

**Federal Deposit Insurance Corporation  
Washington, D.C. 20429**

**FORM 10-Q**

**[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**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**FDIC Certificate number 57524**

**LIBERTY BELL BANK**

(Exact name of registrant as specified in its charter)

**New Jersey**

**22-3811547**

(State or other jurisdiction of incorporation or organization) (IRS Employer Identification Number)

**145 North Maple Avenue, Marlton, New Jersey 08053**

(Address of principal executive offices)

**856 830-1100**

(Registrant's telephone number)

**N/A**

(Former name, former address and former fiscal year, if changed since last report)

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

Yes  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 during the preceding 12 months (or for such shorter period) that the registrant was required to submit and post such files).

Yes  No  (Not applicable)

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

Large accelerated filer  Accelerated filer  Smaller reporting company

Non-accelerated filer  (Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 2,808,551 shares of common stock outstanding as of August 12, 2010.

**LIBERTY BELL BANK**  
**FORM 10-Q**  
**FOR THE QUARTER ENDED June 30, 2010**

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**Liberty Bell Bank****Balance Sheets****June 30, 2010 and December 31, 2009****(Unaudited)**

	2010	2009
<b>Assets</b>		
Cash and cash due from banks	\$ 1,482,822	\$ 1,538,947
Interest-bearing deposits with other banks	1,080,000	7,948,017
Federal funds sold	13,035,000	5,025,000
Cash and cash equivalents	15,597,822	14,511,964
Certificates of deposit with other banks	738,000	980,000
Investment securities available for sale, at fair value	11,330,520	15,830,241
Loans (net of allowance for loan losses of \$1,637,838 and \$1,420,000 at June 30, 2010 and December 31, 2009, respectively)	136,403,641	131,565,224
Bank premises and equipment, net	4,637,346	4,461,772
Federal Home Loan Bank stock, at cost	549,700	534,100
Prepaid FDIC assessment	757,058	878,961
Accrued interest receivable and other assets	1,116,488	1,061,995
Total assets	<u>\$ 171,130,575</u>	<u>\$ 169,824,257</u>
<b>Liabilities and Shareholders' Equity</b>		
<b>Liabilities</b>		
Deposits		
Noninterest-bearing	\$ 12,265,614	\$ 8,123,787
Interest-bearing	137,414,509	140,478,336
Total deposits	149,680,123	148,602,123
Borrowings	7,500,000	7,500,000
Accrued interest payable and other accrued liabilities	530,454	486,011
Total liabilities	<u>157,710,577</u>	<u>156,588,134</u>
<b>Shareholders' Equity</b>		
Common stock, \$5 par value, 5,000,000 shares authorized; Issued and outstanding, 2,808,551 and 2,771,414 shares at June 30, 2010 and December 31, 2009		
	14,042,755	13,857,070
Additional paid-in capital	6,775,377	6,847,071
Accumulated deficit	(7,739,350)	(7,839,590)
Accumulated other comprehensive income	341,216	371,572
Total shareholders' equity	<u>13,419,998</u>	<u>13,236,123</u>
Total liabilities and shareholders' equity	<u>\$ 171,130,575</u>	<u>\$ 169,824,257</u>

See Notes to Financial Statements.

## Liberty Bell Bank

### Statements of Operations (Unaudited)

	Three Months ended, June 30,		Six Months ended, June 30,	
	2010	2009	2010	2009
<b>Interest and Dividend Income</b>				
Interest and fees on loans	\$ 1,929,164	\$ 1,947,044	\$ 3,830,065	\$ 3,876,711
Interest on securities available for sale	124,546	159,763	263,543	360,953
Interest on deposits with banks	6,396	597	20,786	607
Dividends on FHLB stock	6,097	8,569	10,636	14,492
Interest on federal funds sold	5,532	6,601	10,246	9,272
Total interest income	<u>2,071,735</u>	<u>2,122,574</u>	<u>4,135,276</u>	<u>4,262,035</u>
<b>Interest Expense</b>				
Interest on deposits	595,905	882,385	1,230,254	1,788,562
Interest on borrowings	74,759	74,759	148,697	150,431
Total interest expense	<u>670,664</u>	<u>957,144</u>	<u>1,378,951</u>	<u>1,938,993</u>
Net interest income	<u>1,401,071</u>	<u>1,165,430</u>	<u>2,756,325</u>	<u>2,323,042</u>
Provision for Loan Losses	100,000	122,000	220,000	202,000
Net interest income after provision for loan losses	<u>1,301,071</u>	<u>1,043,430</u>	<u>2,536,325</u>	<u>2,121,042</u>
<b>Noninterest Income</b>				
Service charges on deposit accounts	41,065	34,899	82,008	66,126
Other income	27,470	34,536	59,479	69,644
Gain on sale of investment securities available for sale	—	—	72,028	—
Total noninterest income	<u>68,535</u>	<u>69,435</u>	<u>213,515</u>	<u>135,770</u>
<b>Noninterest Expenses</b>				
Compensation and benefits	667,849	597,496	1,341,280	1,193,986
Occupancy	193,856	210,037	390,439	406,697
Equipment and data processing	119,639	111,420	235,015	208,675
Marketing and business development	37,063	32,515	62,913	48,891
Professional services	118,641	119,829	237,557	190,126
Other operating expenses	198,562	252,791	382,397	407,863
Total noninterest expenses	<u>1,335,610</u>	<u>1,324,088</u>	<u>2,649,601</u>	<u>2,456,238</u>
Income Before Income Tax Expense	33,996	(211,223)	100,240	(199,426)
Income Tax Expense	—	—	—	—
Net income (loss)	<u>\$ 33,996</u>	<u>\$ (211,223)</u>	<u>\$ 100,240</u>	<u>\$ (199,426)</u>
Net income Per Share, Basic and Diluted	<u>\$ 0.01</u>	<u>\$ (0.08)</u>	<u>\$ 0.04</u>	<u>\$ (0.07)</u>
Weighted Average Shares Outstanding, Basic and Diluted	<u>2,808,551</u>	<u>2,704,803</u>	<u>2,790,302</u>	<u>2,697,737</u>

See Notes to Financial Statements.

Liberty Bell Bank

Statements of Shareholders' Equity  
Six Months Ended June 30, 2010 and June 30, 2009 (Unaudited)

	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total Shareholders' Equity
Balance, December 31, 2008	\$ 13,452,965	\$ 7,223,776	\$ (7,424,696)	\$ 380,574	\$ 13,632,619
Stock option expense		13,700			13,700
Comprehensive income (loss) :					
Net loss - six months ended June 30, 2009			(199,426)		(199,426)
Common stock dividend issued as a 3 for 100 stock split	404,105	(404,105)			-
Change in net unrealized loss on securities available for sale, net of tax effect, if any				5,900	5,900
Total comprehensive loss					(193,526)
Balance, June 30, 2009	<u>\$ 13,857,070</u>	<u>\$ 6,833,371</u>	<u>\$ (7,624,122)</u>	<u>\$ 386,474</u>	<u>\$ 13,452,793</u>
Balance, December 31, 2009	\$ 13,857,070	\$ 6,847,071	\$ (7,839,590)	\$ 371,572	\$ 13,236,123
Stock issuance - 37,137 shares	185,685	(85,393)			100,292
Stock option expense		13,699			13,699
Comprehensive income (loss):					
Net income - six months ended June 30, 2010			100,240		100,240
Change in unrealized gain on securities available for sale, net of tax effect, if any				41,672	41,672
Reclassification adjustment for (gains) realized, net if tax effect, if any				(72,028)	(72,028)
Total comprehensive income					69,884
Balance, June 30, 2010	<u>\$ 14,042,755</u>	<u>\$ 6,775,377</u>	<u>\$ (7,739,350)</u>	<u>\$ 341,216</u>	<u>\$ 13,419,998</u>

See Notes to Financial Statements

**Liberty Bell Bank**  
**Statements of Cash Flows**

	Six Months ended June 30,	
	2010	2009
<b>Cash Flows from Operating Activities</b>		
Net income (loss)	\$ 100,240	\$ (199,426)
Adjustments to reconcile net income (loss) to net cash provided by (used in ) operating activities:		
Depreciation and amortization	239,083	212,417
Provision for loan losses	220,000	202,000
Origination of loans held for sale	(1,453,200)	(903,546)
Proceeds from the sale of loans held for sale	1,453,200	419,546
Net amortization of securities	4,526	10,209
Gain on sale of investment securities available for sale	(72,028)	-
Stock compensation expense	13,699	13,700
Changes in operating assets and liabilities:		
Amortization of prepaid FDIC assessment	121,903	-
Decrease in accrued interest receivable and other assets	(54,493)	(236,322)
Decrease in accrued interest payable and other liabilities	44,443	39,774
<b>Net cash provided by (used in) operating activities</b>	<b>617,373</b>	<b>(441,648)</b>
<b>Cash Flows from Investing Activities</b>		
Purchases of certificates of deposits with other banks	242,000	-
(Purchase) redemption of FHLB stock	(15,600)	303,100
Purchases of investment securities available for sale	(4,000,000)	(1,500,000)
Proceeds from calls and sales of securities available for sale	7,093,942	10,200,000
Proceeds from principal payments on mortgage-backed securities available for sale	1,442,925	2,607,147
Net increase in loans	(5,058,417)	(8,414,265)
Purchase of bank premises and equipment	(414,657)	(264,878)
<b>Net cash (used in) provided by investing activities</b>	<b>(709,807)</b>	<b>2,628,004</b>
<b>Cash Flows from Financing Activities</b>		
Net decrease in lines of credit borrowings	-	(7,900,000)
Net (decrease) increase in interest-bearing deposits	(3,063,827)	15,465,359
Net increase in noninterest-bearing deposits	4,141,827	226,848
Issuance of common stock	100,292	-
<b>Net cash provided by financing activities</b>	<b>1,178,292</b>	<b>7,792,207</b>
<b>Increase in cash and cash equivalents</b>	<b>1,085,858</b>	<b>9,978,563</b>
Cash and Cash Equivalents, beginning of period	14,511,964	1,215,446
Cash and Cash Equivalents, end of period	\$ 15,597,822	\$ 11,194,009
<b>Supplemental Disclosure of Cash Flow Information:</b>		
Cash paid during the period for:		
Interest on deposits and borrowed funds	\$ 1,412,416	\$ 1,936,581
Income taxes	\$ -	\$ -
Net change in unrealized (loss) gain on investment securities available for sale	\$ (30,356)	\$ 5,900

See Notes to Financial Statements.

