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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2010

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File Number 000-23423

C&F Financial Corporation

(Exact name of registrant as specified in its charter)

Virginia	**54-1680165**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
802 Main Street West Point, VA	**23181**
(Address of principal executive offices)	**(Zip Code)**

(804) 843-2360

(Registrant s telephone number, including area code)

N/A

(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 ¨

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

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

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

At August 5, 2010, the latest practicable date for determination, 3,089,766 shares of common stock, $1.00 par value, of the registrant were outstanding.

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS

(In thousands, except for share and per share amounts)

	June 30, 2010 (Unaudited)	December 31, 2009
ASSETS		
Cash and due from banks	**$ 9,142**	$ 8,434
Interest-bearing deposits in other banks	**4,946**	29,627
Total cash and cash equivalents	**14,088**	38,061
Securities-available for sale at fair value, amortized cost of $118,902 and $116,774, respectively	**121,219**	118,570
Loans held for sale, net	**63,618**	28,756
Loans, net of allowance for loan losses of $25,154 and $24,027, respectively	**614,085**	613,004
Federal Home Loan Bank stock, at cost	**3,887**	3,887
Corporate premises and equipment, net	**29,626**	29,490
Other real estate owned, net of valuation allowance of $3,244 and $2,402, respectively	**13,004**	12,800
Accrued interest receivable	**5,159**	5,408
Goodwill	**10,724**	10,724
Other assets	**28,714**	27,730
Total assets	**$ 904,124**	$ 888,430
LIABILITIES AND SHAREHOLDERS EQUITY		
Deposits		
Noninterest-bearing demand deposits	**$ 96,507**	$ 83,708
Savings and interest-bearing demand deposits	**189,657**	208,388
Time deposits	**328,481**	314,534
Total deposits	**614,645**	606,630
Short-term borrowings	**31,530**	11,082
Long-term borrowings	**124,963**	139,130
Trust preferred capital notes	**20,620**	20,620
Accrued interest payable	**1,604**	1,569
Other liabilities	**20,202**	20,523
Total liabilities	**813,564**	799,554
Commitments and contingent liabilities		
Shareholders equity		
Preferred stock ($1.00 par value, 3,000,000 shares authorized, 20,000 shares issued and outstanding)	**20**	20
Common stock ($1.00 par value, 8,000,000 shares authorized, 3,089,766 and 3,067,666 shares issued and outstanding, respectively)	**3,018**	3,009
Additional paid-in capital	**21,614**	21,210
Retained earnings	**64,701**	63,669

Accumulated other comprehensive income, net	**1,207**	968
Total shareholders equity	**90,560**	88,876
Total liabilities and shareholders equity	**$ 904,124**	$ 888,430

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

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CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(In thousands, except for share and per share amounts)

	Three Months Ended June 30, 2010	Three Months Ended June 30, 2009	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Interest income				
Interest and fees on loans	**$ 16,146**	$ 14,933	**$ 31,485**	$ 29,218
Interest on money market investments	**9**		**27**	
Interest and dividends on securities				
U.S. government agencies and corporations	**80**	98	**167**	229
Tax-exempt obligations of states and political subdivisions	**1,099**	1,042	**2,202**	2,009
Corporate bonds and other	**28**	52	**73**	106
Total interest income	**17,362**	16,125	**33,954**	31,562
Interest expense				
Savings and interest-bearing deposits	**226**	444	**545**	1,009
Certificates of deposit, $100 thousand or more	**841**	902	**1,662**	1,768
Other time deposits	**1,006**	1,355	**2,044**	2,753
Borrowings	**996**	1,013	**1,949**	2,082
Trust preferred capital notes	**249**	274	**494**	561
Total interest expense	**3,318**	3,988	**6,694**	8,173
Net interest income	**14,044**	12,137	**27,260**	23,389
Provision for loan losses	**3,300**	4,400	**6,500**	8,500
Net interest income after provision for loan losses	**10,744**	7,737	**20,760**	14,889
Noninterest income				
Gains on sales of loans	**4,679**	7,374	**8,427**	13,917
Service charges on deposit accounts	**865**	790	**1,606**	1,586
Other service charges and fees	**1,085**	1,334	**1,994**	2,503
Gains on calls and sales of available for sale securities	**16**	23	**76**	30
Other income	**549**	437	**973**	1,163
Total noninterest income	**7,194**	9,958	**13,076**	19,199
Noninterest expenses				
Salaries and employee benefits	**8,763**	9,395	**16,663**	18,311
Occupancy expenses	**1,389**	1,471	**2,786**	2,927
Other expenses	**6,054**	4,439	**10,349**	8,553
Total noninterest expenses	**16,206**	15,305	**29,798**	29,791

