, there was no aggregate intrinsic value of exercisable options.

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ITEM 2 - MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Amended Quarterly Report should be read in conjunction with the more detailed and comprehensive disclosures included on our Amended Form 10-K/A for the year ended December 31, 2009 and our Amended Form 10-Q/A for the quarter ended March 31, 2010. In addition, please read this section in conjunction with our Consolidated Financial Statements and Notes to Consolidated Financial Statements contained herein.

FORWARD-LOOKING STATEMENTS

The Company may from time to time make written or oral forward-looking statements, including statements contained in the Company s filings with the SEC (including this Amendment and the exhibits hereto), in its reports to shareholders and in other communications by the Company, which are made in good faith by the Company pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements include statements with respect to the Company s beliefs, plans, objectives, goals, expectations, anticipations, estimates and intentions, that are subject to significant risks and uncertainties, and are subject to change based on various factors (some of which are beyond the Company s control). The words may, could, should, would, believe, anticipate, estimate, expect, intend, plan expressions are intended to identify forward-looking statements. The following factors, among others, could cause the Company s financial performance to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements: the strength of the United States economy in general and the strength of the local economies in the Company s markets; the effects of, and changes in trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System; inflation, interest rate, market and monetary fluctuations; the timely development of and acceptance of new products and services; the impact of the Company s ability to comply with its regulatory agreements and orders; the effectiveness of the Company s revised system of internal controls; the ability of the Company to attract additional capital investment; the impact of changes in financial services laws and regulations (including laws concerning taxes, banking, securities and insurance); technological changes; acquisitions; changes in consumer spending and saving habits; the nature, extent, and timing of governmental actions and reforms, and the success of the Company at managing the risks involved in the foregoing.

The Company cautions that the foregoing list of important factors is not exclusive. Readers are also cautioned not to place undue reliance on any forward-looking statements, which reflect management s analysis only as of the date of this report, even if subsequently made available by the Company on its website or otherwise. The Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company to reflect events or circumstances occurring after the date of this report.

Readers should carefully review the risk factors described in the Annual Report and other documents that we periodically file with the Securities and Exchange Commission, including our Form 10-K/A for the year ended December 31, 2009 and our Form 10-Q/A for the quarter ended March 31, 2010.

Background

The Company is a Pennsylvania corporation, incorporated in 1997 and is registered as a bank holding company under the Bank Holding Company Act of 1956, as amended. The Company became an active bank holding company on July 1, 1998 when it acquired ownership of First National Community Bank (the   Bank).   The Bank is a wholly-owned subsidiary of the Company.

The Company s primary activity consists of owning and operating the Bank, which provides customary retail and commercial banking services to individuals and businesses. The Bank provides practically all of the Company s earnings as a result of its banking services.

The Bank was established as a national banking association in 1910 as   The First National Bank of Dunmore.   The Bank changed its name to   First National Community Bank   effective March 1, 1988. The Bank s operations are conducted from 21 offices located in Lackawanna, Luzerne, Wayne and Monroe Counties, Pennsylvania. The Bank offers many traditional banking services to its customers.

Unless the context otherwise requires, the words   we,   us,   our   and the   Company   are used to refer to First National

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Community Bancorp, Inc. and its subsidiaries.

Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements of the Company include the accounts of its bank subsidiary, First National Community Bank and its wholly-owned subsidiaries. All inter-company transactions and balances have been eliminated. The accounting and reporting policies of the Company conform to U.S. Generally Accepted Accounting Principles (GAAP) and general practices within the financial services industry. Certain prior period amounts have been reclassified to conform to the current presentation. The Company has evaluated subsequent events for potential recognition and/or disclosure in the consolidated financial statements and accompanying notes included thereto.

In preparing the consolidated financial statements, management has made estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated statements of condition and results of operations for the periods indicated. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to change are the allowance for loan and lease losses (ALLL), securities valuations, the evaluation of deferred income taxes and other intangibles, loan servicing rights and investment securities for impairment. The current economic environment has increased the degree of uncertainty inherent in these material estimates.

Additional information about these accounting policies is included in the Critical Accounting Policies section of Management s Discussion and Analysis in the Company s Amendment No.1 on Form 10-K/A for the year ended December 31, 2009 (the Amended 2009 Form 10-K). Although no significant changes to the Company s critical accounting policies were made during the first six months of 2010, the Company has provided as outlined below the changes in its accounting policies that were adopted effective for 2009 and reflected in the restatement of its financial statements included in the Amended 2009 Form 10-K and this Amendment.

On July 1, 2009, the Accounting Standards Codification (ASC) became the Financial Accounting Standards Board s (the FASB) officially recognized source of authoritative U.S. GAAP applicable to all public and non-public non-governmental entities, superseding all existing FASB, American Institute of Certified Public Accountants (AICPA), Emerging Issues Task Force (EITF) and related literature. Rules and interpretive releases of the SEC under authority of federal securities laws are also sources of authoritative guidance for SEC registrants. All other accounting literature is considered non-authoritative. The issuance of the ASC affects the way companies refer to U.S. GAAP in financial statements and other disclosures.

In connection with regulatory reviews of the Company s operations, financial statements and SEC filings, the Company determined that certain of its accounting and reporting policies did not conform to U.S. GAAP and were not being applied properly or should otherwise be revised. Effective for 2009 and as reflected in the Company s Amended 2009 Form 10-K for the year ended December 31, 2009 and this Amendment, the Company made the following changes to its accounting and reporting policies:

- In its preparation of the financial statements included in the Original Report, the Company did not properly formulate and evaluate its ALLL as a result of the timing of charge-offs and the recognition of TDRs. In determining the ALLL included in the Original Report, the Company increased the specific reserve component of the ALLL when it determined a loan had impairment rather than timely recognizing the loss and reducing the reserve. As reflected in this Amendment, the Company changed its ALLL policy to timely recognize charge-offs in the appropriate accounting period. As revised, when a loan is determined to be impaired and collection of the entire amount of the loan is unlikely, the loan is charged off or charged down to the fair market value of the collateral, thus reducing the carrying value of the loan and the ALLL. Additionally, the general reserve component of the ALLL, previously based on one aggregated pool of unimpaired loans, was increased after assigning these loans to one of three pools of Pass , Special Mention or Accruing and Substandard and applying historical loss factors and varied qualitative factor basis point allocations based on the risk profile in each pool to determine the appropriate reserve related to those loans. The general reserve component of the ALLL also increased because of higher historical loss experience resulting from the increased loan charge-offs of impaired loans. The change in policy led to an increase in the provision for loan and lease losses from the Original Report of $7.8 million to a provision of $9.7 million in this Amendment for the six months ended June 30, 2010.

As a result of the change in ALLL policy reflected herein, the ALLL, which was $20.6 million in the Original Report and was comprised of a specific reserve of $9.3 million and a general reserve of $11.3 million, was restated by charging off an additional $1.4 million in loans during the second quarter and recording an additional provision for loan and lease losses of $1.9 million. This

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change, in addition to changes made at December 31, 2009 and March 31, 2010, reallocated the reserve by reducing the specific reserves by $637 thousand, from $9.3 million to $8.7 million. Included in the $8.7 million specific reserve allocation is $5.0 million in the reserve for TDR impairments which were not previously identified by the Company. The addition of the risk pools, along with higher historical loss experience as a result of increased charge-offs, resulted in the general reserves increasing by $7.4 million, from $11.3 to $18.7 million. As a result the restated ALLL was $27.4 million.

- In connection with determining the appropriate ALLL, the Company also revised its loan impairment measurement process. In the Original Report, the Company employed a policy of impairing or charging off impaired collateral-dependent loans upon receipt of a certified appraisal of the collateral and only used alternative valuation sources for the purposes of writing down loans if the receipt of a certified appraisal was significantly delayed, the timing of receipt was uncertain and an alternative methodology could be derived that produced logical results such as an available appraisal for a similar property in a similar location. As a result of input received from the Company s regulators, the Company revised its valuation policy to record downward adjustments on impaired collateral-dependent loans based on a variety of valuation sources, including, but not limited to, certified appraisals, broker price opinions, letters of intent and executed sale agreements.

Additional loan charge-offs reflected in this report resulted from the change in policy to timely recognize charge-offs in the appropriate accounting period. As a result of this change in policy, this report reflects an additional $1.4 million of loan charge-offs from the amount of charge-offs reflected in the Original Report.

The Company also determined that it had calculated its provision for off-balance sheet commitments incorrectly in the Original Report. The reserve for off-balance sheet commitments was previously calculated using all commitments and assumed these commitments would be fully funded. This methodology was revised to provide a reserve on letters of credit and construction commitments. In addition, individual analyses are performed on the aforementioned commitments to borrowers considered to be impaired. As a result, the Company reduced the related liability by $1.0 million at December 31, 2009. The off-balance sheet reserve is stable at $1.5 million at June 30, 2010.

- The Company also revised its policy for determining and calculating the value of the pooled trust preferred collateralized debt obligations securities (PreTSLs) in its securities portfolio and the amount of related credit impairment to employ more severe assumptions. In changing the methodology, the Company adopted a policy that is more consistent with those used by other market participants and that uses the same approach to value all of the PreTSLs in the Company s portfolio. In the Original Report, the Company had assumed that 50% of issuers who had deferred payments would recover, including by paying previously deferred amounts, within two years of deferral. However, as reflected in this Amendment, the Company changed its policy to cause to be produced cash flow models for each security that assumes all deferring issuers default immediately, with no recovery assumed. The Company did not change its policy with respect to defaulted securities: other than temporary impairment (OTTI) in the Original Report and in this Amendment both reflect the assumption that defaulted issuers default immediately with no recovery. As reflected in the Original Report, the Company had not determined whether factors, other than existing deferrals or defaults, indicated that an impairment loss had been incurred with respect to performing issuers, but rather, it had assumed a 0.375% default rate for all securities and relied on market data provided by a third party. As reflected in this Amendment, we changed our policy to evaluate each bank issuer based upon its financial trends, such as earnings, net interest margin, operating efficiency, liquidity, capital position, level of non-performing loans to total loans, apparent sufficiency of loan loss reserves, Texas ratio and whether the issuer received TARP monies. Based on this analysis of each bank issuer s historical experience and assumptions of future events for each bank issuer, we developed annual expected default rates specific to each bank issuer rather than using the same expected default rate of 0.375% for each issuer. Furthermore, we had previously relied on two outside service providers, including a third party that had sold us the PreTSLs included in our securities portfolio to provide us with fair values for our PreTSLs, but under our revised methodology, fair value was calculated by the third party valuation service unaffiliated with the PreTSLs based on our estimates of future cash flows and the assumption that an investor would require a 15% return on investment for PreTSL XIX and PreTSL XXVI and a 20% return on investment for the remaining PreTSLs to be willing to purchase the cash flows. This change in methodology resulted in an additional impairment charge to earnings of $6.2 million for the six months ended June 30, 2010.

A reduction in OTTI was recorded with respect to securities the issuers of which defaulted or deferred payments between January 1, 2010 and June 30, 2010, after the Company reviewed its subsequent events analysis and determined these events reflected credit impairments that existed as of the fourth quarter of 2009. As such, OTTI related to those impairments was reflected in the restated financial statements for the year ended December 31, 2009 in the Amended 2009 Form 10-K.