## **LIBERTY BELL BANK**

### **NOTES TO THE FINANCIAL STATEMENTS (UNAUDITED)**

#### **NOTE 1. - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

##### **Nature of Operations**

Liberty Bell Bank (the "Bank") is a commercial bank, which was incorporated on November 26, 2002, and commenced operations on August 11, 2003. The Bank is chartered by the New Jersey Department of Banking and Insurance and insured by the Federal Deposit Insurance Corporation ("FDIC"). The Bank became a public filer in April of 2004 when it filed its Form 10-SB Registration Statement with the FDIC. The Bank moved its principal office from Cherry Hill to Evesham, New Jersey that houses the Bank's Operations Center and administrative headquarters on September 3, 2009. In addition to its offices in Cherry Hill and Evesham Township, the Bank also has branch offices in Moorestown and in Mount Laurel. The Bank provides financial services primarily to Camden and Burlington Counties, as well as surrounding counties in New Jersey and Southeastern Pennsylvania. In April 2004, the Bank purchased land with a building in the Township of Voorhees, Camden County, New Jersey. To date, the Bank has not requested regulatory approval to open a branch office at the Voorhees location. The Bank is actively marketing this property for sale.

##### **Financial Statements**

The financial statements as of June 30, 2010, and for the three and six-months ended June 30, 2010 and 2009, included herein have not been audited. The December 31, 2009 Balance Sheet is derived from the audited financial statements. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted ("GAAP") in the United States of America have been condensed or omitted; therefore, these financial statements should be read in conjunction with the Bank's 2009 Annual Report on Form 10-K, as filed with the Federal Deposit Insurance Corporation ("FDIC"). The accompanying financial statements reflect all adjustments, which are, in the opinion of management, necessary to present a fair statement of the results for the interim periods presented. Such adjustments are of a normal recurring nature. The results for the three and six-month periods ended June 30, 2010 are not necessarily indicative of the results that may be expected for the year ending December 31, 2010. The Bank has evaluated subsequent events for potential recognition and/or disclosure from the date of the financial statements included in this quarterly report on Form 10-Q through the date of its filing with the FDIC.

##### **Use of Estimates**

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the 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 significantly from such estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation of deferred tax assets.

## LIBERTY BELL BANK

### NOTES TO THE FINANCIAL STATEMENTS (UNAUDITED)

#### NOTE 1. – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (continued)

##### Accounting Standards Codification:

The Financial Accounting Standards Board's (FASB) Accounting Standards Codification (ASC) became effective on July 1, 2009. At that date, the ASC became FASB's officially recognized source of authoritative U.S. generally accepted accounting principles (GAAP) applicable to all public and non-public non-governmental entities, superseding 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 the authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. All other accounting literature is considered non-authoritative. The switch to the ASC affects the way companies refer to U.S. GAAP in financial statements and accounting policies. The codification became effective for interim and annual periods ending on or after September 15, 2009. Accordingly, the Bank's accounting policies, which are consistent with prior periods and detailed below are now in accordance with ASC and no longer contain references to Statements on Financial Accounting Standards (SFAS), or related literature.

##### Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses. Loans that are determined to be uncollectible are charged against the allowance account, and subsequent recoveries, if any, are credited to the allowance. When evaluating the adequacy of the allowance, an assessment of the loan portfolio will typically include changes in the composition and volume of the loan portfolio, overall portfolio quality and past loss experience, review of specific problem loans, current economic conditions which may affect borrowers' ability to repay, and other factors which may warrant current recognition. Such periodic assessments may, in management's judgment, require the Bank to recognize additions or reductions to the allowance.

Various regulatory agencies periodically review the adequacy of the Bank's allowance for loan losses as an integral part of their examination process. Such agencies may require the Bank to recognize additions or reductions to the allowance based on their judgments of information available to them at the time of their examination. It is reasonably possible that the above factors may change significantly and, therefore, affect management's determination of the allowance for loan losses in the near term.

The allowance consists of specific and general components. The specific component relates to loans that are deemed impaired. For those loans that are classified as impaired, an allowance is established when the discounted cash flows, the collateral value or the observable market price of the impaired loan is lower than the carrying value of that loan. The general component covers nonimpaired loans and is based on environmental factors including growth and volume trends, credit concentrations, collateral quality, delinquency/impairment trends, historical charge-off experience and expected loss given default derived from the Bank's internal risk rating process. Other adjustments may be made to the allowance for pools of loans after an assessment of internal or external influences on credit quality that are not fully reflected in the historical loss or risk rating data.

## **NOTE 1. – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (continued)**

### **Allowance for Loan Losses**

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer and residential loans for impairment disclosures.

### **Securities Available for Sale**

Securities classified as available for sale are stated at fair value. Unrealized gains and losses are excluded from earnings and are reported net of tax as a separate component of shareholders' equity. Such items, along with net income, are components of comprehensive income. Realized gains and losses are determined using the specific-identification method and are included in earnings on the trade date. The Bank classified all of its securities as available for sale at June 30, 2010 and December 31, 2009.

### **Income Taxes**

The Bank accounts for income taxes according to the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using the enacted tax rates applicable to taxable income for the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Valuation reserves are established against certain deferred tax assets when it is more likely than not that the deferred tax assets will not be realized. Increases or decreases in the valuation reserve are charged or credited to the income tax provision.

When tax returns are filed, it is highly certain that some positions taken would be sustained upon examination by the taxing authorities, while others are subject to uncertainty about the merits of the position taken or the amount of the position that ultimately would be sustained. The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, management believes it is more-likely-than not that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. The evaluation of a tax position taken is considered by itself and not offset or aggregated with other positions.

## **NOTE 1. – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (continued)**

### **Income Taxes**

Tax positions that meet the more-likely-than not recognition threshold are measured as the largest amount of tax benefit that is more than 50 percent likely of being realized upon settlement with the applicable taxing authority. The portion of benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the accompanying balance sheet along with any associated interest and penalties that would be payable to the taxing authorities upon examination.

Interest and penalties associated with unrecognized tax benefits are recognized in income tax expense on the income statement.

### **New Accounting Pronouncements**

New authoritative guidance (Accounting Standards Update No. 2010-20) requires an entity to provide disclosures that facilitate financial statement users' evaluation of the following:

- The nature of credit risk inherent in the entity's portfolio of financing receivables;
- How that risk is analyzed and assessed in arriving at the allowance for credit losses; and
- The changes and reasons for those changes in the allowance for credit losses.

To achieve these objectives, an entity should provide disclosures on a disaggregated basis on two defined levels: (1) portfolio segment; and (2) class of financing receivable. The new authoritative guidance makes changes to existing disclosure requirements and includes additional disclosure requirements about financing receivables, including:

- Credit quality indicators of financing receivables at the end of the reporting period by class of financing receivables;
- The aging of past due financing receivables at the end of the reporting period by class of financing receivables; and
- The nature and extent of troubled debt restructurings that occurred during the period by class of financing receivables and their effect on the allowance for credit losses.

The disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. The Bank is currently evaluating the impact of the guidance on its financial statements.

New authoritative accounting guidance (Accounting Standards Update No. 2010-6) provides amendments to ASC Topic 820 that require new disclosures as follows: 1) A reporting entity should disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers. 2) In the reconciliation for fair value measurements using significant unobservable inputs (Level 3), a reporting entity should present separately information about purchases, sales, issuances, and settlements (that is, on a gross basis rather than as one net number). The new authoritative guidance also clarifies existing disclosures as follows: 1) A reporting entity should provide fair value measurement disclosures for each class of assets and liabilities. A class is often a subset of assets or liabilities within a line item in the statement of financial position. A reporting entity needs to use judgment in determining the appropriate classes of assets and liabilities. 2) A reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements that fall in either Level 2 or Level 3.

## **NOTE 1. – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (continued)**

These new disclosures and clarifications of existing disclosures were effective for the Bank's financial statements beginning after December 15, 2009, (except for the disclosures about the purchases, sales, issuances, and settlements in the roll forward activity of Level 3 fair value measurements, which is effective for fiscal years beginning after December 15, 2010) and did not have a significant impact on the Bank's financial statements.