Income before income taxes		**1,732**		2,390		**4,038**		4,297
Income tax expense		**315**		640		**891**		1,039
Net income		**1,417**		1,750		**3,147**		3,258
Effective dividends on preferred stock		**287**		288		**574**		548
Net income available to common shareholders	**$**	**1,130**	$	1,462	**$**	**2,573**	$	2,710
Per common share data								
Net income basic	**$**	**0.37**	$	0.48	**$**	**0.84**	$	0.89
Net income assuming dilution	**$**	**0.36**	$	0.48	**$**	**0.83**	$	0.89
Cash dividends declared	**$**	**0.25**	$	0.25	**$**	**0.50**	$	0.56
Weighted average number of shares basic		**3,084,255**		3,042,233		**3,078,970**		3,040,504
Weighted average number of shares assuming dilution		**3,102,643**		3,042,233		**3,100,669**		3,040,504

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

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CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

(Unaudited)

(In thousands, except per share amounts)

	Preferred Stock	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders Equity
Balance December 31, 2009	**$ 20**	**$ 3,009**	**$ 21,210**	**$ 63,669**	**$ 968**	**$ 88,876**
Comprehensive income:						
Net income				**3,147**		**3,147**
Other comprehensive income, net						
Changes in cash balance pension plan assets and benefit obligations, net					**(8)**	
Unrealized loss on cash flow hedging instrument, net					**(93)**	
Unrealized gains on securities, net of reclassification adjustment					**340**	
Other comprehensive income, net					**239**	**239**
Comprehensive income						**3,386**
Share-based compensation			**194**			**194**
Stock options exercised		**9**	**136**			**145**
Accretion of preferred stock discount			**74**	**(74)**		
Cash dividends paid common stock ($0.50 per share)				**(1,541)**		**(1,541)**
Cash dividends paid preferred stock (5% per annum)				**(500)**		**(500)**
Balance June 30, 2010	**$ 20**	**$ 3,018**	**$ 21,614**	**$ 64,701**	**$ 1,207**	**$ 90,560**

	Preferred Stock	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders Equity
Balance December 31, 2008	$	$ 2,992	$ 551	$ 62,361	$ (1,047)	$ 64,857
Comprehensive income:						
Net income				3,258		3,258
Other comprehensive income, net						
Changes in cash balance pension plan assets and benefit obligations, net					14	
Unrealized gains on securities, net of reclassification adjustment					164	
Other comprehensive income, net					178	178
Comprehensive income						3,436
Share-based compensation			160			160
Issuance of preferred stock and warrant	20		19,894			19,914
Accretion of preferred stock discount			66	(66)		
Cash dividends paid common stock ($0.56 per share)				(1,704)		(1,704)
Cash dividends paid preferred stock (5% per annum)				(350)		(350)

Balance June 30, 2009	$ 20	$ 2,992	$ 20,671	$ 63,499	$ (869)	$ 86,313

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

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CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In thousands)

	Six Months Ended June 30, 2010	Six Months Ended June 30, 2009
Operating activities:		
Net income	**$ 3,147**	$ 3,258
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation	**942**	1,108
Provision for loan losses	**6,500**	8,500
Provision for other real estate owned losses	**1,220**	432
Share-based compensation	**194**	160
Accretion of discounts and amortization of premiums on securities, net	**244**	60
Net realized gain on securities	**(76)**	(30)
Realized gains on sales of other real estate owned	**(6)**	(23)
Proceeds from sales of loans	**308,493**	627,258
Origination of loans held for sale	**(343,355)**	(652,331)
Change in other assets and liabilities:		
Accrued interest receivable	**249**	(26)
Other assets	**(1,169)**	614
Accrued interest payable	**35**	(143)
Other liabilities	**(422)**	(1,995)
Net cash used in operating activities	**(24,004)**	(13,158)
Investing activities:		
Proceeds from maturities, calls and sales of securities available for sale	**15,140**	14,974
Purchases of securities available for sale	**(17,434)**	(24,982)
Net redemptions of Federal Home Loan Bank stock		1,397
Net increase in customer loans	**(9,859)**	(139)
Capitalized costs of other real estate owned	**(131)**	
Proceeds from sales of other real estate owned	**993**	493
Purchases of corporate premises and equipment	**(1,078)**	(209)
Disposals of corporate premises and equipment		26
Net cash used in investing activities	**(12,369)**	(8,440)
Financing activities:		
Net (decrease) increase in demand, interest-bearing demand and savings deposits	**(5,932)**	2,588
Net increase in time deposits	**13,947**	27,886
Net increase (decrease) in borrowings	**6,281**	(25,993)
Proceeds from exercise of stock options	**145**	
Net proceeds from issuance of preferred stock		19,914
Cash dividends	**(2,041)**	(2,054)
Net cash provided by financing activities	**12,400**	22,341
Net (decrease) increase in cash and cash equivalents	**(23,973)**	743
Cash and cash equivalents at beginning of period	**38,061**	9,888