- In the Original Report, the Company accounted for loan fees and costs inconsistently across loan types. The Company engaged a third party to review its methodology, assist in the calculation of the actual deferred fees and costs and the applicable amortization period and to provide a consistent approach. This analysis has been incorporated into the Company s methodology. This change in methodology resulted in an additional deferral of $112 thousand.

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Executive Summary

The following overview should be read in conjunction with our MD&A in its entirety.

The Company recorded a net loss for the three month period ended June 30, 2010 of $(5.2) million, or $(0.32) per diluted common share, a decrease of $3.0 million compared to a net loss of $(2.2) million or $(0.14) per diluted common share, that was reported for the same period in the prior year. The net loss for the six month period ended June 30, 2010 was $(6.0) million or $(0.37) per diluted common share, a decrease of $(7.0) million compared to earnings of $1.0 million or $0.06 per diluted common share for the same period in the prior year. The $3.0 million increase in the net loss for the quarter ended June 30 2010, as compared to the quarter ended June 30, 2009, was largely due to a $2.6 million reduction in other income primarily due to higher OTTI charges, a $1.4 million decrease in net interest income before provision for loan and lease losses, and a $1.2 million increase in other expense, largely due to a $0.9 million write-down in the carrying value of foreclosed real estate partly. The increase was partially offset by a $2.7 million decrease in the provision for loan and lease losses over the same period. The $7.0 million increase in the net loss for the six months ended June 30, 2010 as compared to the six months ended June 30, 2009, was largely due to a $3.0 million decrease in net interest income before provision for loan and lease losses, a $2.4 million reduction in other income primarily due to higher OTTI charges and a $1.9 million dollar increase in other expense. The return on average equity was (34.43)% and (18.96)% for the three and six months ended June 30, 2010, respectively, compared to (10.96)% and 2.46% for the same periods in the prior year. Return on average assets was (1.58) % and (0.91) % for the three and six months ended June 30, 2010, respectively, compared to (0.83) % and (0.19) % for the same periods in the prior year.

Total assets decreased $60.1 million, or 4.4% to $1.31 billion, at June 30, 2010 as compared to $1.37 billion at December 31, 2009 primarily due to a $55.2 million decrease in net loans. Total deposits decreased $49.8 million or 4.7% to $1.02 billion at June 30, 2010 as compared to $1.07 billion at December 31, 2009. During the same period demand deposits decreased by $9.6 million or 11.3%, interest bearing demand decreased $12.1 million or 3.4% and total time deposits decreased by $37.3 million or 6.8%. These decreases were partially offset by a $9.2 million or 10.7% increase in savings deposits, over the same period. Borrowed funds decreased by $6.34 million or 2.9% during the first six months of 2010 to $211.1 million from $217.5 million at December 31, 2009. The Company used $1.9 million of proceeds generated from the issuance of subordinated debentures in the first quarter of 2010 combined with a reduction in cash and cash equivalents to repay $8.2 million of Federal Home Loan Bank advances (FHLB) during the first half of 2010.

Total shareholders equity decreased $2.8 million, or 4.5%, to $60.2 million at June 30, 2010 from $63.1 million at December 31, 2009. The decrease is primarily due to the net loss of $6.02 million for the six months ended June 30, 2010 partly offset by a $3.5 million decrease in other comprehensive loss.

Summary of Performance

Net Interest Income

Net interest income on a tax equivalent basis was $9.8 million for the second quarter of 2010, a $1.4 million decrease from $11.2 million or 12.5% for the second quarter of 2009. The decrease from the second quarter of 2009 was due to lower yields earned on loans and investment securities partially offset by higher holdings of investment securities, federal funds sold and the lower cost of interest-bearing deposits. Net interest income on a tax equivalent basis was $20.0 million for the six months ended June 30, 2010, a $2.8 million decrease from $22.8 million or 12.3% for the six months ended June 30, 2009. The decrease from comparable period in 2009 was also attributable to lower yields earned on loans and investment securities partially offset by higher holdings of investment securities, federal funds sold and the lower cost of interest-bearing deposits.

Interest income on loans on a tax equivalent basis decreased $1.5 million for the three month period ended June 30, 2010 compared to the same period in 2009 primarily due to a 30 basis point decline in the tax equivalent yield on loans and a $63.0 million or 6.7% decrease in average loan balances. Interest income on loans on a tax equivalent basis decreased $2.8 million for the six month period ended June 30, 2010 compared to the same period in 2009 primarily due to a 28 basis point decline in the tax equivalent yield on loans and a $53.6 million or 5.6% decrease in average loan balances. The yield on loans was negatively affected by the payoffs of higher yielding loans which cannot be replaced in this low interest rate environment and lower loan demand caused by the continuing economic slowdown.

Interest and dividend income on investment securities on a tax equivalent basis decreased by $0.3 million during the quarter ended June 30, 2010 as compared to the quarter ended June 30, 2009 primarily due to lower investment yields partially offset by higher outstanding balances. The $7.5 million or 2.7% increase in average investments to $279.2 million at June 30, 2010 from $271.8 million at June 30, 2009 partially offset the 65 basis points decrease in the tax equivalent yield for the quarter ended June 30, 2010 as compared to the same period in 2009. Interest and dividend income on investment securities decreased by $0.7 million during the six months ended June 30, 2010 as compared to the six months ended June 30, 2009.

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primarily due to lower investment yields partially offset by a marginal increase in outstanding investments. The $1.3 million increase in average investments to $280.3 million at June 30, 2010 from $279.0 million at June 30, 2009 partially offset the 56 basis points decrease in the tax equivalent yield for the six months ended June 30, 2010 as compared to the same period in 2009. Proceeds from the sales and calls of higher yielding securities were reinvested into shorter duration lower yielding securities.

Average federal funds sold increased by $25.1 million during the quarter ended June 30, 2010 as compared to the same quarter in 2009 and by $40.7 million for the six months ended June 30, 2010 as compared to the six months ended June 30, 2009. The increase in the average balance of federal funds sold was attributable to the Company not being able to sufficiently re-deploy its excess liquidity into loans and investment securities that met the Company s quality, return and duration requirements.

Interest expense decreased $0.6 million, or 8.6%, to $5.6 million for the three months ended June 30, 2010 from $6.2 million for the three months ended June 30, 2009. The cost of interest-bearing deposits decreased $0.6 million to $3.7 million for the three months ended June 30, 2010 from $4.3 for the three months ended June 30, 2009. The $11.7 million decrease in average time deposits combined with maturities of higher rate deposits resulted in the decrease of $0.7 million in interest expense for the quarter. The average cost of interest-bearing liabilities decreased by 37 basis points to 1.55% for the quarter ended June 30, 2010 from 1.92% for the same period in 2009. The decrease in interest expense was partially offset by an increase of $0.1 million in interest expense on borrowed funds. Average borrowed funds decreased $17.9 million or 7.7% for the quarter ended June 30, 2010 compared to the same period in 2009. The reduction in borrowed funds resulted from the $40.9 million decrease in Federal Home Loan Bank (FHLB) advances partially offset by the issuance of $25 million in subordinated debt during the fourth quarter of 2009 and the first quarter of 2010 that did not exist during this period in the prior year. The cost of borrowed funds increased by 50 basis points to 3.69% for the quarter ended June 30, 2010 as compared to the same period in 2009 primarily as a result of the higher interest rate on the subordinated debt as compared to the FHLB borrowings that were repaid.

Interest expense decreased $0.6 million, or 8.6%, to $11.7 million for the six months ended June 30, 2010 from $12.3 million for the six months ended June 30, 2009. The cost of interest-bearing deposits decreased $0.8 million to $7.7 million for the six months ended June 30, 2010 as compared to $8.5 for the six months ended June 30, 2009. The $77.9 million increase in average interest bearing deposits resulted from an increase of $52.6 million in average interest bearing demand deposits, $15.1 million in average savings deposits, and $10.2 million in average time deposits. The average cost of interest-bearing liabilities decreased by 19 basis points to 2.00% for the six months ended June 30, 2010 from 2.19% for the same period in 2009. This decrease was partially offset by an increase of $0.1 million in interest expense on borrowed funds. Average borrowed funds decreased $33.0 million, or 13.3%, for the six months ended June 30, 2010 compared to the same period in 2009. The reduction in borrowed funds resulted from the $40.9 million decrease in Federal Home Loan Bank (FHLB) advances partially offset by the issuance of $25 million in subordinated debt during the fourth quarter of 2009 and the first quarter of 2010 that did not exist during this period in the prior year. The cost of borrowed funds increased by 61 basis points to 3.76% for the six months ended June 30, 2010 as compared to 3.15% for the same period in 2009. The increase in the average cost of borrowed funds for the quarter and six months ended June 30, 2010 was primarily as a result of the higher interest rate on the subordinated debt that was issued in 2010 as compared to the FHLB borrowings that were repaid. The Company continues to pursue its strategy of replacing higher cost time deposits with lower cost time, savings and interest-bearing demand products and repay outstanding advances to maximize net interest income.

The net yield on average interest earning assets on a tax equivalent basis was 3.26% for the second quarter of 2010, a decrease of 35 basis points from 3.61% for the second quarter of 2009. The yield on interest-earning assets was 5.13%, a 48 basis points decrease from 5.61%, mainly due to the 65 basis point decrease in the yield on average investments and a 30 basis point reduction in the yield on average loans. The cost of interest-bearing liabilities decreased by 23 basis points to 1.95% for the quarter ended June 30, 2010 from 2.18% for the quarter ended June 30, 2009. The decrease was mainly due to the 37 basis point decrease in the cost of interest-bearing deposits to 1.55% from 1.92% for the second quarter of 2009, which was partly offset by a 50 basis point increase in the cost of borrowed funds to 3.69% from 3.19% over the same period. The net interest margin on a tax equivalent basis was 3.28% for the six months ended June 2010, a decrease of 42 basis points from 3.70% for the comparable period in 2009. The yield on interest-earning assets was 5.20%, a decrease of 51 basis points from 5.71%, mainly due to the 56 basis point decrease in the yield on average investments and a 28 basis point reduction in the yield on average loans. The cost of interest-bearing liabilities decreased by 19 basis points to 2.00% for the six months ended June 30, 2010 from 2.19% for the six months ended June 30, 2009. The decrease is mainly due to the 31 basis point decrease in the cost of interest-bearing deposits to 1.61% from 1.92% for the six months ended June 30, 2009, which was partly offset by a 61 basis point increase in the cost of borrowed funds to 3.76% from 3.15% over the same period.

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Average Balances

Net interest income represents the difference between income on interest-earning assets and expense on interest-bearing liabilities. Net interest income depends upon the relative amount of interest-earning assets and interest-bearing liabilities and the interest rate earned or paid on them. The following tables sets forth certain information relating to our consolidated statements of financial condition and consolidated statements of operations for the three and six month periods ended June 30, 2010 and 2009, and reflects the average yield on assets and average cost of liabilities for the periods indicated. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods shown. Average balances are derived from average daily balances. The yields include amortization of fees which are considered adjustments to yields.