FASB ASC Topic 860, "Transfers and Servicing." New authoritative accounting guidance under ASC Topic 860, "Transfers and Servicing," amends prior accounting guidance to enhance reporting about transfers of financial assets, including securitizations, and where companies have continuing exposure to the risks related to transferred financial assets. The new authoritative accounting guidance eliminates the concept of a "qualifying special-purpose entity" and changes the requirements for derecognizing financial assets. The new authoritative accounting guidance also requires additional disclosures about all continuing involvements with transferred financial assets including information about gains and losses resulting from transfers during the period. The new authoritative accounting guidance under ASC Topic 860 became effective January 1, 2010 and did not have a significant impact on the Bank's financial statements.

## **NOTE 2. – EARNINGS PER COMMON SHARE**

Basic earnings per common share is computed by dividing net income available to common stockholders (the numerator) by the weighted average number of common shares outstanding (the denominator) during the period. Shares issued during the period are weighted for the portion of the period that they were outstanding. The weighted average number of common shares outstanding for the three months ended June 30, 2010 and 2009 were 2,808,551 and 2,704,803 and for the six months ended June 30, 2010 and 2009 were 2,790,302 and 2,697,737, respectively.

Diluted earnings per common share consider common stock equivalents (when dilutive) outstanding during the period such as options outstanding. The assumed conversion of these options had an anti-dilutive effect on the calculation of dilutive earnings per share for the three and six month periods ended June 30, 2010 and 2009; accordingly, they were not considered in the dilutive earnings per share computation.

## **NOTE 3. – COMPREHENSIVE INCOME (LOSS)**

Total comprehensive income (loss) includes net income (loss) and other comprehensive income or loss that is comprised of unrealized gains and losses on investment securities available for sale, and the adjustment for realized gain from the sale of securities from the available for sale portfolio net of taxes. The Bank's total comprehensive income (loss) for the three months ended June 30, 2010 and 2009 was \$60,123 and (\$272,424), respectively. The Bank's total comprehensive income (loss) for the six month ended June 30, 2010 and 2009 was \$69,884 and (\$193,526), respectively. The difference between the Bank's net income (loss) and total comprehensive income for these periods relates to the change in net unrealized gains and losses on investment securities available for sale during the applicable period of time and in 2010 the adjustment for realized gain on the sale of investment securities from the available for sale portfolio.

## **NOTE 4. – REGULATORY MATTERS**

The Bank is subject to various regulatory capital requirements administered by federal and state banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly

## REGULATORY MATTERS – (continued)

additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of its assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) 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). Management believes, as of June 30, 2010 and December 31, 2009, that the Bank met all capital adequacy and other regulatory requirements to which it is subject.

The Bank's actual capital amounts and ratios as of June 30, 2010 and December 31, 2009 are presented in the following tables:

	Actual		For Capital Adequacy Purposes		To Be Well-Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(dollars in thousands)						
<b>As of June 30, 2010:</b>						
Total risk based capital (to risk weighted assets)	\$ 14,717	10.71%	\$ 10,992	8.00%	\$ 13,740	10.00%
Tier I capital (to risk weighted assets)	13,079	9.52%	5,496	4.00%	8,244	6.00%
Tier I capital (to average assets)	13,079	7.80%	6,705	4.00%	8,381	5.00%
<b>As of December 31, 2009:</b>						
Total risk based capital (to risk weighted assets)	\$ 14,285	10.46%	\$ 10,993	8.00%	\$ 13,653	10.00%
Tier I capital (to risk weighted assets)	12,865	9.42%	5,461	4.00%	8,192	6.00%
Tier I capital (to average assets)	12,865	7.44%	6,919	4.00%	8,649	5.00%

## NOTE 5. – SHARE BASED PAYMENT

On February 24, 2004, the Bank adopted the 2004 Incentive Stock Option Plan and the 2004 Non Qualified Stock Option Plan, which are stock-based incentive compensation plans (the "Plans"), authorizing an aggregate of 127,596 stock-based awards.

FASB ASC Topic 718, "Compensation – Stock Compensation," requires the Bank to recognize the fair value of stock option awards over a vesting period. Compensation costs totaling \$6,849 and \$6,850 for

**NOTE 5. – SHARE BASED PAYMENT – (continued)**

the three months ended June 30, 2010 and 2009. For the six months ended June 30, 2010 and 2009 total compensation costs were \$13,699 and \$13,700 respectively. As of June 30, 2010, aggregate unrecognized compensation costs of approximately \$48 thousand related to the non-vested share based compensation arrangements existed under Bank's stock option plans. The cost is expected to be recognized over a weighted average period of 1.7 years, the estimated remaining vesting period.

Transactions under the Bank's stock option plans during the quarter ended June 30, 2010 are summarized as follows:

<b>Options</b>	<b>Shares</b>	<b>Weighted Average Exercise Price</b>	<b>Average Remaining Contractual Term</b>	<b>Aggregate Intrinsic Value</b>
Outstanding at January 1, 2010	107,260	\$ 5.79	6.6 years	\$ -
Granted	-	-	-	-
Exercises	-	-	-	-
Expired/Terminated	(5,073)	5.79	6.2 years	-
Outstanding at June 30, 2010	102,187	\$ 5.79	6.1 years	\$ -
Exercisable at June 30, 2010	74,550	\$ 5.86	5.9 years	\$ -

A summary of the status of the Bank's non-vested shares as of June 30, 2010 is as follows:

	<b>Shares</b>	<b>Weighted Average Grant-Date Fair Value</b>
Nonvested at January 1, 2010	43,495	\$1.74
Granted	-	
Vested	(14,499)	1.74
Expired/Terminated	(1,359)	1.74
Nonvested at June 30, 2010	27,637	\$1.74

## NOTE 6. – AVAILABLE FOR SALE SECURITIES PORTFOLIO

The following table provides the major components of securities available for sale at amortized cost and estimated fair value at June 30, 2010 and December 31, 2009. All securities held in the available for sale portfolio are U.S government agencies or government-sponsored enterprises.

	Amortized Cost	Unrealized Gains	Unrealized Losses	Market Value
<u>Available For Sale</u>				
U.S. Government agency obligations	\$ 3,000,000	\$ 4,622	\$ -	\$ 3,004,622
Mortgage-backed securities issued by				
Ginnie Mae	1,930,813	45,215	-	1,976,028
Fannie Mae	3,398,884	155,607	-	3,554,491
Freddie Mac	2,659,607	135,772	-	2,795,379
Total securities available for sale	<u>\$ 10,989,304</u>	<u>\$ 341,216</u>	<u>\$ -</u>	<u>\$ 11,330,520</u>

	December 31, 2009			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
<u>Available For Sale</u>				
U.S. Government agency obligations	\$ 4,500,000	\$ 4,604	\$ (15,973)	\$ 4,488,631
Mortgage-backed securities issued by				
Ginnie Mae	2,012,069	4,064	(6,253)	2,009,880
Fannie Mae	5,671,172	230,340	-	5,901,512
Freddie Mac	3,275,428	154,790	-	3,430,218
Total securities available for sale	<u>\$ 15,458,669</u>	<u>\$ 393,798</u>	<u>\$ (22,226)</u>	<u>\$15,830,241</u>

## NOTE 6. – AVAILABLE FOR SALE SECURITIES PORTFOLIO – (continued)

The table below provides the remaining contractual maturities of U.S. callable agencies and mortgage-backed securities which may have principal repayment provisions, are distributed based on contractual maturities. Expected maturities may differ materially from contractual maturities as a result of early prepayments and calls.

(Dollars in thousands)	At June 30, 2010									
	Within 1 Year		After 1 Within 5 Years		Over 5 Years		Total			
	Value	Yield	Market Value	Yield	Market Value	Yield	Market Value	Yield	Market Value	Yield
Investment securities available for sale:										
U.S. Government agency obligations	\$ -	-	\$ 2,002	1.13%	\$ 1,003	4.00%	\$ 3,005	2.08%		
Mortgage-backed securities issued by										
Ginnie Mae	-	-	-	-	1,976	4.25%	1,976	4.25%		
Fannie Mae	-	-	-	-	3,555	4.37%	3,555	4.37%		
Freddie Mac	-	-	-	-	2,795	4.95%	2,795	4.95%		
Total available for sale	\$ -	-	\$ 2,002	1.13%	\$ 9,329	4.47%	\$ 11,331	3.86%		

For the three and six month periods ended June 30, 2010, gross realized gains on sales of available for sale securities amounted to \$0 and \$72,028, respectively. There were no gross realized losses incurred during these periods. There were no gross realized gains or losses for the three and six month periods ended June 30, 2009.

The Bank has a process in place to identify debt securities that could potentially have a credit impairment that is other-than-temporary. This process involves monitoring late payments, pricing levels, downgrades by rating agencies, key financial ratios, financial statements, revenue forecasts and cash flow projections as indicators of credit issues. On a quarterly basis, we review all securities to determine whether other-than-temporary decline in value exists and whether losses should be recognized. We consider relevant facts and circumstances in evaluating whether a credit or interest rate-related impairment of a security is other-than-temporary. Relevant facts and circumstances considered include: (1) the extent and length of time the fair value has been below cost; (2) the reasons for the decline in value; (3) the financial position and access to capital of the issuer, including the current and future impact of any specific events and (4) for fixed maturity securities, our intent to sell a security or whether it is more likely than not we will be required to sell the security before the recovery of its amortized cost which, in some cases, may extend to maturity and for equity securities, our ability and intent to hold the security for a period of time that allows for the recovery in value.