Cash and cash equivalents at end of period	**$**	**14,088**	$	10,631
Supplemental disclosure				
Interest paid	**$**	**6,659**	$	8,316
Income taxes paid		**3,268**		1,142
Supplemental disclosure of noncash investing and financing activities				
Unrealized gains on securities available for sale	**$**	**521**	$	253
Loans transferred to other real estate owned		**(2,278)**		(9,477)
Pension adjustment		**(12)**		22
Unrealized loss on cash flow hedging instrument		**(149)**		

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1: Summary of Significant Accounting Policies

Principles of Consolidation: The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial reporting and with applicable quarterly reporting regulations of the Securities and Exchange Commission (the SEC). They do not include all of the information and notes required by U.S. GAAP for complete financial statements. Therefore, these consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the C&F Financial Corporation Annual Report on Form 10-K for the year ended December 31, 2009.

The unaudited consolidated financial statements include the accounts of C&F Financial Corporation (the Corporation) and its wholly-owned subsidiary, Citizens and Farmers Bank (the Bank or C&F Bank). All significant intercompany accounts and transactions have been eliminated in consolidation. In addition, C&F Financial Corporation owns C&F Financial Statutory Trust I and C&F Financial Statutory Trust II, which are unconsolidated subsidiaries. The subordinated debt owed to these trusts is reported as a liability of the Corporation.

Nature of Operations: The Corporation is a bank holding company incorporated under the laws of the Commonwealth of Virginia. The Corporation owns all of the stock of its subsidiary, C&F Bank, which is an independent commercial bank chartered under the laws of the Commonwealth of Virginia. The Bank and its subsidiaries offer a wide range of banking and related financial services to both individuals and businesses.

The Bank has five wholly-owned subsidiaries: C&F Mortgage Corporation and Subsidiaries (C&F Mortgage), C&F Finance Company (C&F Finance), C&F Title Agency, Inc., C&F Investment Services, Inc. and C&F Insurance Services, Inc., all incorporated under the laws of the Commonwealth of Virginia. C&F Mortgage, organized in September 1995, was formed to originate and sell residential mortgages and through its subsidiaries, Hometown Settlement Services LLC and Certified Appraisals LLC, provides ancillary mortgage loan production services, such as loan settlements, title searches and residential appraisals. C&F Finance, acquired on September 1, 2002, is a regional finance company providing automobile loans. C&F Title Agency, Inc., organized in October 1992, primarily sells title insurance to the mortgage loan customers of the Bank and C&F Mortgage. C&F Investment Services, Inc., organized in April 1995, is a full-service brokerage firm offering a comprehensive range of investment services. C&F Insurance Services, Inc., organized in July 1999, owns an equity interest in an insurance agency that sells insurance products to customers of the Bank, C&F Mortgage and other financial institutions that have an equity interest in the agency. Business segment data is presented in Note 6.

Basis of Presentation: The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the allowance for indemnifications, impairment of loans, impairment of securities, the valuation of other real estate owned, the projected benefit obligation under the cash balance pension plan, the valuation of deferred taxes, the valuation of derivative financial instruments and goodwill impairment. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, which are necessary for a fair presentation of the results of operations in these financial statements, have been made. Certain reclassifications have been made to prior period amounts to conform to the current period presentation.

Share-Based Compensation: Compensation expense for the second quarter and first six months of 2010 included $94,000 ($58,000 after tax) and $194,000 ($120,000 after tax), respectively, for restricted stock granted since 2006. As of June 30, 2010, there was $993,000 of total unrecognized compensation expense related to unvested restricted stock that will be recognized over the remaining requisite service periods.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Stock option activity for the six months ended June 30, 2010 and stock options outstanding as of June 30, 2010 are summarized below:

	Shares	Exercise Price*	Remaining Contractual Life (in years)*	Intrinsic Value of Unexercised In-The Money Options (in 000 s)
Options outstanding at January 1, 2010	417,717	$ 33.71	4.4	
Exercised	9,000	16.13		
Options outstanding and exercisable at June 30, 2010	408,717	$ 34.10	4.0	$ 54

* *Weighted average*

A summary of restricted stock activity for the six months ended June 30, 2010 is presented below:

	Shares	Weighted-Average Grant Date Fair Value
Unvested, January 1, 2010	58,725	$ 28.59
Granted	13,100	$ 19.72
Unvested, June 30, 2010	71,825	$ 26.97

Derivative Financial Instruments: During the second quarter of 2010, the Corporation entered into a derivative financial instrument. The Corporation recognizes derivative financial instruments as either an asset or liability in the consolidated balance sheet at fair value in other assets or other liabilities. The derivative financial instrument has been designated as and qualifies as a cash flow hedge. The effective portion of the gain or loss on the cash flow hedge is reported as a component of other comprehensive income, net of deferred income taxes, and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings.

