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FIRST NATIONAL CORP /VA/

Form S-1/A

August 21, 2012

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As filed with the Securities and Exchange Commission on August 21, 2012.

Registration No. 333-182968

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Pre-Effective Amendment No. 3

to

FORM S-1

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

FIRST NATIONAL CORPORATION

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

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Virginia
(State or other jurisdiction

6022
(Primary Standard Industrial

54-1232965
(I.R.S. Employer

of incorporation)

Classification Code Number)
112 West King Street

Identification Number)

Strasburg, Virginia 22657

(540) 465-9121

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

Scott C. Harvard

President and Chief Executive Officer

First National Corporation

112 West King Street

Strasburg, Virginia 22657

(540) 465-9121

(Name, address, including zip code, and telephone number, including area code, of agent for service)

Copies of Communications to:

Wayne A. Whitham, Jr., Esq.

Charles W. Kemp, Esq.

Williams Mullen

Williams Mullen Center

200 South 10th Street

Richmond, Virginia 23219

(804) 420-6000

Approximate date of commencement of proposed sale to the public: From time to time after the effectiveness of this Registration Statement.

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If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933 check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

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

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company	<input checked="" type="checkbox"/>

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

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The information in this prospectus supplement is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus supplement is not an offer to sell these securities and is not soliciting an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED AUGUST 21, 2012

PROSPECTUS SUPPLEMENT (To Prospectus Dated)

13,900 Shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A Liquidation Preference Amount \$1,000 Per Share

695 Shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series B

Liquidation Preference Amount \$1,000 Per Share

First National Corporation

This prospectus supplement relates to the offer and sale of 13,900 shares of our Fixed Rate Cumulative Perpetual Preferred Stock, Series A, \$1.25 par value per share, liquidation preference amount \$1,000 per share (the Series A Preferred Shares), and 695 shares of our Fixed Rate Cumulative Perpetual Preferred Stock, Series B, \$1.25 par value per share, liquidation preference amount \$1,000 per share (the Series B Preferred Shares and, together with the Series A Preferred Shares, the Preferred Shares) by the United States Department of the Treasury (Treasury). We issued the Preferred Shares to Treasury on March 13, 2009 as part of Treasury's Troubled Asset Relief Program Capital Purchase Program (the CPP) in a private placement exempt from the registration requirements of the Securities Act of 1933, as amended (the Securities Act).

We will not receive any proceeds from the sale of any Preferred Shares sold by Treasury.

Dividends on the Preferred Shares are payable quarterly in arrears on each February 15, May 15, August 15 and November 15. The initial dividend rate on the Series A Preferred Shares is 5% per annum through May 14, 2014, and will increase to 9% per annum on and after May 15, 2014 if not otherwise redeemed earlier for cash by us. The dividend rate on the Series B Preferred Shares is 9% per annum. We currently must inform and consult with our regulators prior to paying any dividends on the Preferred Shares. As of the date of this prospectus supplement, we have paid in full all of our quarterly dividend obligations on the Preferred Shares. We may redeem the Preferred Shares, at any time, in whole or in part, at our option, subject to prior approval by the appropriate federal banking agency, for cash, for a redemption price equal to 100% of the liquidation preference amount per Preferred Share plus any accrued and unpaid dividends to but excluding the date of redemption, provided that we must redeem, repurchase or otherwise acquire all of the Series A Preferred Shares before any of the Series B Preferred Shares are redeemed.

The Preferred Shares will not be listed for trading on any stock exchange or available for quotation on any national quotation system.

The public offering price and the allocation of the Preferred Shares in this offering will be determined by an auction process. The Series A Preferred Shares and Series B Preferred Shares will be auctioned and priced separately. The auction procedures described herein are the same for the Series A Preferred Shares and Series B Preferred Shares (each of which is separately referred to as a Series). During the auction period, potential bidders will be able to place bids to purchase Series A Preferred Shares, Series B Preferred Shares or both at any price at or above the minimum bid price of \$817.00 per share for the Series A Preferred Shares (such bid price to be in increments of \$0.01) and \$862.00 per share for the Series B Preferred Shares (such bid price to be in increments of \$0.01). The minimum size for any bid will be one Series A Preferred Share or one Series B Preferred Share. After the auction closes, if Treasury decides to sell any of the offered Series, then the underwriters will agree to purchase shares of the applicable Series in a firm commitment underwriting and the public offering price of such shares will equal the clearing price of such Series plus accrued dividends thereon. If bids are received for 100% or more of the offered Series, the clearing price for the applicable Series will be equal to the highest price at which all of the offered shares in such Series can be sold in the auction. If bids are received for 100% or more of the offered Series, and Treasury elects to sell any of the shares in the applicable Series in the auction, Treasury must sell all of the offered shares in such Series at the clearing price. If bids are received for at least half, but less than all, of the offered Series, then the clearing price for the applicable Series will be equal to the minimum bid price of \$817.00 per share for the Series A Preferred Shares and \$862.00 per share for the Series B Preferred Shares, and Treasury may (but is not required to) sell, at the public offering price, the number of shares in such Series it chooses to sell up to the number of bids received in the auction, so long as at least half of the offered shares in such Series are sold. In certain cases, the bids of bidders may be pro-rated. If bids are received for less than half of the offered Series, Treasury will not sell any of the shares of the applicable Series in this offering. Even if bids are received for at least half of the offered Series, Treasury

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may decide not to sell any of the shares of the applicable Series, or, in the case where bids are received for at least half, but less than all, of such Series, may decide to sell a portion (but not less than half) of the offered shares of the applicable Series in the auction process. The method for submitting bids and a more detailed description of this auction process are described in "Auction Process" beginning on page S-33 of this prospectus supplement.

Investing in the Preferred Shares involves risks. You should read the "Risk Factors" section beginning on page S-11 of this prospectus supplement and page 4 of the accompanying prospectus and in our Annual Report on Form 10-K for the year ended December 31, 2011 before making a decision to invest in the Preferred Shares.

	Per Share	Total
Public offering price(1)	\$	\$
Underwriting discounts and commissions to be paid by Treasury(2)	\$	\$
Proceeds to Treasury(1)	\$	\$

(1) Plus accrued dividends from and including August 15, 2012.

(2) Treasury has agreed to pay all underwriting discounts and commissions and transfer taxes. We have agreed to pay all transaction fees, if any, applicable to the sale of the Preferred Shares and certain fees and disbursements of counsel for Treasury incurred in connection with this offering.

None of the Securities and Exchange Commission (the "SEC"), the Federal Deposit Insurance Corporation (the "FDIC"), the Board of Governors of the Federal Reserve System (the "Federal Reserve"), any state or other securities commission or any other federal or state bank regulatory agency has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus supplement or the accompanying prospectus. Any representation to the contrary is a criminal offense.

The Preferred Shares are not savings accounts, deposits or other obligations of any bank, thrift or other depository institution and are not insured or guaranteed by the FDIC or any other governmental agency or instrumentality.

The underwriters expect to deliver the Preferred Shares in book-entry form through the facilities of The Depository Trust Company and its participants against payment on or about .

Joint Book-Running Managers

BofA Merrill Lynch

The date of this prospectus supplement is

Sandler O'Neill + Partners, L.P.