**NOTE 6. – AVAILABLE FOR SALE SECURITIES PORTFOLIO – (continued)**

There were no securities in a continuous unrealized loss position as of June 30, 2010. Provided below is a summary of the Bank's investment securities that were in a continuous unrealized loss position as of December 31, 2009.

Available for Sale:	December 31, 2009			
	Continuous Unrealized Losses Existing for Less than 12 Months		Continuous Unrealized Losses Existing for 12 Months of More	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. Government agencies	\$ 2,984,027	\$ 15,973	\$ -	\$ -
Mortgage-backed securities issued by Ginnie Mae	1,000,742	6,253	-	-
Total securities available for sale	<u>\$ 3,984,769</u>	<u>\$ 22,226</u>	<u>\$ -</u>	<u>\$ -</u>

**U.S. Government and Agency Obligations.** The unrealized losses on the Bank's investment in U.S. Government agencies were caused by interest rate increases. The principal of those investments are guaranteed by an agency of the U.S. government. Accordingly, it is expected that the securities would not be settled at a price less than the amortized cost bases of the Bank's investments. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Bank does not intend to sell the investments and it is not more likely than not that the Bank will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Bank did not consider the three agencies callable (FNMA) at December 31, 2009 to be other-than-temporarily impaired.

**Residential Mortgage-Backed Securities** The unrealized losses on the Bank's investment in federal agency mortgage-backed securities were caused by interest rate increases. The contractual cash flows of these investments are guaranteed by an agency of the U.S. government. Accordingly, it is expected that the securities would not be settled at a price less than the amortized cost bases of the Bank's investments. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Bank does not intend to sell the investments and it is not more likely than not that the Bank will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Bank did not consider the one agency residential mortgage-backed security (GNMA) at December 31, 2009 to be other-than-temporarily impaired. The Bank uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. In accordance with the Fair Value Measurements and Disclosures topic of FASB ASC 820, the fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

## **NOTE 7 – Fair Value of Financial Instruments**

Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Bank's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

The recent fair value guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions. In accordance with this guidance, the Bank groups its assets and liabilities carried at fair value in three levels as follows:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a reporting entity's assumptions about the assumptions that market participants would use in pricing an asset or liability.

A financial instrument's categorization within the valuation hierarchy is based on the lowest level of input that is significant to the fair value measurement.

### **Fair Value on a Recurring Basis**

Securities Available for Sale ("AFS"): Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities would include highly liquid government bonds and exchange traded equities. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics, or discounted cash flow. Level 2 securities would include U.S. agency securities and mortgage backed agency securities, obligations of states and political subdivisions and certain corporate, asset backed and other securities. In certain cases where there is limited activity or less transparency around inputs to the valuation, securities are classified within Level 3 of the valuation hierarchy.

As of June 30, 2010, the fair value of the Bank's AFS securities portfolio was \$11,330,520. Approximately 73 percent of the portfolio was made up of residential mortgage-backed securities, which had a fair value of \$8,325,898 at June 30, 2010. All the residential mortgage-backed securities were issued or are guaranteed by the Government National Mortgage Association ("GNMA"), the Federal National Mortgage Association ("FNMA") or the Federal Home Loan Mortgage Corporation ("FHLMC"). The underlying loans for these securities are residential mortgages that are geographically dispersed throughout the United States. All AFS securities were classified as Level 2 assets at June 30, 2010. The valuation of AFS securities using Level 2 inputs was primarily determined using the market approach, which uses quoted prices for similar securities and all relevant information.

## Fair Value on a Recurring Basis – (continued)

The following tables summarize the available for sale securities measured at fair value as of June 30, 2010 and December 31, 2009, respectively, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value on a recurring basis.

	June 30, 2010			
Available for Sale	Total	Level 1	Level 2	Level 3
U.S. Government agencies	\$ 3,004,622	\$ -	\$ 3,004,622	\$ -
Mortgage-backed securities issued by				
Ginnie Mae	1,976,028	-	1,976,028	-
Fannie Mae	3,554,491	-	3,554,491	-
Freddie Mac	2,795,379	-	2,795,379	-
Total securities available for sale	\$ 11,330,520	\$ -	\$ 11,330,520	\$ -

	December 31, 2009			
Available for Sale	Total	Level 1	Level 2	Level 3
U.S. Government agencies	\$ 4,488,631	\$ -	\$ 4,488,631	\$ -
Mortgage-backed securities issued by				
Ginnie Mae	2,009,880	-	2,009,880	-
Fannie Mae	5,901,512	-	5,901,512	-
Freddie Mac	3,430,218	-	3,430,218	-
Total securities available for sale	\$ 15,830,241	\$ -	\$ 15,830,241	\$ -

## Fair Value on a Non-Recurring Basis

Certain assets and liabilities are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

### Impaired Loans

The carrying value of impaired loans is derived in accordance with FASB ASC Topic 310, "Receivables". Fair value is determined based on the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. Appraised and reported values may be discounted based on management's historical knowledge, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the client and client's business. The valuation allowance for impaired loans is included in the allowance for loan losses in the balance sheets. The valuation allowance for impaired loans at June 30, 2010 and December 31, 2009 was \$416,000 and \$234,000 respectively.

## Impaired Loans – (continued)

The following tables presents the financial assets carried on the balance sheet by caption and by level within the fair value hierarchy (as described above) as of June 30, 2010 and December 31, 2009 for which a nonrecurring change in fair value has been recorded during the six and twelve months periods ended in each respective year.

June 30, 2010

	Level 1	Level 2	Level 3	Total
Impaired Loans	-	-	\$ 1,729,000	\$ 1,729,000

December 31, 2009

	Level 1	Level 2	Level 3	Total
Impaired Loans	-	-	\$ 1,624,000	\$ 1,624,000

There were no changes in the inputs or methodologies used to determine fair value during the quarter ended June 30, 2010 as compared to the quarters ended December 31, 2009 and June 30, 2009.

## Fair Value of Financial Instruments

FASB ASC Topic 825, "Financial Instruments," requires the disclosure of the estimated fair value of certain financial instruments, including those financial instruments for which the Company did not elect the fair value option. These estimated fair values as of September 30, 2009 and December 31, 2008 have been determined using available market information and appropriate valuation methodologies. Considerable judgment is required to interpret market data to develop estimates of fair value. The estimates presented are not necessarily indicative of amounts the Company could realize in a current market exchange. The use of alternative market assumptions and estimation methodologies could have had a material effect on these estimates of fair value. The following methods and assumptions were used to estimate the fair value of other financial instruments for which it is practicable to estimate that value:

Cash and Cash Equivalents: The carrying amount of cash and short-term investments approximates fair value.

Investment Securities Available for Sale: The fair value of investment securities is detailed above.

Certificates of Deposit with Banks: The carrying amount of interest bearing deposits with other banks approximates fair value.

Loans other than Impaired Loans: Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as commercial, residential mortgage and other consumer. Each loan category is further segmented into groups by fixed and adjustable rate interest terms and by performing and non-performing categories.

The fair value of performing loans is typically calculated by discounting scheduled cash flows through their estimated maturity, using estimated market discount rates that reflect the credit and interest rate risk inherent in each group of loans. The fair value of non-performing loans is detailed above. The estimate of maturity is based on contractual maturities for loans within each group, or on the Bank's historical experience with repayments for each loan classification, modified as required by an estimate of the effect of current economic conditions. For all loans, assumptions regarding the characteristics and segregation of loans, maturities, credit risk and cash flows, and discount rates are judgmentally determined using specific borrower and other available information.

Federal Home Loan Bank Stock: The carrying value of restricted stock approximates fair value based on redemption provisions.

Accrued Interest Receivable and Payable: The fair value of interest receivable and payable is estimated to approximate the carrying amounts.

Deposits: The fair value of deposits with no stated maturity, such as demand deposits, checking accounts, savings and money market accounts, is equal to the carrying amount. The fair value of certificates of deposit is based on the discounted value of contractual cash flows, where the discount rate is estimated using market rates currently offered for deposits of similar remaining maturities.

Borrowings: The fair values of borrowings are estimated using discounted cash flow analysis based on the Bank's current market rates for similar types of borrowing arrangements.

Off-Balance Sheet Instruments: Since the majority of the Bank's off-balance sheet instruments are not fee-producing, variable rate commitments, the Bank has determined that they do not have a distinguishable fair value.

The following table summarizes carrying amounts and fair values for financial instruments at June 30, 2010 and December 31, 2009.