Recent Significant Accounting Pronouncements:

In June 2009, the Financial Accounting Standards Board (FASB) issued new guidance relating to the accounting for transfers of financial assets. The new guidance, which was issued as Statement of Financial Accounting Standard (SFAS) No. 166, *Accounting for Transfers of Financial Assets, an amendment to SFAS No. 140*, was adopted into Codification in December 2009 through the issuance of Accounting Standards Update (ASU) 2009-16 (ASU 2009-16). The new standard provides guidance to improve the relevance, representational faithfulness, and comparability of the information that an entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor s continuing involvement, if any, in transferred financial assets. ASU 2009-16 was effective January 1, 2010. The adoption of this guidance did not have a material effect on the Corporation s consolidated financial statements.

In June 2009, the FASB issued new guidance relating to the variable interest entities. The new guidance, which was issued as SFAS No. 167, *Amendments to FASB Interpretation No. 46(R),* was adopted into Codification in December 2009 through the issuance of ASU 2009-17 and updates ASC Topic 810: *Consolidation* (ASC Topic 810). The objective of the guidance is to improve financial reporting by enterprises involved with variable interest entities and to provide more relevant and reliable information to users of financial statements. ASC Topic 810 was effective as of January 1, 2010. The adoption of this guidance did not have a material effect on the Corporation s consolidated financial statements.

In January 2010, the FASB issued ASU No. 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements* (ASU 2010-06). ASU 2010-06 amends Subtopic 820-10 to clarify existing disclosures, require new disclosures, and includes conforming amendments to guidance on employers disclosures about postretirement benefit plan assets. ASU 2010-06 is effective for interim and annual periods beginning after December 15, 2009, except for disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. The adoption of ASU 2010-06 did not have a material effect on the Corporation s consolidated financial statements.

In July 2010, the FASB issued ASU No. 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses* (ASU 2010-20). The new disclosure guidance will significantly expand the existing disclosure requirements and is intended to lead to greater transparency into a company s exposure to credit losses from lending arrangements. The extensive new

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

disclosures of information as of the end of a reporting period will become effective for both interim and annual reporting periods ending after December 15, 2010. Specific items regarding activity that occurred before the issuance of the ASU, such as the allowance rollforward and modification disclosures, will be required for periods beginning after December 15, 2010. The Corporation is currently assessing the impact that ASU 2010-20 will have on its consolidated financial statements.

NOTE 2: Securities

Debt and equity securities are summarized as follows:

(Dollars in thousands)	June 30, 2010			
Available for Sale	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. government agencies and corporations	**$ 14,236**	**$ 103**	**$**	**$ 14,339**
Mortgage-backed securities	**2,894**	**105**		**2,999**
Obligations of states and political subdivisions	**101,598**	**2,412**	**(284)**	**103,726**
Preferred stock	**174**	**1**	**(20)**	**155**
	$ 118,902	**$ 2,621**	**$ (304)**	**$ 121,219**

(Dollars in thousands)	December 31, 2009			
Available for Sale	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. government agencies and corporations	$ 9,772	$ 33	$ (62)	$ 9,743
Mortgage-backed securities	2,628	81		2,709
Obligations of states and political subdivisions	103,097	2,144	(374)	104,867
Preferred stock	1,277	59	(85)	1,251
	$ 116,774	$ 2,317	$ (521)	$ 118,570

The amortized cost and estimated fair value of securities at June 30, 2010, by the earlier of contractual maturity or expected maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without call or prepayment penalties.

(Dollars in thousands)	June 30, 2010	
Available for Sale	Amortized Cost	Estimated Fair Value
Due in one year or less	**$ 19,853**	**$ 19,980**
Due after one year through five years	**30,435**	**30,933**
Due after five years through ten years	**42,566**	**43,493**
Due after ten years	**25,874**	**26,658**
Preferred stock	**174**	**155**

	$ 118,902	**$ 121,219**

Proceeds from the maturities, calls and sales of securities available for sale for the six months ended June 30, 2010 were $15.14 million, resulting in gross realized gains of $80,000 and gross realized losses of $4,000.