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ABOUT THIS PROSPECTUS SUPPLEMENT

You should read this prospectus supplement, the accompanying prospectus and the additional information described under the headings "Where You Can Find More Information" and "Incorporation of Certain Information by Reference" before you make a decision to invest in the Preferred Shares. In particular, you should review the information under the heading "Risk Factors" set forth on page S-11 of this prospectus supplement, the information set forth under the heading "Risk Factors" set forth on page 4 in the accompanying prospectus and the information under the heading "Risk Factors" included in our Annual Report on Form 10-K for the year ended December 31, 2011, which is incorporated by reference herein. You should rely only on the information contained or incorporated by reference in this prospectus supplement, the accompanying prospectus and any related free writing prospectus required to be filed with the SEC. Neither we nor Treasury nor the underwriters are making an offer to sell the Preferred Shares in any manner in which, or in any jurisdiction where, the offer or sale thereof is not permitted. Neither we nor Treasury nor the underwriters have authorized any person to provide you with different or additional information. If any person provides you with different or additional information, you should not rely on it. You should assume that the information in this prospectus supplement, the accompanying prospectus, any such free writing prospectus and the documents incorporated by reference herein and therein is accurate only as of its date or the date which is specified in those documents. Our business, financial condition, capital levels, cash flows, liquidity, results of operations and prospects may have changed since any such date.

In this prospectus supplement, we frequently use the terms "we," "our" and "us" to refer to First National Corporation (the "Company") and its subsidiaries.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain information contained in this prospectus supplement may include "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Exchange Act. These forward-looking statements are generally identified by phrases such as "we expect," "we believe" or words of similar import. Such forward-looking statements involve known and unknown risks including, but not limited to:

the ability to raise capital as needed;

adverse economic conditions in the market area and the impact on credit quality and risks inherent in the loan portfolio such as repayment risk and fluctuating collateral values;

additional future losses if our levels of non-performing assets do not moderate and if the proceeds we receive upon liquidation of assets are less than the carrying value of such assets;

further increases of non-performing assets may reduce interest income and increase net charge-offs, provision for loan losses, and operating expenses;

the adequacy of the allowance for loan losses related to specific reserves on impaired loans, and changes in factors considered such as general economic and business conditions in the market area and overall asset quality;

the adequacy of the valuation allowance for other real estate owned related to changes in economic conditions and local real estate activity;

loss or retirement of key executives;

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the ability to compete effectively in the highly competitive banking industry;

legislative or regulatory changes, including changes in accounting standards, may adversely affect the businesses that the Company is engaged in;

the ability to implement various technologies into our operations may impact the Company's ability to operate profitably;

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the ability of the Company to implement its disaster recovery plan in the event of a natural disaster;

risks related to the timing of the recoverability of the deferred tax asset, which is subject to considerable judgment, and the risk that even after the recovery of the deferred tax asset balance under GAAP, there will remain limitations on the ability to include our deferred tax assets for regulatory capital purposes;

increases in FDIC insurance premiums could adversely affect the Company's profitability;

the ability to retain customers and secondary funding sources if the Bank's reputation would become damaged;

the reliance on secondary sources, such as Federal Home Loan Bank advances, sales of securities and loans, federal funds lines of credit from correspondent banks and out-of-market time deposits, to meet liquidity needs;

changes in interest rates could have a negative impact on the Company's net interest income and an unfavorable impact on the Bank's customers' ability to repay loans; and

other factors identified in Risk Factors, above.

Although we believe that our expectations with respect to the forward-looking statements are based upon reliable assumptions within the bounds of our knowledge of our business and operations, there can be no assurance that our actual results, performance or achievements will not differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements.

WHERE YOU CAN FIND MORE INFORMATION

We are subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the Exchange Act), and file with the SEC proxy statements, Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, as required of a U.S. listed company. You may read and copy any document we file at the SEC's public reference room at 100 F Street, NE, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. Our SEC filings are also available to the public from the SEC's web site at www.sec.gov or on our website at www.fbvirginia.com. However, the information on, or that can be accessible through, our website does not constitute a part of, and is not incorporated by reference in, this prospectus supplement or the accompanying prospectus. Written requests for copies of the documents we file with the SEC should be directed to M. Shane Bell, First National Corporation, 112 West King Street, Strasburg, Virginia 22657, telephone (540) 465-9121.

This prospectus supplement and the accompanying prospectus are part of a registration statement on Form S-1 filed by us with the SEC under the Securities Act. As permitted by the SEC, this prospectus supplement and the accompanying prospectus do not contain all the information in the registration statement filed with the SEC. For a more complete understanding of this offering, you should refer to the complete registration statement, including exhibits, on Form S-1 that may be obtained as described above. Statements contained in this prospectus supplement and the accompanying prospectus about the contents of any contract or other document are not necessarily complete. If we have filed any contract or other document as an exhibit to the registration statement or any other document incorporated by reference in the registration statement, you should read the exhibit for a more complete understanding of the contract or other document or matter involved. Each statement regarding a contract or other document is qualified in its entirety by reference to the actual contract or other document.

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INCORPORATION OF CERTAIN INFORMATION BY REFERENCE

The SEC allows us to incorporate by reference the information that we file with it, which means that we can disclose important information to you by referring you to other documents. The information incorporated by reference is an important part of this prospectus supplement and the accompanying prospectus. We incorporate by reference the following documents (other than information furnished rather than filed in accordance with SEC rules):

Our annual report on Form 10-K for the year ended December 31, 2011 filed with the SEC on March 28, 2012 (the Form 10-K);

The portions of our definitive proxy statement for our 2012 Annual Shareholders Meeting filed with the SEC on April 6, 2012 that have been incorporated by reference into the Form 10-K;

Our quarterly reports on Form 10-Q for the quarters ended March 31, 2012 and June 30, 2012, filed with the SEC on May 15, 2012 and August 14, 2012, respectively; and

Our current reports on Form 8-K filed with the SEC on February 14, 2012, April 13, 2012, May 9, 2012, May 14, 2012, July 3, 2012 and August 15, 2012.

We will provide without charge, upon written or oral request, a copy of any or all of the documents that are incorporated by reference into this prospectus supplement and the accompanying prospectus and a copy of any or all other contracts or documents which are referred to in this prospectus supplement or the accompanying prospectus. Requests should be directed to: M. Shane Bell, First National Corporation, 112 West King Street, Strasburg, Virginia 22657, telephone (540) 465-9121.

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SUMMARY

This summary highlights selected information contained elsewhere or incorporated by reference in this prospectus supplement and the accompanying prospectus and may not contain all the information that you need to consider in making your investment decision to purchase the Preferred Shares. You should carefully read this entire prospectus supplement and the accompanying prospectus, as well as the information incorporated by reference herein and therein, before deciding whether to invest in the Preferred Shares. You should carefully consider the sections entitled Risk Factors in this prospectus supplement, the accompanying prospectus and the documents incorporated by reference herein and therein to determine whether an investment in the Preferred Shares is appropriate for you.

The Company

Overview

We are a bank holding company headquartered in Strasburg, Virginia. Through our wholly-owned bank subsidiary, First Bank, we provide loan, deposit, investment, trust and asset management and other products and services in the northern Shenandoah Valley region of Virginia. Loan products and services include personal loans, residential mortgages, home equity loans and commercial loans. Deposit products and services include checking, savings, NOW accounts, money market accounts, IRA accounts, certificates of deposit, and cash management accounts. We also offer Internet banking, mobile banking, remote deposit capture and other traditional banking services.

Through our Trust and Asset Management Department, we offer a variety of trust and asset management services including estate planning, investment management of assets, trustee under an agreement, trustee under a will, individual retirement accounts, estate settlement and benefit plans. We offer financial planning and brokerage services for our customers through our investment division, First Financial Advisors.

Our products and services are provided through 10 branch offices, 26 ATMs and our website, www.fbvirginia.com. We operate six of our offices under the Financial Center concept. A Financial Center offers all of the Bank's financial services at one location. This concept allows loan, deposit, trust and investment advisory personnel to be readily available to serve customers throughout the Bank's market area.