	June 30, 2010		December 31, 2009	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<b>Financial Assets:</b>				
Cash and cash equivalents	\$ 15,597,822	\$ 15,597,822	\$ 14,511,964	\$ 14,511,964
Certificates of deposit with other banks	738,000	738,000	980,000	980,000
Investment securities	11,330,520	11,330,520	15,830,241	15,830,241
Loans, net	136,403,641	135,812,000	131,565,224	131,671,000
Federal Home Loan Bank, stock	549,700	549,700	534,100	534,100
Accrued interest receivable	513,458	513,458	512,731	512,731
<b>Financial Liabilities</b>				
Demand deposits interest, and non-interest-bearing, and savings deposits	63,659,418	63,659,418	54,934,871	54,934,871
Time deposits	86,020,705	87,111,000	93,667,252	94,861,000
Borrowings	7,500,000	8,612,000	7,500,000	8,731,000
Accrued interest payable	172,366	172,366	205,831	205,831

## NOTE 8 – Impaired Loans and the Allowance For Loan Losses

Summaries of information pertaining to impaired and non-accrual loans are as follows:

	June 30, 2010	December 31, 2009
Impaired loans without a valuation allowance	\$ 8,158,000	\$ 6,045,000
Impaired loans with a valuation allowance	2,145,000	1,858,000
Total Impaired loans	<u>10,303,000</u>	<u>7,903,000</u>
Valuation allowance related to impaired loans	416,000	234,000
Average investment in impaired loans	9,247,000	6,414,000
Total non-accrual loans (included in impaired loans)	6,309,000	5,903,000

Impaired loans without a valuation allowance increased \$2.1 million since December 31, 2009 as a result of the designating new loans as impaired where the current appraisal supports the full amount of the loan .

## Allowance for Loan Losses

Changes in the allowance for loan losses are as follows

	For the three months ended June 30,		For the six months ended June 30,	
	2010	2009	2010	2009
Balance, beginning of period	\$ 1,537,838	\$ 1,213,445	\$ 1,420,000	\$ 1,326,676
Provision for loan losses	100,000	122,000	220,000	202,000
Charge-offs	-	-	(2,162)	(196,231)
Recoveries	-	-	-	-
Balance, at end of period	<u>\$ 1,637,838</u>	<u>\$ 1,335,445</u>	<u>\$ 1,637,838</u>	<u>\$ 1,332,445</u>
Average loans outstanding (1)	<u>\$133,936,207</u>	<u>\$132,429,963</u>	<u>\$ 133,437,036</u>	<u>\$ 130,027,190</u>

(1) Includes non-accruing loans

## **ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

### **Forward-Looking Statements**

This report contains certain "forward-looking statements" which are made by the Bank in good faith pursuant to the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements, include statements of the Bank's plans, objectives, expectations, estimates and intentions, involve risks and uncertainties and are subject to change based on various important factors (some of which are beyond the Bank's control). The following factors, among others could cause the Bank's financial performance to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements: unexpected loan losses, the strength of the United States economy in general and the strength of the local economies in which the Bank conducts operations; 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 of the Bank and the perceived overall value of these products and services by users, including the features, pricing and quality compared to competitors' products and services; 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; and the success of the Bank at managing the risks involved in the foregoing.

The Bank cautions that the foregoing list of important factors is not exclusive. The Bank also cautions readers not to place undue reliance on these forward-looking statements, which reflect management's analysis only as of the date on which they are given. The Bank is not obligated to publicly revise or update these forward-looking statements to reflect events or circumstances that arise after any such date. Readers should carefully review the other documents the Bank files from time to time with the FDIC, including other quarterly reports on Form 10-Q, annual reports on Form 10-K and any current reports on Form 8-K.

### **General**

The Bank's results of operations are dependent primarily on net interest income, which is the difference between the interest income earned on its interest-earning assets, such as loans and securities, and the interest expense paid on its interest-bearing liabilities, such as deposits and borrowings. The Bank also generates noninterest income such as service charges and other fees. The Bank's noninterest expenses primarily consist of compensation and benefits, occupancy expenses, equipment and data processing expenses, marketing and business development costs, professional services and other operating expenses. The Bank is also subject to losses from its loan portfolio if borrowers fail to meet their obligations. The Bank's results of operations are also significantly affected by general economic and competitive conditions, particularly changes in market interest rates, government policies and actions of regulatory agencies.

## **Critical Accounting Policy**

### **Allowance for Losses on Loans**

The allowance for losses on loans is based on management's ongoing evaluation of the loan portfolio and reflects an amount considered by management to be its best estimate of known and inherent losses in the portfolio. Management considers a variety of factors when establishing the allowance, such as the impact of current economic conditions, diversification of the loan portfolio, delinquency statistics, results of loan review and related classifications, and historic loss rates. In addition, certain individual loans which management has identified as problematic are specifically provided for, based upon an evaluation of the borrower's perceived ability to pay, the estimated adequacy of the underlying collateral and other relevant factors. Consideration is also given to examinations performed by regulatory agencies. Although provisions have been established and segmented by type of loan, based upon management's assessment of their differing inherent loss characteristics, the entire allowance for losses on loans is available to absorb further loan losses in any category.

Management uses significant estimates to determine the allowance for loan losses. Since the allowance for loan losses is dependent, to a great extent, on conditions that may be beyond the Bank's control, it is at least reasonably possible that management's estimate of this allowance for loan losses and actual results could differ in the near term.

In addition, regulatory authorities, as an integral part of their examinations, periodically review the allowance for loan losses. They may require additions to the allowance based upon their judgments about information available to them at the time of examination.

## Comparison of Results of Operations for the Three Months Ended June 30, 2010 and 2009

(UNAUDITED)

The following discussion and analysis is intended to provide information about the results of operations for the three month period ended June 30, 2010 (unaudited) compared to the results of operations for the three month period ended June 30, 2009 (unaudited). This discussion should be read in conjunction with the accompanying financial statements (unaudited) and related notes as well as statistical information included in this Form 10-Q.

### Results of Operations

**Net Income.** The Bank recorded net income of \$34 thousand or \$0.01 per basic and diluted common share for the three months ended June 30, 2010, an increase of \$245 thousand as compared to a net loss of \$211 thousand or \$(0.08) per basic and diluted common share for the three months ended June 30, 2009. Earnings were driven primarily by a \$236 thousand increase in net interest income to \$1.4 million for the period ending June 30, 2010, supplemented by a reduction in the provision for loan losses of \$22 thousand to \$100 thousand and offset by slightly higher noninterest expenses, specifically compensation and benefits as the Bank hired a Chief Deposit Officer and support staff to strengthen its business development efforts.

**Net Interest Income.** Net interest income, which is the primary source of earnings for the Bank, is the difference between interest income earned on interest-earning assets, such as loans, investment securities and federal funds sold, and interest expense incurred on the interest-bearing sources of funds, such as, interest-bearing demand, savings and time deposits and borrowings. The level of net interest income is determined primarily by the average balances ("volume") and the rate spreads between the interest-earning assets and interest-bearing liabilities, in the second quarter of 2010. Net interest income, before the provision for loan losses, increased \$236 thousand to \$1.4 million for the three months ended June 30, 2010, compared to net interest income of \$1.2 million for the comparable prior year period. Although interest income decreased \$51 thousand to \$2.1 million for the three months ended June 30, 2010, this was more than offset by a \$287 thousand decrease in interest expense during the period.

Interest income on loans decreased \$18 thousand over these periods. The decrease in interest income on loans is primarily due to the increase in non-accrual loans since the second quarter of 2009, as these loans would have added \$65 thousand to the Bank's interest income for the three months ended June 30, 2010. The Bank had one loan past due greater than 90 days and still accruing at June 30, 2010 compared to none for the same period 2009. The Bank is continuing to accrue interest on this loan because management has determined that it is both well secured and in the process of collection. In addition, interest income generated from the security portfolio decreased \$38 thousand. This can be attributed to a decline in the average yield earned from the security portfolio from 4.38 percent to 3.31 percent. These unfavorable variances in interest income were partially offset by increased interest income generated from deposits with other banks, compared to the second quarter of 2009. Interest income from deposits with other banks was \$6 thousand for the three month period ending June 30, 2010 compared to \$597 for the same period ending 2009.

**Interest expense** was \$671 thousand for the three months ended June 30, 2010, compared to \$957 thousand for the second quarter of 2009. The decrease was due to \$287 thousand decline in interest expense on deposits resulting from a decrease in the average cost of deposits from 2.52 percent to 1.63 percent.

## Results of Operations – (continued)

The decreased interest expense was offset in part, by higher average deposit balances that grew an average of \$5.9 million to \$146.3 million from prior year levels. The reduced average interest rates paid on each of the Bank's deposit classifications during the second quarter 2010 compared to the same period of 2009 reflects a general trend of declining market rates for deposits and management's continued efforts to improve the net interest margin in a challenging interest rate environment.

The largest contributors to lower interest expense for the second quarter of 2010 compared to the same period in 2009 were time deposit accounts. Interest expense on time deposit accounts decreased \$275 thousand over the same period last year as average rates paid declined to 2.21 percent from 3.31 percent. In addition, interest paid on interest bearing checking and savings accounts decreased \$14 thousand and \$9 thousand, respectively, when compared to the second quarter 2009. The average rate paid on interest bearing checking decreased from 1.40 percent in the second quarter 2009 to 1.01 percent in the second quarter 2010 while the average rate paid on savings accounts fell 0.23 percent to 0.62 percent. These favorable variances were partially offset by increased interest expense on money market accounts of \$11 thousand as balances in this deposit classification increased by \$7.6 million on average while the average rates paid declined from 1.59 percent at June 31, 2010 to 1.18 percent for the comparable period in 2010. Long term borrowing levels and rates for the period ending June 30, 2010 and June 30, 2009 were unchanged.

**Noninterest Income.** Noninterest income decreased \$1 thousand from \$69 thousand for the second quarter of 2009 to \$68 thousand for the same period in 2010. Service charges on deposit accounts increased \$6 thousand from \$35 thousand in the second quarter of 2009 to \$41 thousand for the second quarter 2010 reflecting the higher deposit fee structure introduced by the Bank effective September 1, 2009. This favorable variance was offset by lower other income that decreased from \$34 thousand in the second quarter 2009 by \$7 thousand to \$27 thousand for the comparable period in 2010.