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	Three months ended June 30, 2010 (Restated) Average Balance	Interest Income/ Interest	Average Interest Rate	Three months ended June 30, 2009 Average Balance	Interest Income/ Interest	Average Interest Rate
			(Dollars in thousands)			
Assets:						
Interest Earning assets:						
Commercial loans - taxable	$ 597,857	$ 7,518	5.04%	$ 645,555	$ 8,656	5.38%
Commercial loans - tax free	53,450	928	6.96%	49,888	876	7.04%
Mortgage loans	31,738	516	6.52%	34,533	692	8.04%
Installment loans	198,585	2,848	5.75%	214,593	3,122	5.84%
Total loans (1) (2)	881,630	$ 11,810	5.37%	944,569	$ 13,346	5.67%
Investment securities (taxable)	158,239	1,480	3.75%	161,226	2,037	5.07%
Investment securities (tax-free)	120,983	2,141	7.10%	110,543	1,928	7.00%
Total investment securities (1) (3)	279,222	$ 3,621	5.20%	271,769	3,965	5.85%
Interest-bearing deposits with banks	0	0	0.00%	0	0	0.00%
Federal funds sold	48,171	31	0.26%	23,041	13	0.23%
Total money market assets	48,171	31	0.26%	23,041	13	0.23%
Total interest-earning assets	1,209,023	15,462	5.13%	1,239,379	17,324	5.61%
Non-interest earning assets	108,490			86,201		
Total Assets	$ 1,317,513			$ 1,325,580		
Liabilities and Shareholders Equity:						
Interest-bearing liabilities:						
Interest-bearing demand deposits	330,127	863	1.05%	289,413	814	1.13%
Savings deposits	95,490	132	0.55%	80,220	145	0.72%
Time deposits over $100,000	231,499	901	1.56%	223,338	1,123	2.02%
Other time deposits	289,352	1,770	2.45%	309,201	2,240	2.91%
Total interest-bearing deposits	946,468	3,666	1.55%	902,172	4,322	1.92%
Borrowed funds	213,607	1,967	3.69%	231,513	1,841	3.19%
Total interest-bearing liabilities	1,160,075	5,633	1.95%	1,133,685	6,163	2.18%
Demand deposits	84,100			79,158		
Other liabilities	12,823			12,842		
Shareholders equity	60,515			99,895		
Total Liabilities and Shareholders Equity	$ 1,317,513			$ 1,325,580		
Net interest income/ interest rate spread (4)		$ 9,829	3.18%		$ 11,161	3.43%
Tax equivalent adjustment		(1,073)			(980)	
Net interest income, as reported		$ 8,756			$ 10,181	
Net Interest Margin (5)			3.26%			3.61%
Ratio of interest-earning assets as a percentage of interest-bearing liabilities			104.22%			109.32%

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(1) Interest income is presented on a tax equivalent basis using a 35% rate for 2010 and a 34% tax rate for 2009.

(2) Loans are stated net of unearned income and exclude non-performing loans.

(3) The yield for securities that are classified as available for sale is based on the average historical amortized cost.

(4) Interest rate spread represents the difference between the average yield on interest earnings assets and the average cost of interest bearing liabilities and is presented on a fully tax equivalent basis

(5) Net interest income as a percentage of total average interest earning assets.

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	Six months ended June 30, 2010 (Restated)			Six months ended June 30, 2009		
	Average Balance	Interest Income/ Interest	Average Interest Rate	Average Balance	Interest Income/ Interest	Average Interest Rate
			(Dollars in thousands)			
Assets:						
Interest-earning assets:						
Commercial loans - taxable	$ 608,946	$ 15,508	5.14%	$ 652,468	$ 17,598	5.44%
Commercial loans - tax free	54,829	1,894	6.97%	51,616	1,811	7.08%
Mortgage loans	32,606	1,073	6.64%	35,719	1,397	7.89%
Installment loans	201,968	5,805	5.80%	212,184	6,225	5.92%
Total loans (1) (2)	898,349	$ 24,280	5.45%	951,987	$ 27,031	5.73%
Investment securities (taxable)	159,071	3,071	3.89%	169,440	4,309	5.13%
Investment securities (tax-free)(1)	121,229	4,295	7.14%	109,608	3,805	7.00%
Total investment securities (1) (3)	280,300	$ 7,366	5.30%	279,048	8,114	5.86%
Interest-bearing deposits with banks	0	0	0.00%	0	0	0.00%
Federal funds sold	52,340	67	0.26%	11,603	13	0.23%
Total money market assets	52,340	67	0.26%	11,603	13	0.23%
Total interest-earning assets	1,230,989	31,713	5.20%	1,242,638	35,158	5.71%
Non-interest earning assets	105,531			84,089		
Total Assets	$ 1,336,520			$ 1,326,727		
Liabilities and Shareholders Equity:						
Interest-bearing liabilities:						
Interest-bearing demand deposits	342,131	1,895	1.12%	289,498	1,539	1.07%
Savings deposits	93,065	264	0.57%	77,994	269	0.70%
Time deposits over $100,000	236,031	1,834	1.57%	227,185	2,235	1.98%
Other time deposits	293,701	3,705	2.54%	292,306	4,424	3.05%
Total interest-bearing deposits	964,928	7,698	1.61%	886,983	8,467	1.92%
Borrowed funds	215,106	4,007	3.76%	248,029	3,879	3.15%
Total interest-bearing liabilities	1,180,034	11,705	2.00%	1,135,012	12,346	2.19%
Demand deposits	79,006			78,208		
Other liabilities	13,448			13,238		
Shareholders equity	64,032			100,269		
Total Liabilities and Shareholders Equity	$ 1,336,520			$ 1,326,727		
Net interest income/ interest rate spread (4)		$ 20,008	3.19%		$ 22,812	3.51%
Tax equivalent adjustment		(2,166)			(1,966)	
Net interest income, as reported		$ 17,842			$ 20,846	

Net interest margin (5)	3.28%	3.70%
Ratio of interest-earning assets as a percentage of interest-bearing liabilities	104.32%	109.48%

(1) Interest income is presented on a tax equivalent basis using a 35% rate for 2010 and a 34% tax rate for 2009.

(2) Loans are stated net of unearned income and exclude non-performing loans.

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(3) The yield for securities that are classified as available for sale is based on the average historical amortized cost.

(4) Interest rate spread represents the difference between the average yield on interest earnings assets and the average cost of interest bearing liabilities and is presented on a fully tax equivalent basis

(5) Net interest income as a percentage of total average interest earning assets.

The following table sets forth the dollar amount of changes in interest income, interest expense and net interest income between the three months ended June 30, 2010 and June 30, 2009.

	(000 s) Three Month Period Increase (Decrease) Due to Change in Compared with June 30, 2009			(000 s) Six Month Ended (Decrease) Due to Change in Compared with June 30, 2009		
	Volume	**Rate**	**Total**	**Volume**	**Rate**	**Total**
Interest income:						
Loans (taxable)	$ (937)	$ (651)	$ (1,588)	$ (1,622)	$ (1,212)	$ (2,834)
Loans (tax-free) (1)	61	(9)	52	113	(30)	83
Investment securities (taxable)	90	(647)	(557)	(76)	(1,162)	(1,238)
Investment securities (tax-free)(1)	181	32	213	403	87	490
Time deposits with banks and federal funds sold	14	4	18	46	8	54
Total interest income	(591)	(1,271)	(1,862)	(1,136)	(2,309)	(3,445)
Interest expense						
Interest-bearing demand deposits	112	(63)	49	273	83	356
Savings deposits	28	(41)	(13)	52	(57)	(5)
Time deposits	(103)	(589)	(692)	109	(1,229)	(1,120)
Borrowed funds	(142)	268	126	(515)	643	128
Total interest expense	(105)	(425)	(530)	(81)	(560)	(641)
Increase (decrease) in interest differential	$ (486)	$ (846)	$ (1,332)	$ (1,055)	$ (1,749)	$ (2,804)

(1) Changes in interest income and interest expense attributable to changes in both volume and rate have been allocated proportionately to changes due to volume and changes due to rate.

Provision for Loan and Lease Losses

A provision for loan and lease losses of $4.6 million and $9.7 million, respectively, was recorded for the three and six month periods ended June 30, 2010, compared to $7.3 million and 9.7 million, respectively, for the same periods in the prior year. The decrease of $2.7 million from the $7.3 million that was recorded in the quarter ended June 30, 2009 is as a result of substantial provisions taken as of December 31, 2009 and March 31, 2010 in connection with the restatement of the financial statements for those periods. During the six months ended June 30, 2010, non-performing loans increased $10.6 million to $36.5 million from $25.9 million at December 31, 2009. Net charge-offs for the six months ended June 30, 2010 totaled $4.9 million. Non-performing loans primarily consist of loans secured by real estate. Management closely monitors the loan portfolio and the adequacy of the Allowance for Loan and Lease Losses (ALLL) considering underlying borrower financial performance and collateral values and increasing credit risks. Future material adjustments may be necessary to the provision for credit losses and the ALLL if economic conditions or loan performance differ substantially from the assumptions management used in making its evaluation of the ALLL. The increase was primarily related to the increase in non-performing loans, attributable to the decline in the real estate market and the prolonged deterioration in the economy as well as our change in policy for determining the ALLL, including an enhanced loan impairment measurement process and historical loss analysis, described in more detail under Financial Condition - Allowance for Loan and Lease Losses .

Other Income

The Company recorded a loss in other income in the amount of $(0.9) million for the three months ended June 30, 2010, a decrease of $2.6 million from the $1.7 million earned during the comparable period in 2009. The decrease in other income was primarily due to a $2.6 million OTTI charge on PreTSLs and PLCMOs recorded in the three months ended June 30, 2010 compared to the $0.4 million charge for the three months ended June 30, 2009. In addition, gains on the sale of loans decreased $0.3 million during the same period, from $0.5 million to $0.2 million. Other income was $1.7 million for the six months ended June 30, 2010, a decrease of $2.4 million from the $4.1 million for the six months ended June 30, 2009. The decrease in other income was primarily due to a $2.9 million OTTI charge on PreTSLs and PLCMOs recorded during the six

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months ended June 30, 2010 compared to a $0.4 million charge during the same period in 2009.

Other Expense

Other expense was $8.5 million and $15.9 million for the three and six month periods ended June 30, 2010, respectively, compared to $7.3 million and $14.0, respectively, for the same periods in 2009. The $1.2 million and $1.9 million increases for the three and six months ended June 30, 2010, respectively, were primarily due to an increase in foreclosure and other real estate owned expense, increased salaries and benefits expense, and professional fees. The increase was partially offset by a reduction in FDIC assessments and data processing expenses.

Provision for Income Taxes

The Company anticipates that it will have a minimal tax provision or benefit until such time as it is able to reverse the deferred tax asset valuation allowance that it recorded in 2009, and accordingly did not record a provision or benefit during the quarter or six months ended June 30, 2010. The Company recorded a $0.5 million benefit and a $0.2 million provision for the three and six months ended June 30, 2009.