The Corporation pledges securities to secure public deposits, Federal Reserve Bank treasury, tax and loan deposits and repurchase agreements. Securities with an aggregate amortized cost of $78.50 million and an aggregate fair value of $80.30 million were pledged at June 30, 2010. Securities with an aggregate amortized cost of $87.44 million and an aggregate fair value of $88.90 million were pledged at December 31, 2009.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Securities in an unrealized loss position at June 30, 2010, by duration of the period of the unrealized loss, are shown below.

(Dollars in thousands)	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Obligations of states and political subdivisions	**$ 14,663**	**$ 134**	**$ 3,313**	**$ 150**	**$ 17,976**	**$ 284**
Preferred stock	**14**	**7**	**134**	**13**	**148**	**20**
Total temporarily impaired securities	**$ 14,677**	**$ 141**	**$ 3,447**	**$ 163**	**$ 18,124**	**$ 304**

There are 55 debt securities with fair values totaling $17.98 million considered temporarily impaired at June 30, 2010. The primary cause of the temporary impairments in the Corporation s investments in debt securities was fluctuations in interest rates. Because the Corporation intends to hold these investments in debt securities to maturity and it is more likely than not that the Corporation will not be required to sell these investments before a recovery of unrealized losses, the Corporation does not consider these investments to be other-than-temporarily impaired at June 30, 2010 and no impairment has been recognized. There are three equity securities with a fair value of $148,000 considered temporarily impaired at June 30, 2010. The Corporation has the intent and ability to hold these equity securities until a recovery of the unrealized loss and therefore does not consider these investments to be other-than-temporarily impaired at June 30, 2010.

Securities in an unrealized loss position at December 31, 2009, by duration of the period of the unrealized loss, are shown below.

(Dollars in thousands)	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. government agencies and corporations	$ 3,298	$ 62	$	$	$ 3,298	$ 62
Obligations of states and political subdivisions	18,872	255	2,853	119	21,725	374
Subtotal-debt securities	22,170	317	2,853	119	25,023	436
Preferred stock	401	13	408	72	809	85
Total temporarily impaired securities	$ 22,571	$ 330	$ 3,261	$ 191	$ 25,832	$ 521

The Corporation s investment in Federal Home Loan Bank (FHLB) stock totaled $3.89 million at June 30, 2010 and December 31, 2009. FHLB stock is generally viewed as a long-term investment and as a restricted investment security, which is carried at cost, because there is no market for the stock, other than the FHLBs or member institutions. Therefore, when evaluating FHLB stock for impairment, its value is based on the ultimate recoverability of the par value rather than by recognizing temporary declines in value. Despite the FHLB s temporary suspension of repurchases of excess capital stock beginning in 2009, the Corporation does not consider this investment to be other-than-temporarily impaired at June 30, 2010 and no impairment has been recognized. FHLB stock is shown as a separate line item on the balance sheet and is not a part of the available for sale securities portfolio.

NOTE 3: Other Comprehensive Income and Earnings Per Common Share

Other Comprehensive Income

The following table presents the cumulative balances of the components of other comprehensive income, net of deferred tax assets (liabilities) of $644,000 and $(467,000) as of June 30, 2010 and 2009, respectively.

(Dollars in thousands)	June 30, 2010	June 30, 2009
Net unrealized gains on securities	**$ 1,507**	$ 50
Net unrecognized loss on cash flow hedge	**(93)**	
Net unrecognized losses on cash balance pension plan	**(207)**	(919)
Total cumulative other comprehensive income (loss)	**$ 1,207**	$ (869)

The Corporation reclassified net gains of $49,000 from other comprehensive income to earnings for the six months ended June 30, 2010.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Earnings Per Common Share

The components of the Corporation s earnings per common share calculations are as follows:

(Dollars in thousands)	Three Months Ended June 30, 2010	2009
Net income	**$ 1,417**	$ 1,750
Accumulated dividends on Series A Preferred Stock	**(250)**	(253)
Accretion of Series A Preferred Stock discount	**(37)**	(35)
Net income available to common shareholders	**$ 1,130**	$ 1,462
Weighted average number of common shares used in earnings per common share basic	**3,084,255**	3,042,233
Effect of dilutive securities:		
Stock option awards and Warrant	**18,388**	
Weighted average number of common shares used in earnings per common share assuming dilution	**3,102,643**	3,042,233