**Provision for Loan Losses.** The provision for loan losses decreased \$22 thousand to \$100 thousand for the three months ended June 30, 2010, compared to \$122 thousand for the same period in 2009. When determining the provision for loan losses, management assesses the risk inherent in the Bank's loan portfolio based upon information available at such time relating to the composition and volume of the loan portfolio, overall portfolio quality and past loss experience, review of specific problem loans, current economic conditions which may affect borrowers' ability to repay, and other factors which may warrant current recognition. Consistent with the Bank's policy, the provision of \$100 thousand for the second quarter of 2010 represents the provision determined appropriate relative to loan growth and quality necessary to maintain an adequate allowance for loan losses. The allowance for loan losses increased \$218 thousand to \$1.6 million at June 30, 2010 from \$1.4 million at December 31, 2009. Through June 30, 2010, the Bank has charged the allowance for loan losses \$3 thousand related to interest income originally recorded in 2009 related to three loans placed on a non-accrual status during the first quarter 2010.

**Noninterest Expenses.** Total noninterest expense increased \$12 thousand remaining at \$1.3 million for the three months ended June 30, 2010, compared to the same period in 2009. The increase is primarily attributable to higher compensation and benefits, equipment and marketing costs offset by lower occupancy and FDIC insurance premiums. Compensation and benefits increased \$71 thousand to \$668 thousand for the period ending June 30, 2010 compared to \$597 thousand for the same period in 2009. Increased compensation and benefits can be attributed to the hiring of a chief deposit officer, a business development support staff member and higher costs for related taxes and medical insurance coverage.

## Results of Operations – (continued)

Equipment and data processing expense totaled \$120 thousand at June 30, 2010 compared to \$111 thousand for the comparable period in 2009, an increase of \$9 thousand. Higher equipment and data processing costs can be attributed to increased maintenance, license fees and depreciation costs incurred as the Bank continues to grow. Marketing expenditures increased \$5 thousand to \$37 thousand at June 30, 2010 from \$32 thousand for the comparable period in 2009. This increase in costs can be attributed to business development initiatives introduced by the chief deposit officer to spur name recognition in communities serviced by the Bank. Occupancy expenses decreased by \$16 thousand from \$210 thousand at June 30, 2009 to \$194 thousand at June 30, 2010 as the Bank negotiated a \$3 thousand reduction in its monthly lease payments with the landlord of our Cherry Hill Office. Other operating expenses decreased \$54 thousand to \$199 thousand at June 30, 2010 compared to \$253 thousand for the same period in 2009. The decrease is primarily due to the FDIC Special Assessment of \$75 thousand charged in the second quarter 2009 that did not recur, offset by higher insurance premiums of \$9 thousand for the comparable period in 2010. This lower level of other operating expenses was offset, in part, by expenditures for sponsoring the business forum, higher dues, memberships and subscriptions costs of \$3 thousand and \$2 thousand, respectively.

**Income Taxes.** The Bank has incurred cumulative net losses since inception, which has caused there to be no provision for income taxes, deferred taxes and income taxes payable other than de minimus payments to New Jersey for Corporate Business Taxes. Any provision for income taxes is offset by partial release of the deferred tax valuation reserve.

## Comparison of Results of Operations for the Six Months Ended June 30, 2010 and 2009

### (UNAUDITED)

The following discussion and analysis is intended to provide information about the results of operations for the six month period ended June 30, 2010 (unaudited) compared to the results of operations for the six month period ended June 30, 2009 (unaudited). This discussion should be read in conjunction with the accompanying financial statements (unaudited) and related notes as well as statistical information included in this Form 10-Q.

### Results of Operations

**Net Income.** The Bank recorded net income of \$100 thousand, or \$0.04 per basic and diluted common share for the six months ended June 30, 2010, an increase of \$299 thousand as compared to a loss of \$199 thousand or \$(0.07) per basic and diluted common share for the six months ended June 30, 2009. Increased net income year to date is attributed to increased net interest income, supplemented by a gain on the sale of investment securities available for sale offset by an increase in the loan loss provision and higher operating expenses, specifically compensation and benefits, equipment, marketing and professional fees offset by lower occupancy and other operating expenses.

**Net interest income,** before the provision for loan losses, increased \$433 thousand to \$2.8 million for the six months ended June 30, 2010, compared to net interest income of \$2.3 million for the comparable prior year period. Although, interest income decreased \$127 thousand to \$4.1 million for the six months ended June 30, 2010, compared to \$4.2 million for the comparable prior year period, this was more than offset by the \$560 thousand decrease in interest expense for the year.

Interest income on loans decreased \$47 thousand over these periods. The decrease in interest income on loans is primarily due to the increase in loans placed on non-accrual, as these loans would have added \$128 thousand for the six months ending June 30, 2010. The Bank had one loan past due greater than 90 days and still accruing for the six months ended June 30, 2010 compared to none for the same period 2009. The Bank is continuing to accrue interest on this loan because management has determined that it is both well secured and in the process of collection. In addition, interest income generated from the Bank's securities available for sale portfolio declined by \$101 thousand from \$375 thousand for the six months ended June 30, 2009 to \$264 thousand at the comparable period in 2010. The average yield earned from the securities portfolio declined from 4.44 percent to 3.58 percent while the average balance of securities year to date was \$14.8 million, a decrease of \$2.1 million from the same period 2009. These unfavorable variances were offset in part by favorable variances as interest income earned on deposits with banks and federal funds sold increased by \$21 thousand. The increase in the interest income earned on federal funds sold and other interest earning assets was primarily due to an increase of average balances of \$6.7 million coupled with an increase in the weighted average yield of 0.31 percent.

**Interest expense** decreased to \$1.4 million for the six months ended June 30, 2010, compared to \$1.9 million for the comparable period in 2009, primarily due to a \$558 thousand decrease in interest expense on deposits resulting from a decrease in the average cost of deposits from 2.77 percent to 1.80 percent. The decreased interest expense was offset, in part, by higher average deposit balances that grew an average of \$7.6 million to \$137.6 million from the prior comparable period. The reduced average interest rates paid on each of the Bank's deposit classifications year to date in 2010 compared to the same period of 2009 reflects a general trend of declining market rates for deposits and management's efforts to improve the net interest margin in a challenging interest rate environment.

## Results of Operations – (continued)

Interest expense on time deposit accounts decreased \$527 thousand over the same period last year as average rates paid declined to 2.27 percent from 3.49 percent as average balances grew \$322 thousand. In addition, interest paid on interest bearing checking and savings accounts decreased \$28 thousand and \$21 thousand, respectively when compared to year to date 2009. The average rate paid on interest bearing checking decreased from 1.43 percent year to date 2009 to 1.01 percent for the comparable period in 2010 on increased average balances of \$2.0 million.

The average rate paid on savings accounts fell from 0.86 percent to 0.61 percent on lower average balances of \$1.5 million. These favorable variances were offset in part by increased interest expense of \$18 thousand on money market accounts as average balances grew by \$6.8 million while the average rate declined by 0.41 percent to 1.16 percent. Interest expense on long term borrowings was essentially at the same level as for the comparable period in 2009.

**Noninterest Income.** Noninterest income increased \$78 thousand to \$214 thousand year to date 2010 from \$136 thousand for the same period in 2009. This increase can be primarily attributed to a gain on the sale of securities from the available for sale portfolio of \$72 thousand. In addition, service charges on deposit accounts increased \$16 thousand from \$66 thousand year to date 2009 to \$82 for the comparable period in 2010. Increased service charges are primarily the result of the higher deposit fee structure introduced by the Bank effective September 1, 2009. These favorable variances are offset in part by a decline in other income of \$10 thousand from \$70 thousand for the six months ended June 30, 2009 to \$60 thousand for the comparable period in 2010, as a result of lower loan volume.

**Provision for Loan Losses.** The provision for loan losses increased \$18 thousand to \$220 thousand for the six months ended June 30, 2010, compared to \$202 thousand for the same period in 2009. The allowance for loan losses of \$1.6 million at June 30, 2010 approximates 1.19% of total gross loans at June 30, 2010. Although management believes that it uses the best information available to determine the allowance, unforeseen market conditions could result in adjustments and net earnings being significantly affected if circumstances differ substantially from the assumptions used in making the final determinations. Future additions to the Bank's allowance may result from periodic loan, property and collateral reviews and, thus, cannot be predicted in advance.

**Noninterest Expenses.** Total noninterest expense increased \$193 thousand to \$2.6 million for the six months ended June 30, 2010, compared to \$2.4 million for the same period in 2009. The increase is primarily attributable to increased compensation expense, up \$147 thousand for the first six months of 2010 compared to first six months of 2009. In addition, professional fees, equipment and data processing and marketing expenditures increased \$48 thousand, \$26 thousand and \$14 thousand, respectively from the comparable prior year period. These increased costs were offset in part by lower other operating expenses and reduced occupancy expenses of \$26 thousand and \$17 thousand, respectively. Compensation and benefits increased \$147 thousand to \$1.3 million for the six months ended June 30, 2010 compared to \$1.2 million for the same period in 2009. Increased compensation and benefits can be attributed to the hiring of a chief deposit officer, a business development support staff member and higher costs for related taxes and medical insurance coverage. Professional fees increased by \$48 thousand from \$190 thousand for the six months ended June 30, 2009 to \$238 thousand for the comparable period in 2010. Audit fee accruals pertaining to compliance with provisions of Sarbanes-Oxley are at higher levels than for the comparable period in 2009, as are legal fees. Equipment and data processing expense totaled \$235 thousand for the six months ended June 30, 2010 compared to \$209 thousand for the comparable period in 2009, an increase of \$26 thousand.