FINANCIAL CONDITION

Assets

Total assets were $1.31 billion, at June 30, 2010, a decrease of $60.1 million, or 4.4%, from $1.37 billion at December 31, 2009. Cash and cash equivalents decreased $3.6 million, or 4.2% during the six months ended June 30, 2010 to $82.7 million.

Securities

Securities available-for-sale, at fair value, were $253 million at June 30, 2010 and December 31, 2009, respectively. Sales and proceeds from calls, maturities, and pay downs totaled $43.1 million during the six months ended June 30, 2010.   Securities purchases amounted to $39.1 million and combined with a $3.1 million reduction in the unrealized loss on the portfolio, during the same period offsetting the decrease in the portfolio

The following table sets forth the carrying value of available-for-sale securities, which are carried at fair value, and held to maturity securities, which are carried at amortized cost, at the dates indicated:

	June 30, 2010 (as restated)	December 31, 2009 (as restated)	December 31, 2008
		(in thousands)	
U.S. Treasury securities and obligations of U.S. government agencies	$ 27,785	$ 27,089	$ 32,233
Obligations of state and political subdivisions	118,735	120,569	101,451
Collateralized mortgage obligations:			
Government sponsored agency	71,663	53,495	29,223
Private label	12,777	21,059	31,840
Residential mortgage-backed securities	19,788	27,442	30,061
Pooled Trust Preferred Senior Class	1,309	1,391	2,775
Pooled Trust Preferred Mezzanine Class	1,483	2,419	14,877
Corporate debt securities	394	356	4,274
Equity securities	1,018	1,025	974
Total	254,952	254,845	247,708

The following table sets forth the maturities of available-for-sale securities, based on amortized cost, at June 30, 2010 (in thousands) and the weighted average yields of such securities calculated on the basis of the cost and effective yields weighted for the scheduled maturity of each security.

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	Within One Year	Two - Five Years	Six - Ten Years	Over 10 Years	MBS	No Fixed Maturity	Total
US Treasury securities	$	$	$	$	$	$	$
Yield							
Obligations of U.S. government agencies			2,000	25,988			27,988
Yield			4.000%	4.668%			4.620%
Obligations of state and political subdivisions (1)		571	4,908	114,284			119,763
Yield		5.753%	6.177%	6.940%			6.903%
Corporate debt securities				500			500
Yield				0.963%			0.963%
CMOs							
Government sponsored agencies					70,349		70,349
Yield					3.623%		3.623%
Private label					14,872		14,872
Yield					6.076%		6.076%
Residential mortgage-backed securities					18,972		18,972
Yield					4.706%		4.706%
Pooled Trust Preferred Senior Class				3,855			3,855
Yield				1.455%			1.455%
Pooled Trust Preferred Mezzanine Class				9,618			9,618
Yield				0.658%			0.658%
Equity securities (2)						12,789	12,789
Yield						0.907%	0.907%
Total maturities	$ 0	571	6,908	154,245	104,193	12,789	278,706
Weighted Yields	0.000%	5.753%	5.547%	6.009%	4.170%	0.907%	5.076%

(1) Yields on state and municipal securities have been adjusted to a tax-equivalent basis using a 35% federal income tax rate.

(2) Yield presented represents 2010 actual return.

Other-Than-Temporary Impairment (OTTI)

Effective June 30, 2009 management adopted ASC Topic 320, Investments Debt and Equity Securities. Under this guidance, if management has no intent to sell the security and it is not more likely than not that the Company will be required to sell the security before recovery of its amortized cost, then other-than-temporary declines in the fair value of the debt security that are related to credit losses must be recognized in earnings as realized losses and those that are related to other factors are recognized in other comprehensive income. Numerous factors, including lack of liquidity for re-sales of certain investment securities, absence of reliable pricing information for investment securities, adverse changes in business climate, adverse actions by regulators, or unanticipated changes in the competitive environment could have a negative effect on our investment portfolio and may result in OTTI on the Company s investment securities in future periods.

On a quarterly basis, the Company evaluates its investment securities for OTTI. Unrealized losses on securities are considered to be OTTI when the Company believes the security s impairment is due to factors that could include the security issuer s inability to pay interest or dividends, the security issuer s potential for default, and/or other factors. When a held to maturity or available for sale debt security is assessed for OTTI, the Company must first consider (a) whether management intends to sell the security, and (b) whether it is more likely than not that the Company will be required to sell the security prior to recovery of its amortized cost basis. If one of these circumstances applies to a security, an OTTI loss is recognized in the statement of operations equal to the full amount of the decline in fair value below amortized cost. If neither of these circumstances applies to a security, but the Company does not expect to recover the entire amortized cost basis, an OTTI loss has occurred that must be separated into two categories: (a) the amount related to credit loss, and (b) the amount related to other factors. In assessing the level of OTTI attributable to credit loss, the Company compares the present value of cash flows expected to be collected with the amortized cost basis of the security. As discussed above, the portion of the total OTTI related to credit loss is recognized in earnings, while the amount related to other factors is recognized in other comprehensive income. The total OTTI loss is presented in the statement of operations, less the portion recognized in other comprehensive income. When a debt security becomes other than temporarily impaired, its amortized cost basis is reduced to reflect the portion of the total impairment related to credit loss.

To determine whether a security s impairment is other than temporary, management considers factors that include:

- the causes of the decline in fair value, such as credit problems, interest rate fluctuations, or market volatility.
- the severity and duration of the decline.
- the Company s ability and intent to hold equity security investments until they recover in

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value, as well as the likelihood of such a recovery in the near term.

- the Company s intent to sell security investments, or if it is more likely than not that the Company will be required to sell such securities before recovery of their individual amortized cost basis less any current-period credit loss.

For debt securities, the primary consideration in determining whether impairment is other-than-temporary is whether or not it is probable that current or future contractual cash flows have or may be impaired.

Based on the Company s evaluation at June 30, 2010, the Company has determined that the decreases in estimated fair value are temporary with the exception of eight PLCMOs and seven PreTSLs. The Company s discounted estimate of projected cash flows it expects to receive was less than the securities carrying value resulting in a credit-related impairment charge to earnings for the three and six months ended June 30, 2010 of $2.6 and $2.9 million, respectively.

OTTI of Private Label CMOs:

The following PLCMOs as of June 30, 2010 (in thousands as restated), were determined to be credit impaired either in the current or previous year resulting in a charge to earnings.

Description	Book Value	Fair Value	Unrealized gain/loss	S&P credit rating	Collateral type	Credit Impairment Quarter to Date	Credit Impairment Year to Date	Cumulative Credit Impairment
RAST 2006-A10 A5	$ 934	$ 654	$ (280)	D	ALT-A30	$	$ 5	$ 283
RAST 2006-A8 2A2	781	735	(46)	D	ALT-A30		7	421
CWALT 2007-7T2 A12	1,833	1,607	(226)	CC	ALT-A30			282
RALI 2006-QS 16 A10	867	711	(156)	D	ALT-A30		2	356
RALI 2006-QS4 A2	1,305	1,047	(258)	CC	ALT-A30	5	11	389
HALO 2007-1 3A6	1,392	610	(782)	CCC	WH-30			79
WMALT 2006-2 2CB	775	851	76	CCC	ALT-A30		33	467
PRIME 2006-1 1A1	1,854	1,495	(359)	CC	WH-30	4	4	45
Total	$ 9,741	$ 7,710	$ (2,031)			$ 9	$ 62	$ 2,322

The OTTI analysis relies on a review of the individual loans that provide the collateral for each security. This information is then used to develop default and severity assumptions over a future horizon for each security. The factors involved in constructing these assumptions are:

- MSA (Metropolitan statistical area), Geographic location
- HPI (Home Price Index) of specific MSAs
- Loan Balance

- Rate Premium
- LTV (both individual and combined if there are other loans)
- FICO
- Loan Purpose (cash-out versus purchase)
- Documentation
- Loan Structure
- Occupancy Status
- Property Type
- Borrower Payment History
- Historical delinquency and roll/curve rates

Adjustments are made to the default/severity vectors that may be warranted given the current environment. The Company then applies a fairness check to each vector to review whether future default/severity assumptions are in line with current observable performance. The data used to perform this analysis is provided by a third party provider and the individual loan performance.

Once the Company has default/severity assumptions for the underlying collateral (on a deal specific basis), the Company then has to understand how the timing of losses impacts each specific bond/tranche and how each cash flow changes over time.

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The default and severity vectors are modeled using a third party cash flow model and both total collateral and tranche specific cash flows are established. The Company then computes various metrics based on the resulting tranche cash flows:

- Total Collateral Principal Loss
- Total Tranche Loss
- Lifetime Tranche Yield
- Tranche Loss Timing

A security is considered to be other than temporarily impaired if the expected cash flow analysis results in a change of cash flow from the original expectation which indicates that there is the potential that all principal and/or interest may not be received. Information affecting cash flows and the impact on the collectability of principal and interest are evaluated on a monthly basis as received from service providers. The results are recognized through earnings as they become available. Information discovered subsequent to the balance sheet date but prior to the filing date is included in the OTTI analysis. As a result, the Company recorded a charge of $9 thousand and $62 thousand for the three and six months ended June 30, 2010 earnings for credit losses on its PLCMOs.

The table below illustrates the percentage of the current balance of each PLCMO that was delinquent, in foreclosure, in OREO and the trailing 3 month loss severity that was used in our June 30, 2010 OTTI calculations.

Description	**60-89 Days delinquent**	**90+ Days delinquent**	**Foreclosure**	**OREO**	**3 Month Severity**	**Projected Default Severity**
RAST 2006-A10 A5	4.08%	9.03%	13.91%	2.30%	57.24%	36.52%
RAST 2006-A8 2A2	3.10%	6.89%	14.32%	3.05%	64.96%	58.00%
CWALT 2007-7T2 A12	3.04%	19.52%	15.00%	2.54%	22.67%	57.94%
RALI 2006-QS 16 A10	2.78%	7.77%	17.22%	2.11%	57.64%	63.67%
RALI 2006-QS4 A2	3.10%	5.63%	11.54%	1.49%	52.98%	46.99%
HALO 2007-1 3A6	1.71%	10.69%	7.09%	0.85%	57.45%	48.10%
WMALT 2006-2 2CB	1.74%	8.69%	11.57%	1.90%	72.27%	72.10%
PRIME 2006-1 1A1	1.05%	7.84%	5.42%	1.99%	28.75%	40.00%

OTTI of Pooled Trust Preferred Collateralized Debt Obligations:

As of June 30, 2010, the book value of our PreTSLs totaled $13.5 million with an estimated fair value of $2.8 million and is comprised of seven securities each of which are collateralized by debt issued by bank holding companies and insurance companies. The Company holds one senior tranche and six mezzanine tranches below investment grade. All of the securities have been downgraded below investment grade. At the time of initial issue, no more than 5% of any pooled security consisted of a security issued by any one institution. As of June 30, 2010, six of these securities had no excess subordination and one had excess subordination of 8.04% of the current performing collateral. Excess subordination is the amount by which the underlying performing collateral exceeds the outstanding bonds in the current class plus all senior classes. It can also be referred to as credit enhancement. As deferrals and defaults of underlying issuers occur, the excess subordination is reduced or eliminated, increasing the risk of the security experiencing principal or interest shortfalls. Conversely, subordination can be increased as collateral transitions from non-performing to performing. The coverage ratio, or overcollateralization, of a specific security measures the rate of performing collateral to a given class of notes. It is calculated by dividing the performing collateral in a transaction by the current balance of the class of notes plus all classes senior to that class.