(Dollars in thousands)	Six Months Ended June 30, 2010	2009
Net income	**$ 3,147**	$ 3,258
Accumulated dividends on Series A Preferred Stock	**(500)**	(481)
Accretion of Series A Preferred Stock discount	**(74)**	(67)
Net income available to common shareholders	**$ 2,573**	$ 2,710
Weighted average number of common shares used in earnings per common share basic	**3,078,970**	3,040,504
Effect of dilutive securities:		
Stock option awards and Warrant	**21,699**	
Weighted average number of common shares used in earnings per common share assuming dilution	**3,100,669**	3,040,504

Potential common shares that may be issued by the Corporation for its stock option awards and the warrant to purchase common shares issued on January 9, 2009 in connection with the Corporation s participation in the Capital Purchase Program (CPP) established by the U.S. Department of the Treasury (Treasury) under the Emergency Economic Stabilization Act of 2008 (the Warrant) are determined using the treasury stock method. Options and the Warrant on approximately 354,000 and 615,000 shares for the three months ended June 30, 2010 and 2009, respectively, and 354,000 and 619,000 for the six months ended June 30, 2010 and 2009, respectively were not included in computing diluted earnings per common share because they were anti-dilutive.

NOTE 4: Employee Benefit Plans

The Bank has a non-contributory cash balance pension plan for which the components of net periodic benefit cost are as follows:

(Dollars in thousands)	**Three Months Ended June 30,**	
	2010	**2009**
Service cost	**$ 133**	$ 126
Interest cost	**99**	93
Expected return on plan assets	**(124)**	(103)
Amortization of net obligation at transition	**(1)**	(1)
Amortization of prior service cost	**(17)**	(17)
Amortization of net loss	**12**	29
Net periodic benefit cost	**$ 102**	$ 127

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(Dollars in thousands)	Six Months Ended June 30, 2010	2009
Service cost	**$ 266**	$ 252
Interest cost	**198**	186
Expected return on plan assets	**(248)**	(206)
Amortization of net obligation at transition	**(2)**	(2)
Amortization of prior service cost	**(34)**	(34)
Amortization of net loss	**24**	58
Net periodic benefit cost	**$ 204**	$ 254

The Bank made a $400,000 contribution to this plan in the first quarter of 2010.

NOTE 5: Fair Value of Assets and Liabilities

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. U.S. GAAP requires that valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs. U.S. GAAP also establishes a fair value hierarchy which prioritizes the valuation inputs into three broad levels. Based on the underlying inputs, each fair value measurement in its entirety is reported in one of the three levels. These levels are:

Level 1 Valuation is based upon quoted prices for identical instruments traded in active markets. Level 1 assets and liabilities include debt and equity securities traded in an active exchange market, as well as U.S. Treasury securities.

Level 2 Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments 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 observable market data for substantially the full term of the assets or liabilities.

Level 3 Valuation is determined using model-based techniques with significant assumptions not observable in the market.

U.S. GAAP allows an entity the irrevocable option to elect fair value (the fair value option) for the initial and subsequent measurement for certain financial assets and liabilities on a contract-by-contract basis. The Corporation has not made any fair value option elections as of June 30, 2010.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table presents the balances of financial assets measured at fair value on a recurring basis. There were no liabilities measured at fair value on a recurring basis at December 31, 2009.

June 30, 2010

(Dollars in thousands)	Fair Value Measurements Using			Assets at Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Securities available for sale				
U.S. government agencies and corporations		$ 14,339		$ 14,339
Mortgage-backed securities		2,999		2,999
Obligations of states and political subdivisions		103,726		103,726
Preferred stock		155		155
Total securities available for sale		$ 121,219		$ 121,219
Liabilities:				
Derivative payable		$ 149		$ 149
Total liabilities		$ 149		$ 149

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(Dollars in thousands)	December 31, 2009 Fair Value Measurements Using			Assets at
	Level 1	Level 2	Level 3	Fair Value
Securities available for sale				
U.S. government agencies and corporations		$ 9,743		$ 9,743
Mortgage-backed securities		2,709		2,709
Obligations of states and political subdivisions		104,867		104,867
Preferred stock		1,251		1,251
Total securities available for sale		$ 118,570		$ 118,570

Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

The Corporation is also required to measure and recognize certain other financial assets at fair value on a nonrecurring basis in the consolidated balance sheets. For assets measured at fair value on a nonrecurring basis and still held on the consolidated balance sheets, the following table provides the fair value measures by level of valuation assumptions used. Fair value adjustments for other real estate owned (OREO) are recorded in other noninterest expense and fair value adjustments for loans held for investment are recorded in the provision for loan losses, in the consolidated statements of income. There were no liabilities measured at fair value on a nonrecurring basis at June 30, 2010 or December 31, 2009.