Market Area

Our primary market area is located within an hour commute of the Washington, D.C. Metropolitan Area. The Bank's office locations are well-positioned in strong markets along the Interstate 81 and Interstate 66 corridors in the northern Shenandoah Valley region of Virginia, which include the City of Winchester, Frederick County, Warren County and Shenandoah County. Within the market area there are various types of industry including medical and professional services, manufacturing, retail and higher education. Customers include individuals, small and medium-sized businesses, local governmental entities and non-profit organizations.

According to Federal Deposit Insurance Corporation (FDIC) deposit data as of June 30, 2011, we were ranked first in Shenandoah County with \$228.6 million in deposits, representing 30% of the total deposit market; third in Warren County with \$60.1 million or 12% of the market; fourth in Frederick County with \$80.3 million or 15% of the market; and fifth in the City of Winchester with \$107.6 million or 8% of the market. We were ranked second overall in our market area with 15% of the total deposit market.

Recent Developments

On June 29, 2012, we completed the sale of 1,945,815 shares of common stock through a rights offering to existing shareholders and to certain standby investors. In the rights offering, our existing shareholders exercised

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subscription rights to purchase 1,520,815 shares at a subscription price of \$4.00 per share. In conjunction with the rights offering, we entered into standby purchase agreements with certain standby purchasers, pursuant to which they purchased an additional 425,000 shares at the same price of \$4.00 per share. In total, the Company raised net proceeds of \$7.6 million after expenses.

Corporate Information

Our principal executive offices are located at 112 West King Street, Strasburg, Virginia 22657 and our telephone number is (540) 465-9121. We maintain a website at www.fbvirginia.com, which contains information relating to us. Unless specifically incorporated by reference, information on our website is not a part of this prospectus.

The Offering

The following summary contains basic information about the Preferred Shares and the auction process and is not intended to be complete and does not contain all the information that is important to you. For a more complete understanding of the Preferred Shares and the auction process, you should read the sections of this prospectus supplement entitled **Description of Preferred Shares** and **Auction Process** and any similar sections in the accompanying prospectus.

Issuer

First National Corporation

Preferred Shares Offered by Treasury

13,900 shares of our Fixed Rate Cumulative Perpetual Preferred Stock, Series A, \$1.25 par value per share.

695 shares of our Fixed Rate Cumulative Perpetual Preferred Stock, Series B, \$1.25 par value per share.

The Series A Preferred Stock and Series B Preferred Stock will be auctioned and priced separately.

The number of shares of each Series to be sold will depend on the number of bids received in the auction described below and whether Treasury decides to sell any such shares in the auction process. See the section entitled **Auction Process** in this prospectus supplement.

Liquidation Preference

If we liquidate, dissolve or wind up (collectively, a **liquidation**), holders of the Preferred Shares will have the right to receive \$1,000 per share, plus any accrued and unpaid dividends (including dividends accrued on any unpaid dividends) to, but not including, the date of payment, before any payments are made to holders of our common stock or any other capital stock that ranks, by its terms, junior as to rights upon liquidation to the Preferred Shares.

Dividends

Dividends on the Preferred Shares are payable quarterly in arrears on each February 15, May 15, August 15 and November 15. The initial dividend rate on the Series A Preferred Shares is 5% per annum through May 14, 2014, and will increase to 9% per annum on and after May 15, 2014 if not otherwise redeemed earlier for cash by us. The dividend rate on the Series B Preferred Shares is 9% per annum. We currently must inform and consult with our regulators prior to

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paying any dividends on the Preferred Shares. As of the date of this prospectus supplement, we have paid in full all of our quarterly dividend obligations on the Preferred Shares. Holders of Preferred Shares sold by Treasury in the auction, if any, that are record holders on the record date for the November 15, 2012 dividend payment date will be entitled to any declared dividends payable on such date.

Maturity

The Preferred Shares have no maturity date.

Rank

The Preferred Shares rank (i) senior to common stock or any other capital stock that ranks, by its terms, junior as to dividend rights and/or rights upon liquidation to the Preferred Shares (collectively, the Junior Stock), (ii) equally with any shares of our capital stock whose terms do not expressly provide that such class or series will rank senior or junior to the Preferred Shares as to dividend rights and/or rights upon liquidation (collectively, the Parity Stock) and (iii) junior to all of our existing and future indebtedness and any future senior securities, in each case as to dividend rights and/or rights upon liquidation.

Priority of Dividends

So long as any of the Preferred Shares remain outstanding, we may not declare or pay a dividend or other distribution on our common stock or any other shares of Junior Stock (other than dividends payable solely in common stock) or Parity Stock (other than dividends paid on a pro rata basis with the Preferred Shares), and we generally may not directly or indirectly purchase, redeem or otherwise acquire any shares of common stock, Junior Stock or Parity Stock unless all accrued and unpaid dividends on the Preferred Shares for all past dividend periods are paid in full.

Redemption

We may redeem the Preferred Shares, at any time, in whole or in part, at our option, subject to prior approval by the appropriate federal banking agency, for a redemption price equal to 100% of the liquidation preference amount per Preferred Share plus any accrued and unpaid dividends (including dividends accrued on any unpaid dividends) to but excluding the date of redemption, provided that we must redeem, repurchase or otherwise acquire all of the Series A Preferred Shares before any of the Series B Preferred Shares are redeemed. We intend to redeem or repurchase Preferred Shares in such amounts and at such times as we deem prudent, although we have no present plans to redeem, in whole or in part, the Series A Preferred Shares before May 15, 2014, when the dividend rate is scheduled to increase on such shares. Our ability to redeem the Preferred Shares will depend on then-present facts and circumstances and the amount of capital we hold or can raise at the holding company level. In order for our regulators to approve the redemption of the Preferred Shares, we would expect our regulators to consider our financial condition and regulatory capital levels, after giving effect to the redemption of the Preferred Shares so approved.

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Voting Rights

Holders of the Preferred Shares generally have no voting rights. However, if we do not pay dividends on the Preferred Shares for six or more quarterly periods, whether or not consecutive, the holders of the Preferred Shares, voting as a single class with the holders of any other Parity Stock upon which like voting rights have been conferred and are exercisable, will be entitled to vote for the election of two additional directors to serve on our board of directors until all accrued and unpaid dividends (including dividends accrued on any unpaid dividends) on the Preferred Shares for all past dividend periods are paid in full. There is no limit on the number of nominations and a plurality of eligible voters would determine the election of the two new directors.

In addition, the affirmative vote of the holders of at least 66-2/3% of the outstanding Preferred Shares is required for us to authorize, create or increase the authorized number of shares of our capital stock ranking, as to dividends or amounts payable upon liquidation, senior to the Preferred Shares, to amend, alter or repeal any provision of our charter or the Certificate of Designations for the Preferred Shares in a manner that adversely affects the rights of the holders of the Preferred Shares or to consummate a binding share exchange or reclassification of the Preferred Shares or a merger or consolidation of us with another entity unless (x) the Preferred Shares remain outstanding or are converted into or exchanged for preference shares of the surviving entity or its ultimate parent and (y) the Preferred Shares remain outstanding or such preference shares have such terms that are not materially less favorable, taken as a whole, than the rights of the Preferred Shares immediately prior to such transaction, taken as a whole.