The following table presents information about the Company s collateral and subordination for its PreTSLs as of June 30, 2010 (as restated):

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(In thousands) Deal	Performing collateral	Bonds outstanding	Excess/ insufficient collateral	Coverage ratio	Excess subordination	Credit Impairment Quarter to Date	Credit Impairment Year to Date	Credit Impairment Life to Date
PreTSL VIII	$ 235,300	$ 394,861	$ (159,561)	59.59%	N/A	$ 44	$ 44	$ 2,964
PreTSL IX	313,520	337,880	(24,360)	92.79%	N/A			1,680
PreTSL X	282,750	383,171	(100,421)	73.79%	N/A	133	137	2,782
PreTSL XI	426,995	479,847	(52,852)	88.99%	N/A	544	544	3,330
PreTSL XIX	540,135	550,574	(10,439)	98.10%	N/A	1,036	1,203	2,268
PreTSL XXVI	689,200	637,920	51,280	108.04%	8.04%			251
PreTSL XXVIII	281,850	308,278	(26,428)	91.43%	N/A	790	912	7,954
Total						$ 2,547	$ 2,840	$ 21,229

The following list details information for each of the Company s PreTSLs as of June 30, 2010:

Deal		Book value	Fair value	Unrealized gain/loss	Moody s / Fitch ratings	Current number of performing issuers	Actual deferrals / defaults as a % of current collateral	Expected future default rate
PreTSL VIII	Mezzanine	$ 36	$ 1	$ (35)	C / C	23	44.60%	3.16%
PreTSL IX	Mezzanine	1,320	275	(1,045)	Ca / C	36	30.30%	1.60%
PreTSL X	Mezzanine	218	5	(213)	C / C	37	43.50%	2.34%
PreTSL XI	Mezzanine	1,670	216	(1,454)	Ca / C	48	29.00%	2.57%
PreTSL XIX	Mezzanine	4,907	970	(3,937)	B3 / B	56	22.90%	2.19%
PreTSL XXVI	Senior	3,855	1,310	(2,545)	B1 / B	55	28.50%	1.87%
PreTSL XXVIII	Mezzanine	1,468	15	(1,453)	Ca / CC	44	21.90%	1.90%
		$ 13,474	$ 2,792	$ (10,682)				

The Company s PreTSLs are measured for OTTI within the scope of ASC Topic 325 by determining whether an adverse change in estimated cash flows has occurred. Determining whether there has been an adverse change in estimated cash flows from the cash flows previously projected involves comparing the present value of remaining cash flows previously projected against the present value of the cash flows estimated at June 30, 2010. The Company considers the discounted cash flow analysis to be our primary evidence when determining whether credit related OTTI exists.

Results of a discounted cash flow test are significantly affected by variables such as the estimate of the probability of default, estimates of future cash flows, discount rates, prepayment rates and the creditworthiness of the underlying issuers. The following provides additional information for each of these variables:

- Probability of Default An issuer level approach is used to analyze each security and default and recovery assumptions are based on the credit quality of the underlying issuers (generally, bank holding companies or insurance companies). Each bank issuer is evaluated based upon an examination of the trends in its earnings, net interest margin, operating efficiency, liquidity, capital position, level of nonperforming loans to total loans, apparent sufficiency of loan loss reserves, Texas ratio and whether the bank received TARP monies. From this information, each issuer bank that is currently performing is assigned a category of Good, Average, Weak, or Troubled. Default rates are then assigned based upon the historical performance of each category. Additionally, because the information available to the Company regarding the underlying insurance company issuers is more limited than for bank issuers, rather than performing an analysis of each such issuer s results and assigning insurance company issuers to these same categories, the Company uses the Moody s one year long-term default rate assumption for insurance companies. The historical default rates used in this analysis are:

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Default Rate

Category	Year 1	Year 2	Year 3	Thereafter
Good	0.50%	0.60%	0.60%	0.40%
Average	1.80%	2.30%	2.30%	1.50%
Insurance	1.00%	1.20%	1.20%	0.80%
Weak	5.80%	7.20%	7.20%	4.80%
Troubled	9.70%	12.20%	12.20%	8.10%

Each issuer in the collateral pool is assigned a probability of default for each year until maturity. Banks currently in default or deferring interest payments thus far are assumed to default immediately. A zero percent projected recovery rate is applied to defaults. The probability of default is updated quarterly based upon changes in the creditworthiness of each underlying issuer. Timing of defaults and deferrals has a substantial impact on each valuation. As a result of this analysis, each issuer is assigned an expected default rate specific to that issuer.

- Estimates of Future Cash Flows While understanding the composition and characteristics of each bank issuer is important in evaluating the security, certain issuers have a disproportionate impact (both positive and negative) based upon other attributes, such as the interest rate payable by each issuer. Each credit is assessed independently, and the timing and nature of each issuer s performance is assessed. Once assessed, the expected performance of each issuer is applied to a structural cash flow model. Due to the complexity of these transactions, the expected performance of each unique issuer requires an adherence to the governing documents of the securitization to derive a cash flow. A model produced by third party is utilized to assist in determining cash flows. Utilization of third party cash flow modeling to derive cash flows from assumptions is a market convention for these types of securities.

- Discount Rate The Company is discounting projected cash flows based upon its discount margin defined at the time of purchase, which constitutes a spread over 3-month LIBOR plus credit premium, consistent with our pre-purchase yield.

- Prepayment Rate Lack of liquidity in the market for PreTSL securities, credit rating downgrades and market uncertainties related to the financial industry are factors contributing to the impairment of these securities. During the early years of PreTSL securities, prepayments were common as issuers were able to refinance into lower cost borrowings. Since the middle of 2007, however, this option has all but disappeared and the Company is operating in an environment which makes early redemption of these instruments unlikely. Accordingly, the Company has assumed zero prepayments when modeling the cash flows of these securities. The Company will reevaluate its prepayment assumptions from time to time as appropriate. The Company performed a sensitivity analysis using 1% and 3% prepayment assumptions. As a result of this analysis, the Company determined that employing a 1% and a 3% prepayment assumption rather than assuming zero prepayments would have resulted in an additional credit loss of approximately $859 thousand and $894 thousand, respectively, to the $2.9 million impairment charge taken during the first six months of 2010. Credit losses would increase as a result of an increase in the prepayment assumption because prepayments reduce the amount of excess subordination that would be available to absorb expected losses.

- Credit Analysis A quarterly credit evaluation is performed for each of the securities. While the underlying core component of these securities are the credit characteristics of the underlying issuers , typically banks, other characteristics of the securities and, issuers are evaluated and stressed to determine cash flow. These include but are not limited to interest rate payable by each issuer, certain derivative contracts, default timing, and interest rate volatility. Issuer level credit considers all evidence available to us and includes the nature of the issuer s business, its years of operating history, corporate structure, loan composition, loan concentrations, deposit mix, asset growth rates, geographic footprint and local environment. Depending upon the security, and its place in the capital structure, certain analytical assumptions are isolated with greater scrutiny. The core analysis for each specific issuer focuses on profitability, return on assets, shareholders equity, net interest margin, credit quality ratios, operating efficiency, capital adequacy and liquidity.

The Company has evaluated our PreTSLs and PLCMOs considering all available evidence, including information received after the balance sheet date but before the filing date, and determined that the estimated projected cash flows are less than the securities carrying value, resulting in an impairment charge to earnings for the three and six months ended June 30, 2010 of $2.5 million and $2.9 million, respectively.

The table below provides a cumulative roll forward of credit losses recognized (dollars in thousands):

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Other-Than-Temporarily Impaired Securities

Beginning Balance, January 1, 2010	$	20,649
Credit losses on debt securities for which OTTI was not previously recognized		
Additional credit losses on debt securities for which OTTI was previously recognized		2,902
Ending Balance, June 30, 2010	$	23,551

Investments in FHLB and FRB stock, which have limited marketability, are carried at cost in Other Assets and totaled $12.1 million and $11.8 million at June 30, 2010 and December 31, 2009, respectively. Management noted no indicators of impairment for the FHLB of Pittsburgh at June 30, 2010.

Loans

Net loans decreased $55.2 million, or 6.0% during the six months ended June 30, 2010 to $862.3 million from $917.5 million at December 31, 2009. The net decrease in loans is primarily the result of net repayments in the amount of $45.7 million, charge-offs in the amount of $4.9 million, transfers to OREO in the amount of $3.9 million and a $4.9 million increase in the ALLL in the current quarter. Loan demand has remained at reduced levels due to the current economic environment.

Net loans represented 66.0% of total assets as of June 30, 2010, compared to 67.2% of total assets as of December 31, 2009. The Company noted nominal increases in residential real estate loans and other loans. Increases in these categories were offset by decreases in all the other categories of loans. Historically, commercial lending activities have represented a significant portion of the Company s loan portfolio. This includes commercial and industrial loans and commercial real estate loans.   Furthermore, from a collateral standpoint, a majority of the Company s loan portfolio consisted of loans secured by real estate. Real estate secured loans as of percentage of total net loans has increased from 60.3% of the loan portfolio as of December 31, 2009 to 60.8% of the loan portfolio as of June 30, 2010.

Commercial and industrial loans decreased $12.7 million or 5.8%, from $220.8 million as of December 31, 2009 to $208.1 million as of June 30, 2010. Commercial loans consist primarily of equipment loans, permanent working capital financing, revolving lines of credit and loans secured by cash and marketable securities. The decrease was primarily a reduction in borrowings under revolving line of credit facilities within the portfolio.

Loans secured by commercial real estate decreased $16.9 million, or 5.3%, to 300.5 million as of June 30, 2010 from $317.4 million as of December 31, 2009. Commercial real estate loans include long-term commercial mortgage financing, construction loans and land development loans, and are primarily secured by first or second lien mortgages. The decrease in commercial real estate loans is primarily attributable to some large payoffs, along with charge-offs and transfers to OREO.

Residential real estate loans totaled $140.5 million as of June 30, 2010. This represents an increase of $3.0 million, or 2.2%, from $137.5 million as of December 31, 2009. The components of residential real estate loans include fixed rate mortgage loans primarily held for sale in the secondary market, which represent less than one percent of the overall loan portfolio, and home equity loans and lines of credit. The Company continues to adhere to a philosophy of underwriting fixed rate purchase and refinance residential mortgage loans that are generally then sold in the secondary market to reduce interest rate risk and provide funding for additional loans.

Installment loans decreased $11.1 million during the six months ended June 30, 2010, or 8.6%, from $128.4 million as of December 31, 2009 to $117.3 million as of June 30, 2010. The decrease in installment loans is due primarily to decline in the Company s indirect auto loan portfolio.