	June 30, 2010 Fair Value Measurements Using			Assets at
(Dollars in thousands)	Level 1	Level 2	Level 3	Fair Value
Impaired loans, net		**$ 7,992**		**$ 7,992**
OREO		**13,004**		**13,004**
Total		**$ 20,996**		**$ 20,996**

	December 31, 2009 Fair Value Measurements Using			Assets at Fair
(Dollars in thousands)	Level 1	Level 2	Level 3	Value
Impaired loans, net		$ 6,720		$ 6,720
OREO		12,800		12,800
Total		$ 19,520		$ 19,520

Fair Value of Financial Instruments

The following reflects the fair value of financial instruments whether or not recognized on the consolidated balance sheet at fair value.

	June 30, 2010		December 31, 2009	
(Dollars in thousands)	**Carrying Amount**	**Estimated Fair Value**	**Carrying Amount**	**Estimated Fair Value**
Financial assets:				
Cash and short-term investments	**$ 14,088**	**$ 14,088**	$ 38,061	$ 38,061
Securities available for sale	**121,219**	**121,219**	118,570	118,570
Loans, net	**614,085**	**614,661**	613,004	611,420
Loans held for sale, net	**63,618**	**66,336**	28,756	29,032
Accrued interest receivable	**5,159**	**5,159**	5,408	5,408
Financial liabilities:				
Demand deposits	**286,164**	**286,164**	292,096	292,096
Time deposits	**328,481**	**333,013**	314,534	319,593
Borrowings	**177,113**	**174,322**	170,832	166,533
Derivative payable	**149**	**149**		
Accrued interest payable	**1,604**	**1,604**	1,569	1,569

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

The following describes the valuation techniques used by the Corporation to measure financial assets and financial liabilities at fair value as of June 30, 2010 and December 31, 2009.

Cash and short-term investments. The nature of these instruments and their relatively short maturities provide for the reporting of fair value equal to the historical cost.

Securities available for sale. Securities available for sale are recorded at fair value on a recurring basis.

Loans, net. The estimated fair value of the loan portfolio is based on present values using discount rates equal to the market rates currently charged on similar products.

Certain loans are accounted for under ASC Topic 310 *Receivables*, including impaired loans measured at an observable market price (if available), or at the fair value of the loan s collateral (if the loan is collateral dependent). Collateral may be in the form of real estate or business assets including equipment, inventory and accounts receivable. A significant portion of the collateral securing the Corporation s impaired loans is real estate. The fair value of real estate collateral is determined utilizing an income or market valuation approach based on an appraisal conducted by an independent, licensed appraiser outside of the Corporation using observable market data, which in some cases may be adjusted to reflect current trends, including sales prices, expenses, absorption periods and other current relevant factors (Level 2). The value of business equipment is based upon an outside appraisal if deemed significant, or the net book value on the applicable business s financial statements, if not considered significant, using observable market data (Level 2). At June 30, 2010 and December 31, 2009, the Corporation s impaired loans were valued at $7.99 million and $6.72 million, respectively.

Loans held for sale, net. Loans held for sale are required to be measured at the lower of cost or fair value. These loans currently consist of residential loans originated for sale in the secondary market. Fair value is based on the price secondary markets are currently offering for similar loans using observable market data, which is generally not materially different than cost due to the short duration between origination and sale (Level 2). As such, the Corporation records any fair value adjustments on a nonrecurring basis. No nonrecurring fair value adjustments were recorded on loans held for sale during the three or six months ended June 30, 2010.

Accrued interest receivable. The carrying amount of accrued interest receivable approximates fair value.

Deposits. The fair value of all demand deposit accounts is the amount payable at the report date. For all other deposits, the fair value is determined using the discounted cash flow method. The discount rate was equal to the rate currently offered on similar products.

Borrowings. The fair value of borrowings is determined using the discounted cash flow method. The discount rate was equal to the rate currently offered on similar products.

Derivative payable. The fair value of the derivative is determined using the discounted cash flow method.

Accrued interest payable. The carrying amount of accrued interest payable approximates fair value.

Letters of credit. The estimated fair value of letters of credit is based on estimated fees the Corporation would pay to have another entity assume its obligation under the outstanding arrangements. These fees are not considered material.

Unused portions of lines of credit. The estimated fair value of unused portions of lines of credit is based on estimated fees the Corporation would pay to have another entity assume its obligation under the outstanding arrangements. These fees are not considered material.