Auction Process

The Series A Preferred Shares and Series B Preferred Shares will be auctioned and priced separately. The auction procedures described herein are the same for each Series. Prospective purchasers may bid for Series A Preferred Shares, Series B Preferred Shares or both. The public offering price and the allocation of the Preferred Shares in this offering will be determined through an auction process conducted by Merrill Lynch, Pierce, Fenner & Smith Incorporated and Sandler O'Neill & Partners, L.P., the joint book-running managers in this offering, in their capacity as the auction agents. The auction process will entail a modified Dutch auction mechanic in which bids may be submitted through the auction agents or one of the other brokers that is a member of the broker network, which are collectively referred to in this prospectus supplement as the network brokers, established in connection with the auction process. Each broker will make suitability determinations with respect to its own customers wishing to participate in the auction process. The auction agents will not provide bidders with any information about the bids of other bidders or auction trends, or with advice regarding bidding strategies, in connection with the auction process. We encourage you to discuss any questions regarding the bidding process and suitability determinations applicable to your bids with your broker. We do not intend to submit any bids in the auction.

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For more information about the auction process, see [Auction Process](#) in this prospectus supplement.

Minimum Bid Size and Price Increments

This offering is being conducted using an auction process in which prospective purchasers are required to bid for the Preferred Shares. Prospective purchasers may bid for Series A Preferred Shares, Series B Preferred Shares or both. During the auction period, bids may be placed for Preferred Shares at any price at or above the minimum bid price of \$817.00 per share for the Series A Preferred Shares (such bid price to be in increments of \$0.01) and \$862.00 per share for the Series B Preferred Shares (such bid price to be in increments of \$0.01) with a minimum bid size of one Preferred Share. See [Auction Process](#) in this prospectus supplement.

Bid Submission Deadline

The auction will commence at 10:00 a.m., New York City time, on the date specified in a press release issued on such day, and will close at 6:30 p.m., New York City time, on the second business day immediately thereafter, which is referred to as the submission deadline. Network brokers and other brokers will impose earlier submission deadlines than those imposed by the auction agents. Please see page S-36 of this prospectus supplement for more information regarding the bid submission deadline.

Irrevocability of Bids

Bids that have not been modified or withdrawn by the time of the submission deadline are final and irrevocable, and bidders who submit bids that are accepted by Treasury will be obligated to purchase the Preferred Shares allocated to them. The auction agents are under no obligation to reconfirm bids for any reason, except as may be required by applicable securities laws; however, the auction agents, in their sole discretion, may require that bidders confirm their bids before the auction process closes. See [Auction Process](#) in this prospectus supplement.

Clearing Price

The price at which the Series A Preferred Shares will be sold to the public will be the clearing price for such Series (the [Series A Clearing Price](#)) plus accrued dividends thereon. The [Series A Clearing Price](#) will be determined as follows:

If valid, irrevocable bids are received for 100% or more of the offered Series A Preferred Shares at the submission deadline, the [Series A Clearing Price](#) will be equal to the highest price at which all of the offered Series A Preferred Shares can be sold in the auction;

If valid, irrevocable bids are received for at least half, but less than all, of the offered Series A Preferred Shares at the time of the submission deadline, the [Series A Clearing Price](#) will be equal to the minimum bid price of \$817.00 per share for the Series A Preferred Shares.

Even if bids are received for at least half of the offered Series A Preferred Shares, Treasury may decide not to sell any Series A

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Preferred Shares in the auction process or, in the case where bids are received for at least half, but less than all, of the Series A Preferred Shares, may decide only to sell a portion (but not less than half) of the offered Series A Preferred Shares in the auction process. If Treasury decides to sell Series A Preferred Shares in the auction, after Treasury confirms its acceptance of the Series A Clearing Price and the number of Series A Preferred Shares to be sold, the auction agents and each network broker that has submitted a successful bid will notify successful bidders that the auction has closed and that their bids have been accepted by Treasury (subject, in some cases, to pro-ration, as described below). The Series A Clearing Price and number of Series A Preferred Shares to be sold are also expected to be announced by press release on the business day following the end of the auction. See *Auction Process* in this prospectus supplement.

The price at which the Series B Preferred Shares will be sold to the public will be the clearing price for such Series (the *Series B Clearing Price*) plus accrued dividends thereon. The Series B Clearing Price will be determined as follows:

If valid, irrevocable bids are received for 100% or more of the offered Series B Preferred Shares at the submission deadline, the Series B Clearing Price will be equal to the highest price at which all of the offered Series B Preferred Shares can be sold in the auction;

If valid, irrevocable bids are received for at least half, but less than all, of the offered Series B Preferred Shares at the time of the submission deadline, the Series B Clearing Price will be equal to the minimum bid price of \$862.00 per share for the Series B Preferred Shares.

Even if bids are received for at least half of the offered Series B Preferred Shares, Treasury may decide not to sell any Series B Preferred Shares in the auction process or, in the case where bids are received for at least half, but less than all, of the Series B Preferred Shares, may decide only to sell a portion (but not less than half) of the offered Series B Preferred Shares in the auction process. If Treasury decides to sell Series B Preferred Shares in the auction, after Treasury confirms its acceptance of the Series B Clearing Price and the number of Series B Preferred Shares to be sold, the auction agents and each network broker that has submitted a successful bid will notify successful bidders that the auction has closed and that their bids have been accepted by Treasury (subject, in some cases, to pro-ration, as described below). The Series B Clearing Price and number of Series B Preferred Shares to be sold are also expected to be announced by press release on the business day following the end of the auction. See *Auction Process* in this prospectus supplement.

Number of Preferred Shares to be Sold

If bids are received for 100% or more of the offered Series A Preferred Shares, Treasury must sell all of the offered Series A

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Preferred Shares if it chooses to sell any Series A Preferred Shares. If bids are received for at least half, but less than all, of the offered Series A Preferred Shares, then Treasury may, but is not required to, sell at the minimum bid price for such Series in the auction (which will be deemed to be the Series A Clearing Price) the number of Series A Preferred Shares it chooses to sell up to the number of bids received in the auction, so long as at least half of the offered Series A Preferred Shares are sold. If bids are received for less than half of the offered Series A Preferred Shares, Treasury will not sell any Series A Preferred Shares in this offering. Even if bids are received for at least half of the offered Series A Preferred Shares, Treasury may decide not to sell any Series A Preferred Shares or, in the case where bids are received for at least half, but less than all, of the offered Series A Preferred Shares, may decide only to sell a portion (but not less than half) of the offered Series A Preferred Shares in the auction process. If Treasury elects to sell any Series A Preferred Shares in the auction, Treasury must sell those shares at the Series A Clearing Price plus accrued dividends thereon. In no event will Treasury sell more Series A Preferred Shares than the number of Series A Preferred Shares for which there are bids. See Auction Process in this prospectus supplement.

If bids are received for 100% or more of the offered Series B Preferred Shares, Treasury must sell all of the offered Series B Preferred Shares if it chooses to sell any Series B Preferred Shares. If bids are received for at least half, but less than all, of the offered Series B Preferred Shares, then Treasury may, but is not required to, sell at the minimum bid price for such Series in the auction (which will be deemed to be the Series B Clearing Price) the number of Series B Preferred Shares it chooses to sell up to the number of bids received in the auction, so long as at least half of the offered Series B Preferred Shares are sold. If bids are received for less than half of the offered Series B Preferred Shares, Treasury will not sell any Series B Preferred Shares in this offering. Even if bids are received for at least half of the offered Series B Preferred Shares, Treasury may decide not to sell any Series B Preferred Shares or, in the case where bids are received for at least half, but less than all, of the offered Series B Preferred Shares, may decide only to sell a portion (but not less than half) of the offered Series B Preferred Shares in the auction process. If Treasury elects to sell any Series B Preferred Shares in the auction, Treasury must sell those shares at the Series B Clearing Price plus accrued dividends thereon. In no event will Treasury sell more Series B Preferred Shares than the number of Series B Preferred Shares for which there are bids. See Auction Process in this prospectus supplement.