All other loans, which include obligations of state and municipal governments, totaled $39.5 million as of June 30, 2010, an increase of $2.5 million, or 6.7%, from $37.0 million as of December 31, 2009. The continued economic slowdown has reduced loan demand.

Major classifications of loans are summarized as follows (in thousands):

	June 30, 2010 (as restated)	December 31, 2009 (as restated)
Residential real estate	$ 140,501	$ 137,520
Commercial real estate	300,517	317,408
Commercial and industrial loans	208,123	220,849
Construction Loans	83,281	98,383
Installment loans	117,308	128,392
Other loans	39,495	37,013
Gross loans	889,225	939,565
Less: Allowance for loan and lease losses	(27,378)	(22,458)
Unearned discount	(261)	(298)
Plus: Loan fees	741	707
Net loans	$ 862,327	$ 917,516

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Asset Quality

The Company manages credit risk through the efforts of loan officers, the loan review function, and the Loan Quality as well as the ALLL management committees and oversight from the board of directors, along with the application of policies and procedures designed to foster sound underwriting and credit monitoring practices. The Company continually evaluates this process to ensure it is reacting to problems in the loan portfolio in a timely manner. Although, as is the case with any financial institution, a certain degree of credit risk is dependent in part on local and general economic conditions that are beyond the Company s control.

Under the Company s risk rating system, loans rated as special mention, substandard, doubtful or loss are reviewed regularly as part of the Company s risk management practices. The Company s Loan Quality Committee, which consists of key members of senior management and credit administration, meets monthly or more often, as necessary, to review individual problem credits and workout strategies and makes reports to the Board of Directors.

A loan is considered impaired when it is probable that the Bank will be unable to collect all amounts due (including principal and interest) according to the contractual terms of the note and loan agreement. For purposes of the Company s analysis, loans which are identified as troubled debt restructures (TDRs) or are non-accrual substandard or doubtful loans are considered impaired. Impaired loans are analyzed individually for the amount of impairment. The Company generally utilizes the fair value of collateral method for collateral dependent loans, which make up the majority of the Company s impaired loans. A loan is considered to be collateral dependent when repayment of the loan is anticipated to come from the liquidation of the collateral held. For loans that are secured by real estate, external appraisals are obtained annually, or more frequently as warranted, to ascertain a current market value so that the impairment analysis can be updated. Should a current appraisal not be available at the time of impairment analysis, other sources of valuation such as current letters of intent, broker price opinions or executed agreements of sale may be used. For non-collateral dependent loans, the Company measures impairment based on the present value of expected future cash flows, net of disposal costs, discounted at the loan s original effective interest rate.

Loans are placed on nonaccrual when a loan is specifically determined to be impaired or when management believes that the collection of interest or principal is doubtful. This is generally when a default of interest or principal has existed for 90 days or more, unless such loan is well secured and in the process of collection or management becomes aware of facts or circumstances that the loan would default before 90 days. When the interest accrual is discontinued, all interest income related to unpaid interest is reversed and charged back against current earnings. Any cash payments subsequently received are applied, first to the outstanding loan amounts, then to the recovery of any charged-off loan amounts. Any excess is treated as a recovery of lost interest. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Loans to borrowers that are experiencing financial difficulty that are modified and result in the Company granting concessions to the borrower are classified as troubled debt restructurings (TDRs) and are considered to be impaired. Concessions granted under a troubled debt restructuring generally involve a reduction of the rate or an extension of a loan s stated maturity date. Nonaccrual troubled debt restructurings are restored to accrual status if principal and interest payments, under the modified terms, are current for six consecutive months after modification.

Non-performing loans and OREO are monitored on an ongoing basis as part of the Company s loan review process and through the Loan Quality Committee. Additionally, work-out efforts continue and are actively monitored for non-performing loans and OREO. Potential loss on non-performing loans and OREO is generally evaluated by comparing the outstanding loan balance to the fair market value of the pledged collateral.

Under the fair value of collateral method, the impaired amount of the loan is deemed to be the difference between the loan amount and fair value of the collateral, less the estimated costs to sell. For the Company s calculations on a real estate secured loans, a factor of 10% is generally utilized to estimate costs to sell, which is based on typical cost factors, such as a 6% broker commission, 2% transfer taxes, and 2% various other miscellaneous costs associated with the sales process. If the valuation indicates that the market value has deteriorated below the carrying value of the loan, either the entire loan is written off or the partial difference between the market value and the principal balance is charged off unless there are material

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mitigating factors to the contrary. For loans which are considered to be impaired, but for which the value of the collateral (minus costs to sell) exceeds the loan value, the impairment is considered to be zero.

At June 30, 2010 and December 31, 2009 the loans on nonaccrual totaled $36.5 million and $25.9 million, respectively. OREO is included in other assets and totaled $15 million and $11.2 million at June 30, 2010 and December 31, 2009, respectively. The total recorded investment in loans past due ninety days or more and still accruing interest amounted to $0 and $117,000 at June 30, 2010 and December 31, 2009, respectively. The total recorded investment in impaired loans amounted to $48.5 million and $36.7 million at June 30, 2010 and December 31, 2009, respectively. At June 30, 2010, OREO consisted of sixteen properties with seven of the properties comprising $14.3 million or 96% of the balance. Troubled debt restructurings totaling $12.0 million were all performing in accordance with the restructured agreements as of June 30, 2010.

The additional interest income that would have been earned on nonaccrual and restructured loans outstanding at June 30, 2010 and June 30, 2009 in accordance with their original terms approximated $1.3 million and $1.2 million, respectively. There was no interest income recognized on non-performing loans for cash payments received during the three and six months ended June 30, 2010 and June 30, 2009.

The following schedule reflects various non-performing lending categories as the dates noted (in thousands):

		June 30, 2010 (as restated)		December 31, 2009 (as restated)
Impaired/Nonaccrual loans	$	36,483	$	25,865
Loans past due 90 days or more and still accruing		0		117
Total Non-Performing Loans		36,483	$	25,982
Other Real Estate Owned		15,022	$	11,184
Total Non-Performing Assets		51,505	$	37,166
Performing TDRs		11,998	$	10,743
ALLL related to impaired loans	$	8,688	$	3,982

		June 30, 2010 (as restated)		December 31, 2009 (as restated)
Loans with no allocated allowance for loan and lease losses	$	12,759	$	11,348
Loans with allocated allowance for loan and lease losses		35,722		25,260
Total Balance of loans considered impaired	$	48,481	$	36,608

The average balance of impaired loans was $44.2 million and $45.4 million for the six months ended June 30, 2010 and 2009, respectively. The Company recorded $396 thousand and $448 thousand of interest income on impaired loans for the six months ended June 30, 2010 and six months ended June 30, 2009, respectively.

In the first six months of 2010, total non-performing assets increased $14.3 million, from $37.2 million as of December 31, 2009 to $51.5 million as of June 30, 2010, as the effects of the severe and prolonged economic downturn continued to impact individual and business customers of the Company. Included in non-performing assets are nonaccrual loans which increased $10.6 million during the year. The increase in nonaccrual loans is primarily centered in commercial real estate loans, including a concentration in land development and construction loans. Continued downturn in the real estate market could lead to additional increases in impaired loans.

The Company has historically participated in loans with other financial institutions, the majority of which have been loans originated by financial institutions located in the Company s general market area. Over the past six years, the Company has participated in seven (7) commercial real estate loans with a financial institution that was headquartered in Minneapolis, Minnesota. The majority of these loans were for out of market commercial real estate projects. Two (2) projects were located in Pennsylvania, one (1) project was located in New York and the remaining four (4) projects were located in Florida. The Company s original aggregate commitment for these various loans totaled approximately $34 million. Two of these loans, one local Pennsylvania project and the New York project, have been paid in full. The remaining Pennsylvania loan continues to pay as agreed but is rated as Substandard . The remaining outstanding balance under these Florida participations totals $6.9 million. These credits are all classified as either non-performing or as OREO. All of these credits have been written down to the current fair market value of each respective property.

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Non-performing loans increased $10.6 million from $25.9 million as of December 31, 2009 to $36.5 million as of June 30, 2010. The decline in the real estate market and the prolonged deterioration in the economy contributed to an increase in non-performing loans and net charge-offs, primarily in the commercial real estate portfolio concentrated in land development loans. The increase in non-performing loans is centered in a few large credits, all of which are secured by real estate collateral. Four loans that the Company placed on non-accrual status in the six months ended June 30, 2010 accounted for the $10.6 million increase. The Company ordered and received independent third-party appraisals at the time the loans were placed on non-accrual status and recorded direct charge-offs in the amount of $2.2 million, which it determined was appropriate based on the valuations contained in the appraisals.

Loans to borrowers that are experiencing financial difficulty that are modified and result in the Company granting concessions to the borrower are classified as troubled debt restructurings (TDRs) and are considered to be impaired. Concessions granted under a troubled debt restructuring generally involve a reduction of the rate or an extension of a loan s stated maturity date. Nonaccrual troubled debt restructurings are restored to accrual status if principal and interest payments, under the modified terms, are current for six consecutive months after modification. TDRs increased $1.3 million to $12.0 million at June 30, 2010 compared to December 31, 2009.

Reclassifications of performing loans to non-accrual during the first six months of 2010 primarily consisted of four (4) large credits totaling $13.3 million. These credits were:

• $6.8 million This credit represents various time loans secured by land; this credit was written down to $6.5 million as of June 30, 2010. Additionally, $1.1 million of the allowance for loan losses is allocated to this credit.

• $2.2 million This credit represents the non-sold portion of a government guaranteed loan secured by commercial real estate; this credit was written down to $1.1 million as of June 30, 2010. Additionally, $109 thousand of the allowance for loan losses is allocated to this credit.

• $2.1 million This credit represents a time loan secured by residential and commercial real estate; this credit was written down to $1.6 million as of June 30, 2010. Additionally, $147 thousand of the allowance for loan losses is allocated to this credit.

• $2.2 million This credit represents a term loan and line of credit secured by commercial real estate; this credit was written down to $1.8 million as of June 30, 2010. Additionally, $180 thousand of the allowance for loan losses is allocated to this credit.

In addition, these four credits plus eight credits reclassified in prior years constituted 85.5% of total non-performing loans as of June 30, 2010. The eight credits reclassified prior to 2010 were:

• $5.0 million This credit represents a land development loan secured by a residential subdivision located outside of the Company s primary market area; this credit was written down to $2.6 million as of June 30, 2010. Additionally, $260 thousand of the allowance for loan losses is allocated to this credit.

- $4.8 million This credit represents a land development loan secured by a residential subdivision located outside of the Company s general market area; this credit was written down to $3.3 million as of June 30, 2010. Additionally, $328 thousand of the allowance for loan losses is allocated to this credit.

- $11.1 million This credit represents a land development loan secured by a residential subdivision. This credit was written down to $5.3 million as of June 30, 2010. Additionally, $534 thousand of the allowance for loan losses is allocated to this credit.

- $2.5 million This credit represents a participation in an out of area real estate bridge loan made to a non-Bank related customer, secured by real estate. Due to sufficient collateral value, no allocation is provided for this credit in the allowance for loan losses.