The Corporation assumes interest rate risk (the risk that general interest rate levels will change) as a result of its normal operations. As a result, the fair values of the Corporation s financial instruments will change when interest rate levels change and that change may be either favorable or unfavorable to the Corporation. Management attempts to match maturities of assets and liabilities to the extent believed necessary to balance minimizing interest rate risk and increasing net interest income in current market conditions. However, borrowers with fixed rate obligations are less likely to prepay in a rising rate environment and more likely to prepay in a falling rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors interest rates, maturities and repricing dates of assets and liabilities and attempts to manage interest rate risk by adjusting terms of new loans, deposits and borrowings and by investing in securities with terms that mitigate the Corporation s overall interest rate risk.

NOTE 6: Business Segments

The Corporation operates in a decentralized fashion in three principal business segments: Retail Banking, Mortgage Banking and Consumer Finance. Revenues from Retail Banking operations consist primarily of interest earned on loans and investment securities and service charges on deposit accounts. Mortgage Banking operating revenues consist principally of gains on sales of loans in the secondary market, loan origination fee income and interest earned on mortgage loans held for sale. Revenues from Consumer Finance consist primarily of interest earned on automobile retail installment sales contracts.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

The Corporation s other segments include an investment company that derives revenues from brokerage services, an insurance company that derives revenues from insurance services, and a title company that derives revenues from title insurance services. The results of these other segments are not significant to the Corporation as a whole and have been included in Other. Revenue and expenses of the Corporation s holding company are also included in Other, and consist primarily of dividends received on the Corporation s investment in equity securities and interest expense associated with the Corporation s trust preferred capital notes.

(Dollars in thousands)	Three Months Ended June 30, 2010					
	Retail Banking	Mortgage Banking	Consumer Finance	Other	Eliminations	Consolidated
Revenues:						
Interest income	$ 8,556	$ 583	$ 9,120	$ 42	$ (939)	$ 17,362
Gains on sales of loans		4,679				4,679
Other	1,475	594	134	312		2,515
Total operating income	10,031	5,856	9,254	354	(939)	24,556
Expenses:						
Interest expense	2,638	91	1,286	258	(955)	3,318
Provision for loan losses	1,450		1,850			3,300
Salaries and employee benefits	3,595	3,532	1,466	171	(1)	8,763
Other noninterest expenses	2,837	3,797	668	141		7,443
Total operating expenses	10,520	7,420	5,270	570	(956)	22,824
Income (loss) before income taxes	(489)	(1,564)	3,984	(216)	17	1,732
Provision for (benefit from) income taxes	(537)	(626)	1,554	(81)	5	315
Net income (loss)	$ 48	$ (938)	$ 2,430	$ (135)	$ 12	$ 1,417
Total assets	$ 767,465	$ 75,904	$ 209,549	$ 2,589	$ (151,383)	$ 904,124
Capital expenditures	$ 558	$ 80	$ 25	$	$	$ 663

(Dollars in thousands)	Three Months Ended June 30, 2009					
	Retail Banking	Mortgage Banking	Consumer Finance	Other	Eliminations	Consolidated
Revenues:						
Interest income	$ 8,485	$ 729	$ 7,707	$ 66	$ (862)	$ 16,125
Gains on sales of loans		7,374				7,374
Other	1,217	937	108	322		2,584
Total operating income	9,702	9,040	7,815	388	(862)	26,083
Expenses:						
Interest expense	3,262	85	1,224	286	(869)	3,988
Provision for loan losses	1,400	200	2,800			4,400
Salaries and employee benefits	3,386	4,646	1,232	131		9,395
Other noninterest expenses	2,948	2,059	815	88		5,910

Total operating expenses	10,996	6,990	6,071	505	(869)	23,693
Income (loss) before income taxes	(1,294)	2,050	1,744	(117)	7	2,390
Provision for (benefit from) income taxes	(847)	876	666	(57)	2	640
Net income (loss)	$ (447)	$ 1,174	$ 1,078	$ (60)	$ 5	$ 1,750
Total assets	$ 729,082	$ 70,025	$ 184,631	$ 2,428	$ (106,724)	$ 879,442
Capital expenditures	$ 1	$ 102	$ 2	$	$	$ 105

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(Dollars in thousands)	Six Months Ended June 30, 2010					
	Retail Banking	Mortgage Banking	Consumer Finance	Other	Eliminations	Consolidated
Revenues:						
Interest income	$ 17,020	$ 860	$ 17,740	$ 101	$ (1,767)	$ 33,954
Gains on sales of loans		8,430			(3)	8,427
Other	2,692	1,089	293	575		4,649
Total operating income	19,712	10,379	18,033	676	(1,770)	47,030
Expenses:						
Interest expense	5,358	115	2,498	511	(1,788)	