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Allocation; Pro-Ration

If bids for 100% or more of the offered Series A Preferred Shares are received and Treasury elects to sell Series A Preferred Shares in the offering, then any accepted bids submitted in the auction above the Series A Clearing Price will receive allocations in full, while any accepted bids submitted at the Series A Clearing Price may experience pro-rata allocation. If bids for at least half, but less than all, of the offered Series A Preferred Shares are received, and Treasury chooses to sell fewer Series A Preferred Shares than the number of Series A Preferred Shares for which bids were received, then all bids will experience equal pro-rata allocation. See [Auction Process](#) in this prospectus supplement.

If bids for 100% or more of the offered Series B Preferred Shares are received and Treasury elects to sell Series B Preferred Shares in the offering, then any accepted bids submitted in the auction above the Series B Clearing Price will receive allocations in full, while any accepted bids submitted at the Series B Clearing Price may experience pro-rata allocation. If bids for at least half, but less than all, of the offered Series B Preferred Shares are received, and Treasury chooses to sell fewer Series B Preferred Shares than the number of Series B Preferred Shares for which bids were received, then all bids will experience equal pro-rata allocation. See [Auction Process](#) in this prospectus supplement.

Use of Proceeds

We will not receive any proceeds from the sale of any Preferred Shares sold by Treasury. See [Use of Proceeds](#).

Listing

The Preferred Shares will not be listed for trading on any stock exchange nor will they be available for quotation on any national quotation system.

Risk Factors

See [Risk Factors](#) and other information included or incorporated by reference in this prospectus supplement and the accompanying prospectus for a discussion of factors you should consider carefully before making a decision to invest in the Preferred Shares.

Auction Agents

Merrill Lynch, Pierce, Fenner & Smith Incorporated and Sandler O'Neill & Partners, L.P.

Network Brokers

See page S-35 for a list of brokers participating as network brokers in the auction process.

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The following tables present our selected consolidated financial data as of or for the six months ended June 30, 2012 and 2011 and as of and for each of the five years ended December 31, 2007 through 2011. The information as of or for the years ended December 31, 2007 through 2011 is derived in part from, and should be read together with, our audited consolidated financial statements and notes thereto incorporated by reference herein. The information as of or for the six months ended June 30, 2012 and 2011 is from our unaudited consolidated financial statements and notes thereto which are incorporated by reference herein. In the opinion of our management, however, all adjustments consisting of normal recurring adjustments necessary for a fair presentation of the results of operations for the unaudited periods have been made. The operating data for the six months ended June 30, 2012 are not necessarily indicative of the results that might be realized for the year ending December 31, 2012.

	Six Months Ended June 30,		Years Ended December 31,				
	2012	2011	2011	2010	2009	2008	2007
(In thousands, except per share data)							
Results of Operations							
Interest and dividend income	\$ 12,088	\$ 12,975	\$ 25,648	\$ 27,215	\$ 27,414	\$ 30,913	\$ 35,501
Interest expense	2,213	2,957	5,450	6,814	9,084	12,793	17,401
Net interest income	9,875	10,018	20,198	20,401	18,330	18,120	18,100
Provision for loan losses	2,650	3,820	12,380	11,731	2,300	1,994	398
Net interest income after provision for loan losses	7,225	6,198	7,818	8,670	16,030	16,126	17,702
Noninterest income	3,976	2,825	5,799	6,082	5,577	5,951	6,072
Noninterest expense	9,338	9,071	20,743	20,561	18,703	16,014	15,286
Income (loss) before income taxes	1,863	(48)	(7,126)	(5,809)	2,904	6,063	8,488
Income tax expense (benefit)	694	(106)	3,835	(2,206)	755	1,840	2,741
Net (loss) income	1,169	58	(10,961)	(3,603)	2,149	4,223	5,747
Effective dividend and accretion on preferred stock	451	446	894	887	704		
Net (loss) income available to common shareholders	\$ 718	\$ (388)	\$ (11,855)	\$ (4,490)	\$ 1,445	\$ 4,223	\$ 5,747
Key Performance Ratios							
Return on average assets	0.44%	0.02%	(1.96)%	(0.66)%	0.39%	0.78%	1.09%
Return on average equity	6.17%	0.24%	(22.46)%	(6.52)%	4.27%	10.65%	16.52%
Net interest margin	4.01%	3.94%	3.98%	4.07%	3.62%	3.63%	3.71%
Efficiency ratio (1)	70.26%	68.60%	69.66%	66.77%	73.10%	65.37%	62.22%
Dividend payout		1,017.24%	(5.30)%	(36.64)%	113.09%	38.61%	26.79%
Equity to assets	8.41%	8.75%	6.88%	8.90%	9.92%	7.15%	6.99%
Per Common Share Data							
Net (loss) income, basic and diluted	\$ 0.24	\$ (0.13)	\$ (4.01)	\$ (1.53)	\$ 0.49	\$ 1.45	\$ 1.98
Cash dividends		0.20	0.20	0.56	0.56	0.56	0.53
Book value at period end	6.19	11.64	7.72	11.66	13.92	13.41	12.95

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	Six Months Ended		Years Ended December 31,				
	June 30, 2012	2011	2011	2010	2009	2008	2007
Financial Condition							
Assets	\$ 531,230	\$ 555,249	\$ 539,064	\$ 544,629	\$ 552,674	\$ 548,237	\$ 541,565
Loans, net	370,136	401,724	379,503	418,994	436,129	446,327	445,380
Securities	87,267	82,780	91,665	60,420	60,129	54,791	54,117
Deposits	458,694	476,494	469,172	463,500	463,886	447,493	445,142
Shareholders' equity	44,696	48,597	37,096	48,498	54,807	39,185	37,859
Average shares outstanding, diluted	2,977	2,951	2,953	2,940	2,921	2,913	2,906
Capital Ratios							
Leverage	10.14%	10.18%	8.45%	10.54%	11.50%	9.10%	9.53%
Risk-based capital ratios							
Tier 1 capital	13.79%	13.06%	11.24%	12.91%	13.70%	10.52%	10.89%
Total capital	15.07%	14.33%	12.51%	14.18%	14.96%	11.72%	11.80%

(1) The efficiency ratio is computed by dividing noninterest expense excluding the provision for other real estate owned and gains and losses on other real estate owned by the sum of net interest income on a tax equivalent basis and non-interest income excluding securities and premises and equipment gains and losses. This is a non-GAAP financial measure that the Company believes provides investors with important information regarding operational efficiency. Such information is not prepared in accordance with U.S. generally accepted accounting principles (GAAP) and should not be construed as such. Noninterest expense excluding the provision for other real estate owned and gains and losses on other real estate owned was \$9,019 and \$8,887 for the six months ended June 30, 2012 and 2011, respectively, and \$18,275, \$17,902, \$17,709, \$16,014, and \$15,286 for 2011, 2010, 2009, 2008 and 2007, respectively. Net interest income on a tax equivalent basis was \$9,979 and \$10,170 for the six months ended June 30, 2012 and 2011, respectively, and \$20,496, \$20,723, \$18,668, \$18,442, and \$18,391 for 2011, 2010, 2009, 2008 and 2007, respectively. Non-interest income excluding securities and premises and equipment gains and losses was \$2,858 and \$2,784 for the six months ended June 30, 2012 and 2011, respectively, and \$5,740, \$6,089, \$5,558, \$6,055, and \$5,812 for 2011, 2010, 2009, 2008 and 2007, respectively. Management believes such financial information is meaningful to the reader in understanding operating performance, but cautions that such information not be viewed as a substitute for GAAP. The Company, in referring to its net income, is referring to income under generally accepted accounting principles, or GAAP. See Non-GAAP Financial Measures included in Item 7 of the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

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RISK FACTORS

An investment in our Preferred Shares is subject to risks inherent in our business, risks relating to the structure of the Preferred Shares and risks relating to the auction process being conducted as part of this offering. The material risks and uncertainties that management believes affect your investment in the Preferred Shares are described below and in the sections entitled "Risk Factors" in the accompanying prospectus and our Annual Report on Form 10-K for the year ended December 31, 2011 incorporated by reference herein. Before making an investment decision, you should carefully consider the risks and uncertainties described below and in the accompanying prospectus and information included or incorporated by reference in this prospectus supplement and the accompanying prospectus. If any of these risks or uncertainties are realized, our business, financial condition, capital levels, cash flows, liquidity, results of operations and prospects, as well as our ability to pay dividends on the Preferred Shares, could be materially and adversely affected and the market price of the Preferred Shares could decline significantly and you could lose some or all of your investment.