- $3.2 million This credit represents a commercial construction loan secured by real estate; this credit was written down to $2.0 million as of March 31, 2010. Additionally, $196 thousand of the allowance for loan losses is allocated to this credit. This credit is guaranteed by two former members of the Company s Board of Directors.

- $1.2 million This credit represents a commercial mortgage loan secured by commercial real estate. Due to sufficient collateral value, no allocation is provided for this credit in the allowance for loan losses.

- $1.7 million This credit represents a participation in an out of area real estate bridge loan made to a non-Bank related customer, secured by real estate. Due to sufficient collateral value, no allocation is provided for this credit in the allowance for loan losses.

- $1.6 million This credit represents a commercial mortgage loan secured by commercial real estate. $160 thousand of the allowance for loan losses is allocated to this credit.

The following table outlines delinquency within the Company s loan portfolio is provided below.

	June 30, 2010 (as restated)	**December 31, 2009 (as restated)**
30-59 days	0.61%	.35%
60-89 days	0.40%	.05%
90 + days	0%	.01%
Non-Accrual	4.10%	2.75%
Total Delinquencies	5.11%	3.16%

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The Company attempts to limit its exposure to concentrations of credit risk by diversifying its loan portfolio and closely monitoring any concentrations of credit risk. The commercial real estate and commercial construction portfolios comprise $380.0 million (as restated) or 44.1% of net loans at June 30, 2010. In addition, the company had $46.3 million or 5.4% of net loans secured by properties outside of Pennsylvania. Geographic concentrations exist because the Company provides a full range of banking services, including commercial, consumer and mortgage loans to individuals and corporate customers in its market areas in Pennsylvania. Management believes underwriting guidelines and ongoing review by loan review mitigates these risks.

Allowance for Loan and Lease Losses

The ALLL represents management s estimate of probable loan losses inherent in the loan portfolio. The ALLL is analyzed in accordance with GAAP and varies from period to period based on management s evaluation of the adequacy of the ALLL in relation to the risks inherent in the loan portfolio. Effective for 2009, the ALLL methodology was revised to include an enhanced measurement process. Enhancements were also made to the historical loss analysis including an expanded and a more comprehensive loan pool analysis including a more detailed qualitative adjustment factors analysis.

In its evaluation, management considers qualitative factors such as changes in lending policies and procedures, changes in concentrations of credit, the nature and volume of the portfolio, the volume and severity of delinquencies, classified and non-accrual loans, competition, legal and regulatory environments, management capabilities, current local and national economic trends, loan review methodology and Board of Directors oversight, as well as various other factors. Consideration is also given to examinations performed by regulatory authorities and loan review.

The downturn in the economy has resulted in increased loan delinquencies, defaults and foreclosures, primarily in the commercial real estate portfolio. Nonaccrual loans increased by $10.6 million to $36.5 million at June 30, 2010 from $25.9 million at December 31, 2009. Four loans that the Company placed on non-accrual status in the six months ended June 30, 2010 accounted for the $10.6 million increase in non-accrual loans. The Company recorded direct charge-offs in the amount of $2.2 million on these loans when they were placed on non-accrual status. Management monitors the loan portfolio on an ongoing basis with emphasis on the declining real estate market and a weakened economy and the effect on repayment. Adjustments to the ALLL are made based on management s assessment of these trends and the factors outlined above. Evaluations are intrinsically subjective, as the results are estimated based on management knowledge and experience and are subject to interpretation and modification as information becomes available or as future events occur. The Company recorded a provision for loan and lease losses of $9.7 million for the six months ended June 30, 2010, which was substantially the same as the provision recorded in the same period in the prior year. The ALLL increased from $22.5 million at December 31, 2009 to $27.4 million at June 30, 2010. The ratio of ALLL to total non-performing loans decreased to 75.0% at June 30, 2010 from 86.7% at December 31, 2009, whereas the ratio of the ALLL to gross loans increased to 3.1% at June 30, 2010 compared to 2.4% at December 31, 2009. These changes were primarily the result of loans pay-offs, charge-offs and transfers to OREO resulting in the contraction of the overall loan portfolio.

	Three months ended June 30,		Six months ended June 30,	
	2010 (as restated)	**2009**	**2010 (as restated)**	**2009**
Balance, beginning of period	$ 25,505	$ 11,278	$ 22,458	$ 9,150
Recoveries credited to allowance	43	43	103	87
Provision for loan and lease losses	4,574	7,250	9,682	9,710
Total	30,122	18,571	32,243	18,947
Losses charged to allowance	2,744	8,053	4,865	8,429

Balance, end of period	$	27,378	$	10,518	$	27,378	$	10,518

All doubtful, non-accrual substandard loans and troubled debt restructurings are considered to be impaired and are analyzed individually to determine the amount of impairment. Circumstances such as construction delays, declining real estate values, and the inability of the borrowers to make scheduled payments have resulted in these loan relationships being classified as impaired. The fair value of collateral method is generally used for this measurement unless the loan is non-collateral dependent in which case, a discounted cash flow analysis is performed. Appraisals are received at least annually to ensure that adequate impairment measurements reflect current market conditions. Should a current appraisal not be available at the time of impairment analysis, other valuation sources including current letters of intent, Broker Price Opinions or executed agreements of sale may be used. Only downward adjustments are made based on these supporting values. Included in all impairment calculations is a cost to sell adjustment of approximately 10%, which is based on typical cost factors, including a 6% broker commission, 2% transfer taxes and 2% various other miscellaneous costs associated with the sales process. The ALLL analysis is adjusted for subsequent events that may arise after the end of the reporting period but before the financial reports are filed.

Some of the charge-offs resulted from participations in a small number of out of area real estate loans made to non-Bank customers. At the time these loans were issued, the Bank was looking to expand into other market areas and spread risk. The decision to participate in these credit facilities was based upon perceived favorable market conditions, substantial equity positions, excellent loan to value ratios, fee income, and above average interest rates at the time these loans were approved. Management has since made a decision to discontinue participation in out of area loans. See further discussion under Asset Quality .

The Company s ALLL consists of both specific and general components. At June 30, 2010, the ALLL that related to impaired loans, the guidance for which is provided by ASC 310 *Impairment of a Loan* (ASC 310), was $8.7 million or 31.7% of total ALLL, which reflects an increase from the specific allowance of $4.0 million at December 31, 2009 commensurate with the increase in impaired loans to $48.5 million at June 30, 2010 from $36.7 million at December 31, 2009. A general allocation of $18.7 million was calculated for loans analyzed under ASC 450 *Contingencies* (ASC 450), which represented 68.3% of the total ALLL of $27.4 million and reflects a small increase from the general allocation of $18.5 million at December 31, 2009. The ratio of the ALLL to total loans at June 30, 2010 and December 31, 2009 was 3.1% and 2.4%, respectively, based on total loans of $889.2 million and $939.6 million, respectively. The ALLL increased to $27.4 million at June 30, 2010 from $22.5 million at December 31, 2009 due primarily to the market conditions and other items noted above.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at the amount of unpaid principal, net of unearned interest, deferred loan fees and costs, and reduced by the ALLL. The ALLL is established through a provision for loan losses charged to earnings. Interest on loans is recognized using the effective interest method in accordance with GAAP and credited to income from operations based upon principal amounts outstanding.

Loans are placed on nonaccrual when a loan is specifically determined to be impaired or when management believes that the collection of interest or principal is doubtful. This is generally when a default of interest or principal has existed for 90 days or more, unless such loan is well secured and in the process of collection, or when management becomes aware of facts or circumstances that the loan would default before 90 days. When the interest accrual is discontinued, all unpaid interest is reversed and charged back against current earnings. Any cash payments received are applied, first to the outstanding loan amounts, then to the recovery of any charged-off loan amounts. Any excess is treated as a recovery of lost interest. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

In the Company s historical loss analysis, loans are analyzed by industry concentration, loan type and risk rating. Management measures the effects of various qualitative factors on each of these loan segments. The factors include changes in lending policies and procedures, changes in concentrations of credit, changes in the nature and volume of the portfolio, changes in the volume and severity of delinquencies, classified and nonaccrual loans, changes in competition and legal and regulatory environments, management capabilities, current local and national economic trends, knowledge of customer base and changes in loan review methodology/board of director oversight. Consideration is also given to examinations performed by regulatory authorities.

Evaluations are intrinsically subjective, as the results are estimated based on management knowledge and

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experience and are subject to interpretation and modification as information becomes available or as future events occur. Management monitors the loan portfolio on an ongoing basis with emphasis on the declining real estate market and a weakened economy and affect on repayment. Adjustments to the ALLL are made based on management s assessment of the factors noted above.

Management actively manages impaired loans in an effort to reduce loan balances by working with customers to develop strategies to resolve borrower issues, through sale or liquidation of collateral, foreclosure, and other appropriate means. If real estate values continue to decline, it is more likely that we would be required to further increase our provision for loan and lease losses, which in turn, could result in reduced earnings.

The following table outlines the changes in the allowance for loan and lease losses for the three months and six months ended June 30, 2010 and 2009.

	For the three months ended June 30,		For the six months ended June 30,	
(Dollars in thousands)	**2010 (restated)**	**2009**	**2010 (restated)**	**2009**
Balance at beginning of period	$ 25,505	$ 11,278	$ 22,458	$ 9,150
Provision for loan losses	4,574	7,250	9,682	9,710
Loans charged-off:				
Residential Real estate		(171)		(348)
Commercial real estate	(1,820)	(6,113)	(2,248)	(6,258)
Commercial and industrial loans	(19)	(1,565)	(80)	(1,565)
Construction loans	(734)		(2,054)	
Installment loans	(27)	(243)	(181)	(243)
Other loans charged-off	(144)	39	(302)	(15)
Total loans charged-off	(2,744)	(8,053)	(4,865)	(8,429)
Recoveries:				
Residential real estate	9	(36)	13	3
Commercial real estate	17	30	27	33
Commercial and industrial loans	4		9	
Construction loans				
Installment loans	12	45	52	45
Other loans	1	4	2	6
Total recoveries	43	43	103	87
Net charge-offs	(2,701)	(8,010)	(4,762)	(8,342)
Balance at end of period	$ 27,378	$ 10,518	$ 27,378	$ 10,518
Ratio of net charge-offs during the period as a percentage of average loans outstanding during the period	0.31%	0.85%	0.53%	0.88%
Ratio of allowance for loan losses as a percentage of loans at end of period	3.08%	1.09%	3.08%	1.09%

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Other Real Estate Owned

OREO totaled $15.0 million as of June 30, 2010, which is an increase of $3.8 million, from $11.2 million as of December 31, 2009 and is included in other assets. As of June 30, 2010, OREO consisted of sixteen properties as compared to fourteen properties as of December 31, 2009. Nine of the properties held in OREO as of June 30, 2010 totaled $14.3 million and represented approximately 96% of the total. Included in OREO are three properties totaling $2.7 million, or 18%, of OREO, located outside of the Company s general market area. Additionally, $8.1 million, or 54%, of OREO is located in the Pocono region located within the Company s primary market area that has been particularly hit hard during the current economic recession.