## **Noninterest Expenses – (continued)**

Higher maintenance and license fees related to the enhancement of our remote capture product, increased fees paid to our core service provider based on the Bank's growth, and higher depreciation costs incurred for computer hardware and software for our Mount Laurel office that was opened for two more months in the first half of 2010 compared to the first half of 2009, all contributed to this increased expense. Marketing expenditures increased \$14 thousand to \$63 thousand for the six months ended June 30, 2010 from \$49 thousand for the comparable period in 2009. This increase in costs can be attributed to business development initiatives introduced by the chief deposit officer to grow core deposits and spur name recognition in communities serviced by the Bank. Occupancy expenses decreased by \$17 thousand from \$407 thousand at June 30, 2009 to \$390 thousand for the six month ended June 30, 2010 as the Bank negotiated a \$3 thousand reduction in its monthly lease payments with the landlord of our Cherry Hill Office offset in part by higher real estate taxes assessed for the Bank's corporate headquarters located in Evesham Township. Other operating expenses decreased \$26 thousand to \$382 thousand for the six months ended June 30, 2010 compared to \$408 thousand for the same period in 2009. The decrease is primarily due to the FDIC Special Assessment of \$75 thousand charged in the second quarter 2009 that did not recur, offset by higher insurance premiums of \$23 thousand for the comparable period in 2010. This lower level of other operating expenses was offset, in part by higher ATM processing costs related to volume increases, higher loan expenses related to maintaining current loan appraisal, director and miscellaneous expenses related to business development of \$6 thousand and \$4 thousand each, respectively.

**Income Taxes.** The Bank recorded no income tax expense for the first six months of 2010 or the first six months of 2009 and anticipates that any tax liabilities in 2010 will be offset by available net operating loss carry forwards. Any provision for income taxes is offset by partial release of the deferred tax valuation reserve.

## **Financial Condition**

Total assets increased \$1.3 million year to date to \$171.1 million from \$169.8 million at December 31, 2009. Bank management has made a concerted effort to control balance sheet growth by bringing CD rates offered our customers to median level compared to peers in our market. The objective of this initiative is to reduce excess liquidity, lower dependence on certificates of deposits while working toward the improvement in the Bank's deposit mix thereby enhancing the net interest margin.

Total securities of \$11.3 million at June 30, 2010 were \$4.5 million below 2009 year end levels reflecting the sale of two securities totaling \$1.5 million from the investment securities available for sale portfolio, \$5.6 million in securities called and \$1.4 million in principal reductions among the Bank's holdings of mortgage backed securities. These decreases were partially offset by the purchase of U.S. government agency bonds totaling \$4.0 million. The available-for-sale investment portfolio includes a net unrealized gain of \$341 thousand at June 30, 2010. The market value of the available-for-sale portfolio decreased \$30 thousand from a net unrealized gain of \$371 thousand at year end 2009.

Total gross loans of \$138.0 million at June 30, 2010 increased approximately \$5.0 million from \$133.0 million at December 31, 2009. Growth was funded by a reduction in Federal Funds Sold. The commercial mortgage and commercial loans grew by \$4.5 million and \$2.2 million, respectively, from year end 2009 levels offset in part by a decline in consumer loans of \$1.7 million. Loans comprised 82.2 percent of average interest-earning assets at June 30, 2010, compared to 84.9 percent at June 30, 2009.

## **Financial Condition – (continued)**

Interest bearing deposits with other banks declined \$6.8 million from \$7.9 million at December 31, 2009 to \$1.1 million at the end of the second quarter 2010. Federal funds sold as of June 30, 2010 were \$13.0 million compared to \$5.0 million at year end 2009 an increase of \$8.0 million. Management continues to strive to improve its net interest margin based on strategic decisions, described above.

Deposits increased \$1.1 million as of June 30, 2010 from December 31, 2009. The Bank has improved its deposit mix from year end levels as interest bearing balances decreased \$3.1 million from \$140.5 million at December 31, 2009 to \$137.4 million at June 31, 2010 while noninterest bearing balances increased by \$4.2 million from \$8.1 million to \$12.3 million for the same time periods. Borrowings at June 30, 2010 and December 31, 2009 were \$7.5 million.

### Average Balances, Interest Income and Expense, Average Yields and Rates:

The following table illustrates the average balances of total interest-earning assets and total interest-bearing liabilities for the periods indicated, showing the average balances of assets, liabilities, shareholders' equity and the related interest income, interest expense and corresponding weighted average yields and costs.

	Six months ended June 30,					
	(Dollars in thousands)					
	2010			2009		
	Average Balance	Interest	Average Yield /Rate	Average Balance	Interest	Average Yield /Rate
<b>Earning assets:</b>						
Loans, net of deferred fees (3)	\$ 126,856	\$ 3,830	6.09%	\$ 128,284	\$ 3,877	6.09%
Securities	14,751	264	3.58%	16,896	361	4.27%
Federal Funds Sold	8,152	10	0.24%	5,766	9	0.31%
Other interest-earning assets	4,546	31	1.38%	194	15	15.59%
Total interest-earning assets	<u>154,305</u>	<u>4,135</u>	5.40%	<u>151,140</u>	<u>4,262</u>	5.69%
<b>Noninterest earning assets:</b>						
Cash and due from banks	1,648			1,345		
Allowance for loan losses	(1,508)			(1,259)		
Non accrual loans	6,504			1,686		
Other assets	6,810			6,074		
Total noninterest earning assets	<u>13,454</u>			<u>7,846</u>		
Total assets	<u>\$ 167,759</u>			<u>\$ 158,986</u>		
<b>Interest-bearing liabilities:</b>						
<b>Interest-bearing deposits:</b>						
Interest-bearing demand	\$ 20,103	101	1.01%	\$ 18,147	129	1.43%
Money Market	17,221	99	1.16%	10,429	81	1.57%
Savings	12,140	37	0.61%	13,658	58	0.86%
Time	88,139	993	2.27%	87,817	1,520	3.49%
Total interest-bearing deposits	<u>137,603</u>	<u>1,230</u>	1.80%	<u>130,051</u>	<u>1,788</u>	2.77%
<b>Borrowings:</b>						
Short Term borrowing	-	-	-	734	2	0.54%
FHLB Advances	7,500	149	3.95%	7,500	149	3.95%
Total borrowings	<u>7,500</u>	<u>149</u>	3.95%	<u>8,234</u>	<u>151</u>	3.65%
Total interest bearing liabilities	<u>145,103</u>	<u>1,379</u>	1.92%	<u>138,285</u>	<u>1,939</u>	2.83%
<b>Noninterest bearing liabilities:</b>						
Demand deposits	8,837			6,535		
Other liabilities	403			419		
Total noninterest-bearing liabilities	<u>9,240</u>			<u>6,954</u>		
Total liabilities	<u>154,343</u>			<u>145,239</u>		
Shareholders' equity	<u>13,416</u>			<u>13,747</u>		
Total liabilities and shareholders equity	<u>\$ 167,759</u>			<u>\$ 158,986</u>		
Net interest spread (1)			3.49%			2.86%
Net interest income and margin (2)		<u>\$ 2,756</u>	3.60%		<u>\$ 2,323</u>	3.10%
Average interest-earning assets as a percentage of interest-bearing liabilities		106.34%			109.30%	

(1) Net interest spread is the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.

(2) Net interest margin is net interest income divided by the average total interest-earning assets.

(3) The loan averages are stated net of non accrual loans, unearned income and discontinued interest (in those periods when the Bank has loans for which the accrual of interest has been discontinued).

The table below recaps loans accruing past due 90 days or more, non-accrual loans, OREO (other Real Estate Owned), and troubled debt restructuring as of the dates listed.

	June 30, 2010	December 31, 2009
Loans accruing, past due 90 days or more		
Real Estate - Construction	\$ 1,994,000	\$ -
Non-accrual Loans:		
Commercial, Financial and Agricultural		
Real Estate - Construction	2,570,661	2,570,661
Real Estate - Commercial	3,429,094	3,312,868
Commercial Loans	308,542	21,604
Home Equity	195,296	192,578
Total Non-accrual loans	<u>6,503,593</u>	<u>6,097,711</u>
Total Non-performing loans	<u>8,497,593</u>	<u>6,097,711</u>
Other Real Estate Owned	-	-
Total Non-performing assets	<u>\$ 8,497,593</u>	<u>\$ 6,097,711</u>
Non-performing loans/Total loans	6.15%	4.58%
Non-performing assets/Total assets	4.97%	3.59%
Allowance for loan losses/Total non-performing loans	19.27%	23.29%

## Liquidity

Liquidity is the ability to meet the current and future financial obligations that arise out of the ordinary course of business, such as deposit withdrawals on demand or at contractual maturity, and current and planned expenditures. Liquidity is derived primarily from cash on hand, the sale of assets, deposits and other borrowings and the repayment of and income from earning-assets. The primary sources of liquidity for the six months ended June 30, 2010 were sales and calls from the available for sale securities portfolio of \$7.1 million.