Risk Factors Related to our Business

We may be further adversely affected by economic conditions in our market area.

We are headquartered in the northern Shenandoah Valley region of Virginia. Because our lending is concentrated in this market, we are affected by the general economic conditions in the region. Changes in the economy may influence the growth rate of loans and deposits, the quality of the loan portfolio and loan and deposit pricing. A continued decline in general economic conditions caused by inflation, recession, unemployment or other factors beyond our control would further impact these local economic conditions and the demand for banking products and services generally, which could negatively affect our performance and financial condition.

Deteriorating credit quality, particularly in real estate loans, has adversely impacted us and may continue to adversely impact us.

During 2008, we began to experience a downturn in the overall credit performance of the loan portfolio, as well as acceleration in the deterioration of general economic conditions. This deterioration, including a significant increase in national and regional unemployment levels, is negatively impacting some borrowers' ability to repay. During the year ended December 31, 2008, these conditions resulted in a \$13.9 million increase in non-performing assets and loans over 90 days past due to \$16.2 million. At December 31, 2011, 2010 and 2009, non-performing assets and loans over 90 days past due remained at elevated levels, totaling \$18.7 million, \$15.4 million and \$14.8 million, respectively. The provision for loan losses totaled \$12.4 million, \$11.7 million and \$2.3 million for the years ended December 31, 2011, 2010 and 2009, respectively. Non-performing assets and loans over 90 days past due and still accruing interest totaled \$17.2 million at June 30, 2012 and the provision for loan losses totaled \$2.7 million for the six months ended June 30, 2012. Additional increases in loan loss reserves may be necessary in the future. Continued deterioration in the quality of the loan portfolio can have a material adverse effect on earnings, liquidity and capital.

We will realize additional future losses if our levels of non-performing assets do not moderate and if the proceeds we receive upon liquidation of assets are less than the carrying value of such assets.

We expect to continue to focus on reducing non-performing asset levels during 2012 by selling other real estate owned (OREO) and restructuring our problem loans and potential problem loans. Other potential problem loans are defined as performing loans that possess certain risks, including the borrower's ability to pay and the collateral value securing the loan, that management has identified that may result in the loans not being repaid in accordance with their terms. At June 30, 2012, other potential problem loans totaled \$53.4 million. Among our potential problem loans are several large credit relationships. Consequently, an adverse development with respect to one of these loans or credit relationships could expose us to a significant increase in nonperforming assets.

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The actual volume of future distressed asset sales could increase based on regulatory directives, the level of migration of performing loans to problem loan status, as well as opportunities to sell such assets, thus resulting in higher credit costs. The continuing weakness in the residential and commercial real estate markets may negatively impact the ability to dispose of distressed assets, and may result in higher credit losses on sales of distressed assets. Non-performing assets are recorded on the financial statements at the estimated fair value, which considers management's plans for disposition. We will realize additional future losses if the proceeds received upon dispositions of assets are less than the recorded carrying value of such assets. If market conditions continue to decline, the magnitude of losses realized upon the disposition of non-performing assets may increase, which could materially adversely affect our business, financial condition and results of operations.

Further increases in non-performing assets may reduce interest income and increase net loan charge-offs, provision for loan losses, and operating expenses.

As a result of the prolonged economic downturn, we are experiencing historically high levels of non-accrual loans. Non-accrual loans increased from 1.87% at December 31, 2009 to 2.49% and 3.02% of total loans at December 31, 2010 and 2011, respectively. Non-accrual loans totaled 2.77% of total loans at June 30, 2012. Until economic and market conditions improve at a more rapid pace, we expect to incur charge-offs to the allowance for loan losses and lost interest income relating to increased non-performing loans and, as a result, additional increases in loan loss reserves may be necessary in the future. Non-performing assets (including non-accrual loans and other real estate owned) totaled \$16.0 million at June 30, 2012. These non-performing assets can adversely affect net income mainly through increased operating expenses incurred to maintain such assets or loss charges related to subsequent declines in the estimated fair value of foreclosed assets. Adverse changes in the value of our non-performing assets, or the underlying collateral, or in the borrowers' performance or financial conditions could adversely affect our business, results of operations and financial condition. There can be no assurance that we will not experience further increases in non-performing loans in the future, or that non-performing assets will not result in lower financial returns in the future.

If our allowance for loan losses becomes inadequate, results of operations may be adversely affected.

We maintain an allowance for loan losses that we believe is a reasonable estimate of known and inherent losses in the Bank's loan portfolio. Through a quarterly review of the loan portfolio, management determines the amount of the allowance for loan losses by considering economic conditions, credit quality of the loan portfolio, collateral supporting the loans, performance of customers relative to their financial obligations and the quality of the Bank's loan administration. The amount of future losses is susceptible to changes in economic, operating and other conditions, including changes in interest rates that may be beyond our control, and these losses may exceed current estimates. Although we believe the allowance for loan losses is a reasonable estimate of known and inherent losses in the loan portfolio, such losses and the adequacy of the allowance for loan losses cannot be fully predicted. Excessive loan losses could have a material impact on financial performance through additions to the allowance for loan losses.

Federal and state regulators periodically review the allowance for loan losses and may require an increase to the provision for loan losses or recognition of further loan charge-offs, based on judgments different than those of management. Any increase in the amount of provision or loans charged-off as required by these regulatory agencies could have a negative effect on operating results.

If our valuation allowance on OREO becomes inadequate, results of operations may be adversely affected.

We maintain a valuation allowance that we believe is a reasonable estimate of known losses in OREO. We obtain appraisals on all OREO properties on an annual basis and adjust the valuation allowance accordingly. The carrying value of OREO is susceptible to changes in economic and real estate market conditions. Although we

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believe the valuation allowance is a reasonable estimate of known losses, such losses and the adequacy of the allowance cannot be fully predicted. Excessive declines in market values could have a material impact on financial performance.

Our concentrations of loans could result in higher than normal risk of loan defaults and losses.

We offer a variety of secured loans, including commercial lines of credit, commercial term loans, real estate, construction and land development, home equity, consumer and other loans. The majority of the loans are secured by real estate (both residential and commercial) in the market area. At June 30, 2012, these loans totaled \$350.3 million, or 91%, of total loans. A major change in the real estate market, such as further deterioration in the value of this collateral, or in the local or national economy, could adversely affect customers' ability to pay these loans, which in turn could impact us. Risk of loan defaults and foreclosures are unavoidable in the banking industry, and we try to limit exposure to this risk by monitoring extensions of credit carefully. We cannot fully eliminate credit risk, and as a result credit losses may occur in the future.

We rely on secondary sources, such as Federal Home Loan Bank advances, sales of securities and loans, federal funds lines of credit from correspondent banks and out-of-market time deposits, to meet liquidity needs.