The Company is actively marketing these properties for sale through a variety of channels including internal marketing and the use of outside brokers/realtors. The carrying value of OREO is generally calculated at an amount not greater than 90% of the most recent fair market appraised value. A 10% factor is generally used to estimate costs to sell, which is based on typical cost factors, such as 6% broker commission, 2% transfer taxes, and 2% various other miscellaneous costs associated with the sales process. This market value is updated on an annual basis or more frequently if new valuation information is available. Further deterioration in the real estate market could result in additional losses on these properties.

The following schedule reflects a breakdown of OREO for the periods reviewed.

	June 30, 2010 (as restated)	December 31, 2009
Land/Lots	$ 9,080	$ 5,887
Commercial Real Estate	5,374	4,852
Residential Real Estate	568	445
Total	$ 15,022	$ 11,184

The Company foreclosed on four properties during the six months ended June 30, 2010, two of which comprised substantially all of the $3.8 million in OREO (the other properties comprised 227 thousand of the increase). In connection with the transfer to OREO, the Company charged off $242 thousand of the loan balances against the ALLL to bring the properties down to their carrying value of $5.2 million.

The expenses related to maintaining OREO and the subsequent write down of the values related to declines in value since foreclosure amounted to $1.2 million and $1.5 million for the three and six months ended June 30, 2010, respectively compared to $42 thousand for the same periods in 2009.

Liabilities

Total liabilities were $1,246 million at June 30, 2010, a decrease of $57.3 million, or 4.4%, from December 31, 2009. During the six months ended June 30, 2010, deposit liabilities decreased $49.8 million to $1,021.8 million as a result of decreases of $21.7 million in demand deposits and of $37.3 million in time deposits partially offset by a $9.2 million increase in saving deposits. Borrowed funds decreased $6.4 million as the Company used the proceeds generated by net loan repayments and

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the general reduction in cash and cash equivalents to pay down its FHLB advances.

Equity

Total shareholders equity decreased $2.8 million, or 4.5%, to $60.2 million at June 30, 2010 from $63.1 million at December 31, 2009. The decrease is primarily due to the net loss off $6.0 million and a decrease in other comprehensive loss of $3.1 million for the six months ended June 30, 2010. The decrease in other comprehensive loss was primarily attributed to the increase in the market value of securities held in the available for sale portfolio. Book value per common share was $3.70 at June 30, 2010 compared to $3.87 at December 31, 2009. As of the date of the filing of this Amendment, the Order prohibits the Bank from paying dividends to the Company and the Agreement further prohibits the Company from taking dividend payments from the Bank.

Liquidity

During the six months ended June 30, 2010, funds provided by our operating activities amounted to $8.2 million. The Company funded $40.9 million in purchases of securities available for sale. Funds were primarily provided by $17.5 million in calls, maturities and pay downs of securities and $25.5 million in proceeds from sales of securities available for sale. These funds, together with $86.3 million of cash and cash equivalents available at the beginning of the year, were utilized to fund net deposit outflows of $49.8 million and the net repayment of $6.4 million of borrowed funds.

Interest Rate Risk

Our consolidated statements of financial position have been prepared in accordance with GAAP, which requires the measurement of financial position and operating results in terms of historical dollars without considering the changes in fair value of certain investments due to changes in interest rates. Generally, the fair value of financial investments such as loans and securities fluctuates inversely with changes in interest rates. As a result, increases in interest rates could result in decreases in the fair value of our interest-earning assets which could adversely affect our results of operation if such assets were sold, or, in the case of securities classified as available-for-sale, decreases in our shareholders equity, if such securities were retained.

We manage the mix of interest-earning assets and interest-bearing liabilities on a continuous basis to maximize return and adjust our exposure to interest rate risk. This report quantifies the potential changes in net interest income and net portfolio value should interest rates go up or down (shocked) 200 basis points, assuming the yield curves of the rate shocks will be parallel to each other. Net portfolio value is defined as the market value of assets net of the market value of liabilities. The market value of assets and liabilities is determined using a discounted cash flow calculation. The net portfolio value ratio is the ratio of the net portfolio value to the market value of assets. All changes in income and value are measured as percentage changes from the projected net interest income and net portfolio value at the base interest rate scenario. The base interest rate scenario assumes interest rates at, June 30, 2010. Various estimates regarding prepayment assumptions are made at each level of rate shock. However, prepayment penalty income is excluded from this analysis. Actual results could differ significantly from these estimates.

The following table presents our interest rate shock as of June 30, 2010:

	Projected Percentage Change In	
	Net Interest Income	**Net Portfolio Value**
Change in Interest Rate		
-200 Basis points	-0.69%	19.61%
Base interest rate	0.00	0.00
+200 Basis points	-2.99%	-32.10%

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ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in the company s exposure to market risk during the first six months of 2010. For discussion of the Company s exposure to market risk, refer to Item 7A, Quantitative and Qualitative Disclosure about Market Risk, contained in the Company s Amended 2009 Form 10-K.

ITEM 4 CONTROLS AND PROCEDURES

The Company s management has evaluated the effectiveness of the design and operation of the Company s disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, as of June 30, 2010. Internal control over financial reporting includes those policies and procedures that pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company; provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are only being made in accordance with authorizations of management and directors of the Company; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company s assets that could have a material effect on the financial statements. Due to inherent limitations, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of our financial statements would be prevented or detected.

Based on that evaluation, the Company s Principal Executive Officer and Chief Financial Officer concluded, as a result of the material weaknesses described below, that the Company s disclosure controls and procedures were not effective as of such date. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the Company s annual or interim consolidated financial statements will not be prevented or detected on a timely basis.

The following material weaknesses were identified:

- Control deficiencies were found to exist in the Company s accounting and finance function. It was determined that the Company had a material weakness in internal control over financial reporting because, in its Original Report, the Company did not properly account for OTTI of collateralized debt obligations in the Company s securities portfolio, the provision and allowance for loan and lease losses and the timing of charge-offs, the provision for off-balance sheet commitments, impairment of goodwill and deferred loan fees and costs. These errors also resulted in an incorrect determination of the Company s income tax benefit, deferred tax asset and related allowance. On October 27, 2010, the Company concluded that it would amend its Annual Report on Form 10-K for the fiscal year ended December 31, 2009 and its quarterly reports on Form 10-Q for the quarters ended March 31, 2010 and June 30, 2010, to revise and restate its financial statements included therein to properly account for its ALLL, the reserve for unfunded commitments and OTTI of its securities portfolio in accordance with its revised policies and procedures, to record a charge for the impairment of goodwill, to correct errors in its deferred loan fees and costs and to record the related change to the calculation of the Company s deferred tax assets. The changes to the accounting policies and procedures and the impact on the financial statements are more fully described in Part I, Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies and Note 2 to the consolidated financial statements included in this report. Overall, the restatement necessitated by this material weakness in internal control resulted in a decrease of $3.4 million and $6.2 in net income for the three and six months ended June 30, 2010, respectively, from net income (loss) of $(1.8) million and $0.2 million, respectively, as reported in the Original Report, to a net loss of $5.2 million and $6.0 million as reported herein.

• Systemic control deficiencies were also identified in the Company s processes, procedures and safeguards for information systems security. In particular, users of the Company s computer sub-systems may have had inappropriate access and system privileges that allowed them to view information and/or perform functions that are not appropriate to their job functions. Such access may have led to transactions being recorded improperly or may have permitted unauthorized transactions to occur. The Company is not aware of any transactions that were improperly undertaken as a result of this material weakness and therefore does not believe that such material weakness had any material impact on the Company s financial statements.

The insufficient policies and procedures, the accounting errors and the corresponding restatements, as well as the lack of appropriate processes, procedures and safeguards for information systems security, have resulted in management s determination that material weaknesses existed with respect to the internal controls over financial reporting. The lack of internal controls over financial reporting extended to the review function with regard to internal and external financial reporting and the overall review process at various levels of the Company s previous management. The material weakness in the accounting and finance function existed at December 31, 2009, March 31, 2010 and June 30, 2010 and was not identified until October 2010. To remediate this material weakness, the Company and its management modified the Company s policies and procedures as described in Part I, Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations of this report. The Company is also implementing accounting policy changes and is performing additional reviews of its financial statement preparation, reconciliation and disclosure

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processes. The Company has hired third party experts to assist with these changes. The material weakness in information systems security existed throughout 2009 and 2010 and was not identified until May 2011. To remediate this material weakness, the Company has modified its information systems procedures to centralize information systems access granting privileges to the information technology department rather than across various department functions across the Company and has hired outside consultants to review and implement policy, process and security improvements. The Company is not aware of any transactions that were improperly undertaken as a result of the material weakness in its information systems security and therefore does not believe that such material weakness had any material impact on the Company s financial statements.

The Company continually seeks to improve the effectiveness and efficiency of its internal controls over financial reporting, resulting in frequent process refinement. Except as described above to remediate the material weaknesses identified, there have been no changes in the Company s internal control over financial reporting during the three and six months ended June 30, 2010 that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

PART II Other Information

Item 1 Legal Proceedings.

From time to time, the Company becomes subject to various legal claims that arise in the normal course of business. At June 30, 2010 the Company was not the subject of any material pending legal proceedings other than ordinary routine litigation occurring in the normal course of its business. The various pending legal claims against the Company will not, in the opinion of management, result in any material liability to the Company and will not materially affect our financial position, results of operation, or cash flow.

Item 1A. Risk Factors.

Management of the Company does not believe there have been any material changes in the risk factors that were previously disclosed in the Company s Form 10-K/A for the year ending December 31, 2009.

Item 2 Unregistered Sales of Equity Securities and Use of Proceeds.

None.

Item 3 - Defaults upon Senior Securities.

None.

Item 4 [Removed and Reserved.]

Item 5 - Other Information.

None.

Item 6 Exhibits.

Exhibit 3.1	Amended and Restated Articles of Incorporation (Incorporated by reference to Exhibit 3.1 of the Company s Form 10-K for the year ended December 31, 2005)
Exhibit 3.2	Amended and Restated Bylaws (Incorporated by reference to Exhibit 3(ii) of the Company s Form 8-K filed on December 16, 2009)
Exhibit 4.1	Form of Subordinated Note (Incorporated by reference to Exhibit 4.1 of the Company s Form 8-K filed with the Commission on August 28, 2009)
Exhibit 4.2	Form of Common Stock Certificate of the Company (Incorporated by reference to Exhibit 4.1 of the Company s Form 10-K for the year ended December 31, 2009)
Exhibit 31.1*	Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act
Exhibit 31.2*	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act
Exhibit 32.1*	Certification of Principal Executive Officer and Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act

* Filed herewith.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Registrant: FIRST NATIONAL COMMUNITY BANCORP, INC.

Date: December 2, 2011	By:	/s/ Dominick L. DeNaples
	Dominick L. DeNaples Chairman of the Board of Directors Principal Executive Officer	
Date: December 2, 2011	By:	/s/ Edward J. Lipkus
	Edward J. Lipkus Chief Financial Officer Principal Financial Officer Principal Accounting Officer	