At June 30, 2010 and December 31, 2009, the Bank had cash and cash equivalents of \$15.6 million and \$14.5 million, respectively. The Statement of Cash Flows presents the change in cash and cash equivalents from operating, investing and financing activities.

As of June 30, 2010, the Bank's investment securities portfolio included approximately \$8.3 million of mortgage-backed securities that provide cash flow each month. The Bank's investment portfolio is classified as available for sale, is readily marketable, and is available to meet liquidity needs.

As of June 30, 2010, the Bank had approved unused overnight lines of credit with the Federal Home Loan Bank of New York and The Independent Bankers Bank of \$8.3 million and \$1.0 million, respectively. The Bank held \$2.9 million in unpledged securities to support use of these lines. The Bank's Asset Liability Management continues to closely monitor deposit rates offered by peers for comparable products within its geographic market considering its liquidity position, market share and interest rate environment.

## **Capital**

Total shareholders' equity increased approximately \$184 thousand to \$13.4 million at June 30, 2010 from \$13.2 million at December 31, 2009. The increase is primarily attributable to the purchase of 37,137 shares of common stock by a bank director that approximates \$100 thousand plus year-to-date income earned of \$100 thousand and recognition of \$14 thousand stock option expense less the decrease of \$30 thousand in the market values of securities available for sale.

A strong capital position is fundamental to support the continued growth of the Bank. The Bank is subject to various regulatory capital requirements. Regulatory capital is defined in terms of Tier I capital (shareholders' equity less unrealized gains or losses on available-for-sale securities), Tier II capital (which includes a portion of the allowance for loan losses) and total capital (Tier I plus Tier II). Risk-based capital ratios are expressed as a percentage of risk-weighted assets. Risk-weighted assets are determined by assigning various weights to all assets and off-balance sheet associated risk. Regulators have also adopted minimum Tier I leverage ratio standards, which measure the ratio of Tier I capital to quarterly average assets.

The Bank's regulatory capital ratios at June 30, 2010 and December 31, 2009 are provided in "Note 3 Regulatory Matters" in Notes to the Financial Statements. At June 30, 2010, management believes that the Bank is "well-capitalized" and in compliance with all applicable regulatory requirements.

The Bank intends to seek additional capital in 2010 to support future growth. We currently anticipate that it will be in the form of a common stock offering.

## **Changes in Laws and Regulations**

On July 21, 2010, the President signed the Dodd-Frank Wall Street Reform and Consumer Protection Act, a financial regulatory reform bill into legislation. The act includes the creation of a Consumer Financial Protection Bureau within the Federal Reserve Board and increases premiums paid to the FDIC by financial institutions with \$10 billion or more in assets. The act also requires the creation of a nine-member Financial Stability Oversight Council to monitor and make recommendations to the Federal Reserve to increase the capital, leverage, liquidity, and risk management requirements for financial institutions, as companies have grown in size and complexity. The act does amend Section 404 of the Sarbanes Oxley Act of 2002 (SOX) to exempt smaller reporting companies, such as the Bank, from compliance with the internal control over financial reporting auditor attestation requirements of SOX. This act may subject the Bank to increased regulation, which may impose additional cost and operational burdens on the Bank. However, we cannot say with any certainty whether or how the regulations which may be promulgated under the authority of this legislation will affect our business.

## **Off-Balance Sheet Arrangements**

The Bank's financial statements do not reflect off-balance sheet arrangements that are made in the normal course of business. These off-balance sheet arrangements consist of unfunded loans and letters of credit made under the same standards as on-balance sheet instruments. These unused commitments at June 30, 2010 totaled \$12.3 million. The commitments at June 30, 2010 consisted of \$2.2 million in construction lines of credit; \$5.7 million in residential lines of credit; \$4.0 million in commercial lines of credit; \$230 thousand in commercial real estate loans; and the remainder in other unused commitments. These instruments have fixed maturity dates, and because many of them will expire without being drawn upon, they do not generally present any significant liquidity risk to the Bank.

## Off-Balance Sheet Arrangements – (continued)

The Bank is confident that if it experiences an unforeseen and unusual demand to draw on previously unused loan commitments or lines of credit, it can fund the demands through increased deposits generated through certificates of deposit. The Bank has not had demands of this nature to date. Management believes that any amounts drawn on these commitments can be funded in the normal course of operations.

The following table reflects our commitments to extend credit by type of loan and maturity date.

Commitments to extend credit:	At June 30, 2010				
	Total Amounts Committed	Less Than 1 Year	1-3 Years	4-5 Years	After 5 Years
	(Dollars in thousands)				
Commercial Real Estate	\$ 230	\$ 230	\$ -	\$ -	\$ -
Commercial	3,963	3,946	17	-	-
Construction	2,253	2,253	-	-	-
Residential first and second mortgages	5,720	944	-	-	4,776
Other commitments	102	3	-	-	99
Total Commitments	\$ 12,268	\$ 7,376	\$ 17	\$ -	\$ 4,875

## ITEM 4T. CONTROLS AND PROCEDURES

### (a) Evaluation of Disclosure Controls and Procedures.

The management of the Bank, including the Chief Executive Officer and Vice President/Finance, have conducted an evaluation of the effectiveness of the Bank's disclosure controls and procedures pursuant to Rule 13a-15(e) under the Securities Exchange Act of 1934 as of the end of the period covered by this report (the "Evaluation Date"). Based on that evaluation, the Chief Executive Officer and Vice President/Finance concluded that, as of the Evaluation Date, the Bank's disclosure controls and procedures were effective in ensuring that all material information relating to the Bank required to be set forth in this report has been made known to them in a timely manner.

### (b) Changes in Internal Control Over Financial Reporting.

There have not been any changes in the Bank's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the last fiscal quarter of the year to which this report relates that have materially affected, or are reasonably likely to materially affect, the Bank's internal control over financial reporting.

## **Part II. OTHER INFORMATION –**

### **Item 5. OTHER INFORMATION**

The Bank is subject to the informational requirements of the Securities and Exchange Act of 1934, as amended, and in accordance therewith files reports and other information with the FDIC. Reports, registration statements, proxy statements and other information filed by the Bank with the FDIC can be inspected and copied at the public reference facilities maintained by the FDIC at 550, 17th Street, N.W., Washington, D.C.

### **ITEM 6. EXHIBITS –**

3.1 Certificate of Incorporation of Liberty Bell Bank (Incorporated by reference to Exhibit 3.1 to the Bank's Registration Statement on Form 10-SB filed with the Federal Deposit Insurance Corporation on April 28, 2004).

3.2 Amended and Restated Bylaws of Liberty Bell Bank (Incorporated by reference to Exhibit 3.1 to the Bank's Current Report on Form 8-K filed with the FDIC on December 22, 2008).

3.3 Specimen share certificate of the common stock of Liberty Bell Bank (Incorporated by reference to Exhibit 4.1 to the Bank's Form 10-SB filed with the Federal Deposit Insurance Corporation on April 28, 2004).

31.1 Certification of Chief Executive Officer and Acting Chief Financial Officer pursuant to Rule 13a.-14(a)/15d-14(a), as adopted pursuant to section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of the Chief Executive Officer and Acting Chief Financial Officer pursuant to 18 U.S.C. section 906 of the Sarbanes-Oxley Act of 2002.

## 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.

LIBERTY BELL BANK

Date: August 12, 2010

/s/ Kevin L. Kutcher  
Kevin L. Kutcher  
President, Chief Executive Officer and  
Acting Chief Financial Officer

## Certification

## Exhibit 31.1

I, Kevin L. Kutcher, President, Chief Executive Officer and Acting Chief Financial Officer of Liberty Bell Bank, certify that:

1. I have reviewed this Form 10-Q of Liberty Bell Bank to which this certification is an exhibit (the "Bank");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Bank as of, and for, the periods presented in this report;
4. I am responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Bank and I have:
  - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under my supervision, to ensure that material information relating to the Bank is made known to me by others within the Bank, particularly during the period in which this report is being prepared;
  - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under supervision to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) evaluated the effectiveness of the Bank's disclosure controls and procedures and presented in this report my conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) disclosed in this report any change in the Bank's internal control over financial reporting, that occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Bank's internal control over financial reporting.
5. I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Bank's auditors and the audit committee of the Bank's board of directors (or persons performing the equivalent functions):
  - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Bank's ability to record, process, summarize and report financial information; and
  - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Bank's internal control over financial reporting.

Date: August 12, 2010

/s/ Kevin L. Kutcher  
Kevin L Kutcher  
President, Chief Executive Officer and  
Acting Chief Financial Officer

**32.1 Section 1350 Certification of Chief Executive Officer and Chief Financial Officer**

**Statement of Chief Executive Officer and Chief Financial Officer Pursuant to Section 1350 of Title 18 of the United States Code**

Pursuant to Section 1350 of Title 18 of the United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned, Kevin L. Kutcher, the President, Chief Executive Officer and Acting Chief Financial Officer of Liberty Bell Bank (“the Bank”), hereby certifies that, to the best of my knowledge:

- (1) The Bank’s Quarterly Report on Form 10-Q for the period ended June 30, 2010 (the “Report”) fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank.

Date: August 12, 2010

/s/ Kevin L. Kutcher  
Kevin L. Kutcher  
President, Chief Executive Officer and Acting  
Chief Financial Officer