In managing our consolidated balance sheet, we depend on secondary sources to provide sufficient liquidity to meet our commitments and business needs, and to accommodate the transaction and cash management needs of clients. Other sources of funding available to us, and upon which we rely as regular components of our liquidity risk management strategy, include federal funds lines of credit, sales of securities and loans, brokered deposits and borrowings from the Federal Home Loan Bank system. The availability of these funding sources is highly dependent upon the perception of the liquidity and creditworthiness of the financial institution, and such perception can change quickly in response to market conditions or circumstances unique to a particular company. Any occurrence that may limit our access to these sources, such as a decline in the confidence of debt purchasers, or our depositors or counterparties, may adversely affect our liquidity, financial position, and results of operations.

If we need additional capital in the future, we may not be able to obtain it on terms that are favorable. This could negatively affect our performance.

We anticipate that we will have sufficient capital to support asset growth and potential loan charge-offs. However, additional capital may be needed in the future to maintain capital levels. The ability to raise capital through the sale of additional securities will depend primarily upon our financial condition and the condition of financial markets at that time. We may not be able to obtain additional capital in amounts or on terms that are satisfactory. Our ability to grow our balance sheet may be constrained if we are unable to raise additional capital as needed.

Changes in interest rates may negatively impact net interest income if we are unable to successfully manage interest rate risk.

Our profitability will depend substantially upon the spread between the interest rates earned on investments and loans and interest rates paid on deposits and other interest-bearing liabilities. Changes in interest rates, including the shape of the treasury yield curve, will affect our financial performance and condition through the pricing of securities, loans, deposits and borrowings. We attempt to minimize exposure to interest rate risk, but will be unable to eliminate it. Our net interest spread will depend on many factors that are partly or entirely outside of our control, including competition, federal economic, monetary and fiscal policies and general economic conditions.

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Our small-to-medium sized business target market may have fewer financial resources to weather a downturn in the economy.

We target our commercial development and marketing strategy primarily to serve the banking and financial services needs of small and medium sized businesses. These businesses generally have less capital or borrowing capacity than larger entities. If general economic conditions negatively impact this major economic sector in the markets in which we operate, our results of operations and financial condition may be adversely affected.

Difficult market conditions have adversely affected our industry.

Dramatic declines in the housing market over the past three years, with falling home prices and increasing foreclosures and unemployment, have negatively impacted the credit performance of real estate related loans and resulted in significant write-downs of asset values by financial institutions. These write-downs, initially of mortgage-backed securities (MBS) but spreading to other securities and loans has caused many financial institutions to seek additional capital, to reduce or eliminate dividends, to merge with larger and stronger institutions and, in some cases, to fail. Reflecting concern about the stability of the financial markets generally and the strength of counterparties, many lenders and institutional investors have reduced or ceased providing funding to borrowers, including to other financial institutions. This market turmoil and tightening of credit have led to an increased level of commercial and consumer delinquencies, lack of consumer confidence, increased market volatility and widespread reduction of business activity generally. The resulting economic pressure on consumers and lack of confidence in the financial markets has adversely affected our business, financial condition and results of operations. Market developments may affect consumer confidence levels and may cause adverse changes in payment patterns, causing increases in delinquencies and default rates, which may impact charge-offs and the provision for loan losses. A worsening of these conditions would likely have an adverse effect on us and others in the financial services industry.

The soundness of other financial institutions could adversely affect us.

Our ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. As a result, defaults by, or even rumors or questions about, one or more financial services institutions, or the financial services industry generally, may lead to market-wide liquidity problems and to losses or defaults by us or by other institutions. Many of these transactions expose us to credit risk in the event of default of its counterparty or client. There is no assurance that any such losses would not materially and adversely affect our results of operations.

We rely heavily on our management team and the unexpected loss of any of those personnel could adversely affect our operations; we depend on our ability to attract and retain key personnel.

Our future operating results depend substantially upon the continued service of its executive officers and key personnel. Our future operating results also depend in significant part upon our ability to attract and retain qualified management, financial, technical, marketing, sales and support personnel. Competition for qualified personnel is intense, and we cannot ensure success in attracting or retaining qualified personnel. There may be only a limited number of persons with the requisite skills to serve in these positions, and it may be increasingly difficult for us to hire personnel over time.

Our ability to retain key officers and employees may be further impacted by legislation and regulation affecting the financial services industry. For example, certain executive compensation restrictions apply to us as a result of our participation in the CPP and shall generally continue to apply for as long as any Preferred Shares are owned by Treasury. Such restrictions and standards may further impact management's ability to compete with financial institutions that are not subject to the same limitations as us as a result of the CPP.

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Our compensation expense may increase substantially after Treasury's sale of the Preferred Shares.

As a result of our participation in the CPP, among other things, we are subject to Treasury's current standards for executive compensation and corporate governance for the period during which Treasury holds any of our Preferred Shares. These standards were most recently set forth in the Interim Final Rule on TARP Standards for Compensation and Corporate Governance, published June 15, 2009. If the auction is successful and Treasury elects to sell all of the Preferred Shares, these executive compensation and corporate governance standards will no longer be applicable and our compensation expense for our executive officers and other senior employees may increase substantially.

Future success is dependent on the ability to compete effectively in the highly competitive banking industry.

We face vigorous competition from other financial institutions, including other commercial banks, savings and loan associations, savings banks, finance companies and credit unions for deposits, loans and other financial services in its market area. A number of these other financial institutions are significantly larger than us and have substantially greater access to capital and other resources, as well as larger lending limits and branch systems, and offer a wider array of banking services. To a limited extent we also compete with other providers of financial services, such as money market mutual funds, brokerage firms, insurance companies and governmental organizations which may offer more favorable products and services than us. Many of the non-bank competitors are not subject to the same extensive regulations that govern us. As a result, the non-bank competitors have advantages over us in providing certain services. This competition may reduce or limit profit margins and market share and may adversely affect the results of operations and financial condition.

Regulation by federal and state agencies could adversely affect the profitability of the business.

We are heavily regulated by federal and state agencies. This regulation is to protect depositors, the federal deposit insurance fund and the banking system as a whole. Congress and state legislatures and federal and state regulatory agencies continually review banking laws, regulations, and policies for possible changes. Changes to statutes, regulations, or regulatory policies, including interpretation or implementation of statutes, regulations, or policies, could affect us adversely, including limiting the types of financial services and products we may offer and/or increasing the ability of non-banks to offer competing financial services and products. If we do not comply with laws, regulations, or policies, we could receive regulatory sanctions and damage to our reputation.

Government measures to regulate the financial industry, including the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), subject us to increased regulation and could adversely affect us.

As a financial institution, we are heavily regulated at the state and federal levels. As a result of the financial crisis and related global economic downturn that began in 2007, we have faced, and expect to continue to face, increased public and legislative scrutiny as well as stricter and more comprehensive regulation of our financial services practices. In July 2010, the Dodd-Frank Act was signed into law. The Dodd-Frank Act includes significant changes in the financial regulatory landscape and will impact all financial institutions, including the Company and the Bank. Many of the provisions of the Dodd-Frank Act have begun to be or will be implemented over the next several months and years and will be subject both to further rulemaking and the discretion of applicable regulatory bodies. Because the ultimate impact of the Dodd-Frank Act will depend on future regulatory rulemaking and interpretation, we cannot predict the full effect of this legislation on our businesses, financial condition or results of operations.

In December 2010, the Basel Committee on Banking Supervision, an international forum for cooperation on banking supervisory matters, announced the Basel III capital rules, which set new capital requirements for banking organizations. On June 7, 2012, the Federal Reserve Board requested comment on three proposed rules that, taken together, would establish an integrated regulatory capital framework implementing the Basel III

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regulatory capital reforms in the United States. As proposed, the U.S. implementation of Basel III would lead to significantly higher capital requirements and more restrictive leverage and liquidity ratios than those currently in place. Once adopted, these new capital requirements would be phased in over time. Additionally, the U.S. implementation of Basel III contemplates that, for banking organizations with less than \$15 billion in assets, the ability to treat trust preferred securities as tier 1 capital would be phased out over a ten-year period. The ultimate impact of the U.S. implementation of the new capital and liquidity standards on the Company and the Bank is currently being reviewed. At this point we cannot determine the ultimate effect that any final regulations, if enacted, would have upon our earnings or financial position. In addition, important questions remain as to how the numerous capital and liquidity mandates of the Dodd-Frank Act will be integrated with the requirements of Basel III.

Recently enacted legislation could allow us to deregister under the Exchange Act, which would result in a reduction in the amount and frequency of publicly-available information about us.

Recently enacted legislation called the Jumpstart Our Business Startups Act (or JOBS Act) may allow us to terminate the registration of our common stock under the Exchange Act. If we determined to deregister our common stock under the Exchange Act, it would enable us to save significant expenses relating to our public disclosure and reporting requirements under the Exchange Act. However, a deregistration of our common stock also would result in a reduction in the amount and frequency of publicly-available information about the Company and the Bank.

Changes in our accounting policies or in accounting standards could materially affect how we report financial results and condition.

From time to time, the Financial Accounting Standards Board (FASB) and SEC change the financial accounting and reporting standards that govern the preparation of our financial statements. These changes can be hard to predict and can materially impact how we record and report our financial condition and results of operations. In some cases, we could be required to apply a new or revised standard retroactively, resulting in restating prior period financial statements.

Our ability to operate profitably may be dependent on our ability to implement various technologies into our operations.

The market for financial services, including banking service and consumer finance services is increasingly affected by advances in technology, including developments in telecommunications, data processing, computers, automation, internet-based banking and tele-banking. Our ability to compete successfully in its market may depend on the extent to which we are able to exploit such technological changes. If we are not able to afford such technologies, properly or timely anticipate or implement such technologies, or properly train its staff to use such technologies, our business, financial condition or operating results could be adversely affected.

Our operations depend upon third party vendors that perform services for us.

We outsource many of our operating and banking functions, including some data processing functions and the interchange and transmission services for the ATM network. As such, our success and ability to expand operations depends on the services provided by these third parties. Disputes with these third parties may adversely affect operations. We may not be able to engage appropriate vendors to adequately service our needs, and the vendors that we engage may not be able to perform successfully.

Negative public opinion could damage our reputation and adversely impact liquidity and profitability.

As a financial institution, our earnings, liquidity, and capital are subject to risks associated with negative public opinion of us and of the financial services industry as a whole. Negative public opinion could result from our actual or alleged conduct in any number of activities, including lending practices, the failure of any product

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or service sold by us to meet our clients' expectations or applicable regulatory requirements, corporate governance and acquisitions, or from actions taken by government regulators and community organizations in response to those activities. Negative public opinion can adversely affect our ability to keep, attract and/or retain customers and can expose us to litigation and regulatory action. Actual or alleged conduct by one of our businesses can result in negative public opinion about our other businesses. Negative public opinion could also affect our ability to borrow funds in the unsecured wholesale debt markets.

Potential future losses may result in an additional valuation allowance for deferred tax assets. Recapture of the deferred tax asset balance (i.e., reversal of the valuation allowance) is subject to considerable judgment and could be adversely impacted by changes in future income tax rates.

During 2011, we reached a three-year cumulative pre-tax loss position. Under GAAP, cumulative losses in recent years are considered significant negative evidence which is difficult to overcome in assessing the realizability of a deferred tax asset. As a result, beginning with the fourth quarter of 2011, we no longer consider future taxable income in determining the realizability of its deferred tax assets. At June 30, 2012, we had recorded a full valuation allowance of \$6.5 million on its net deferred tax assets.

We expect to reverse the valuation allowance for deferred tax assets once it has demonstrated a sustainable return to profitability. However, the reversal of the valuation allowance is subject to considerable judgment. Additionally, even after the recovery of the deferred tax asset balance under GAAP, which would immediately benefit GAAP capital and the tangible common equity ratio, there will remain limitations on the ability to include the deferred tax assets for regulatory capital purposes.

Increases in FDIC insurance premiums could adversely affect our profitability.

The Dodd-Frank Act directed the FDIC to amend its regulations to re-define the method of calculation of an insured depository institution's insurance fund assessment. The Dodd-Frank Act requires the assessment base to be an amount equal to the average consolidated total assets of the insured depository institution during the assessment period, minus the sum of the average tangible equity of the insured depository institution during the assessment period and an amount the FDIC determines is necessary to establish assessments consistent with the risk-based assessment system found in the Federal Deposit Insurance Act. The FDIC has issued final rules outlining this new insurance assessment methodology, which will impact the amount of the Bank's insurance assessment. In addition, the FDIC may make additional changes to the way in which it calculates insurance premiums. We cannot predict the timing of any future changes, and if made, the effect that these changes could have on our insurance assessment.

Risk Factors Related to an Investment in the Preferred Shares

The Preferred Shares are equity and are subordinated to all of our existing and future indebtedness; we are highly dependent on dividends and other amounts from our subsidiaries in order to pay dividends on, and redeem at our option, the Preferred Shares, which are subject to various prohibitions and other restrictions; and the Preferred Shares place no limitations on the amount of indebtedness we and our subsidiaries may incur in the future.

The Preferred Shares are equity interests in the Company and do not constitute indebtedness. As such, the Preferred Shares, like our common stock, rank junior to all existing and future indebtedness and other non-equity claims on the Company with respect to assets available to satisfy claims on the Company, including in a liquidation of the Company. Additionally, unlike indebtedness, where principal and interest would customarily be payable on specified due dates, in the case of perpetual preferred stock like the Preferred Shares, there is no stated maturity date (although the Preferred Shares are subject to redemption at our option) and dividends are payable only if, when and as authorized and declared by our board of directors and depend on, among other matters, our historical and projected results of operations, liquidity, cash flows, capital levels, financial condition, debt service requirements and other cash needs, financing covenants, applicable state law, federal and state

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regulatory prohibitions and other restrictions and any other factors our board of directors deems relevant at the time. The Company currently must inform and consult with its regulators prior to paying any dividends on the Preferred Shares.

If (i) there has occurred and is continuing an event of default under the Company's trust preferred securities or (ii) the Company has given notice of its election to defer payments of interest on its trust preferred securities or such a deferral has occurred and is continuing, then the Company may not declare or pay any dividends or distributions on, or redeem, purchase, acquire or make a liquidation payment with respect to, any of its capital stock (including the Preferred Shares).

The Preferred Shares are not savings accounts, deposits or other obligations of any depository institution and are not insured or guaranteed by the FDIC or any other governmental agency or instrumentality. Furthermore, the Company is a legal entity that is separate and distinct from its subsidiaries, and its subsidiaries have no obligation, contingent or otherwise, to make any payments in respect of the Preferred Shares or to make funds available therefor. Because the Company is a holding company that maintains only limited cash at that level, its ability to pay dividends on, and redeem at its option, the Preferred Shares will be highly dependent upon the receipt of dividends, fees and other amounts from its subsidiaries, which, in turn, will be highly dependent upon the historical and projected results of operations, liquidity, cash flows and financial condition of its subsidiaries. In addition, the right of the Company to participate in any distribution of assets of any of its subsidiaries upon their respective liquidation or reorganization will be subject to the prior claims of the creditors (including any depositors) and preferred equity holders of the applicable subsidiary, except to the extent that the Company is a creditor, and is recognized as a creditor, of such subsidiary. Accordingly, the holders of the Preferred Shares will be structurally subordinated to all existing and future obligations and preferred equity of the Company's subsidiaries.

There are also various legal and regu