

BANK OF SOUTH CAROLINA CORP
Form 10-Q
August 09, 2011

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period
ended June 30, 2011

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number: 0-27702

Bank of South Carolina Corporation
(Exact name of registrant issuer as specified in its charter)

South Carolina
(State or other jurisdiction of
incorporation or organization)

57-1021355
(IRS Employer Identification Number)

256 Meeting Street, Charleston, SC 29401
(Address of principal executive offices)

(843) 724-1500
(Registrant's telephone number)

Indicate by check mark whether the issuer (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its Company 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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.

Large accelerated filer

Accelerated filer

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Non-accelerated filer

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

As of August 3, 2011 there were 4,444,275 Common Shares outstanding.

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for quarter ended
June 30, 2011

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PART I - ITEM 1 - FINANCIAL STATEMENTS

BANK OF SOUTH CAROLINA CORPORATION AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

	(Unaudited) June 30, 2011	(Audited) December 31, 2010
Assets:		
Cash and due from banks	\$5,148,410	\$ 4,697,450
Interest bearing deposits in other banks	22,361,541	715,231
Federal funds sold	—	19,018,104
Investment securities available for sale	53,243,002	39,379,613
Mortgage loans to be sold	3,620,934	5,908,316
Loans	212,335,093	208,025,664
Allowance for loan losses	(2,854,059)	(2,938,588)
Net loans	209,481,034	205,087,076
Premises and equipment, net	2,401,831	2,436,526
Other real estate owned	659,430	659,492
Accrued interest receivable	1,004,740	1,054,791
Other assets	1,199,391	1,564,668
Total assets	\$299,120,313	\$ 280,521,267
Liabilities and Shareholders' Equity:		
Deposits:		
Non-interest bearing demand	\$63,941,545	\$ 56,884,235
Interest bearing demand	54,277,473	50,394,101
Money market accounts	74,989,657	68,007,823
Certificates of deposit \$100,000 and over	42,200,691	45,523,280
Other time deposits	17,816,022	17,760,278
Other savings deposits	14,136,458	11,867,258
Total deposits	267,361,846	250,436,975
Short-term borrowings	404,286	767,497
Accrued interest payable and other liabilities	1,130,456	597,913
Total liabilities	268,896,588	251,802,385
Common Stock - No par value; 12,000,000 shares authorized; Shares issued 4,663,726 at June 30, 2011 and 4,649,317 at December 31, 2010; Shares outstanding 4,444,275 at June 30, 2011 and 4,429,866 shares at December 31, 2010	—	—
Additional paid in capital	28,342,627	28,202,939
Retained earnings	2,697,641	2,167,927
Treasury stock – 219,451 shares at June 30, 2011 and December 31, 2010	(1,902,439)	(1,902,439)
Accumulated other comprehensive income, net of income taxes	1,085,896	250,455
Total shareholders' equity	30,223,725	28,718,882
Total liabilities and shareholders' equity	\$299,120,313	\$ 280,521,267

See accompanying notes to consolidated financial statements

BANK OF SOUTH CAROLINA CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	Three Months Ended June 30,	
	2011	2010
Interest and fee income		
Interest and fees on loans	\$2,702,717	\$2,571,561
Interest and dividends on investment securities	323,909	380,417
Other interest income	15,888	2,859
Total interest and fee income	3,042,514	2,954,837
Interest expense		
Interest on deposits	213,883	271,601
Interest on short-term borrowings	—	1,245
Total interest expense	213,883	272,846
Net interest income	2,828,631	2,681,991
Provision for loan losses	120,000	110,000
Net interest income after provision for loan losses	2,708,631	2,571,991
Other income		
Service charges, fees and commissions	228,323	263,338
Mortgage banking income	143,383	203,703
Gain on sale of securities	58,186	—
Other non-interest income	9,188	6,546
Total other income	439,080	473,587
Other expense		
Salaries and employee benefits	1,177,992	1,131,524
Net occupancy expense	330,339	334,331
Other operating expenses	537,545	524,702
Total other expense	2,045,876	1,990,557
Income before income tax expense	1,101,835	1,055,021
Income tax expense	333,810	326,179
Net income	\$768,025	\$728,842
Basic earnings per share	\$0.17	\$0.17
Diluted earnings per share	\$0.17	\$0.17
Weighted average shares outstanding		
Basic	4,460,218	4,408,037
Diluted	4,460,218	4,408,037
Cash Dividend Per Share	\$0.10	\$0.10

All share and per share data have been restated to reflect a 10% stock dividend declared on August 26, 2010.

See accompanying notes to consolidated financial statements

BANK OF SOUTH CAROLINA CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

	Six Months Ended June 30,	
	2011	2010
Interest and fee income		
Interest and fees on loans	\$ 5,319,301	\$ 5,243,002
Interest and dividends on investment securities	645,464	747,364
Other interest income	26,453	3,925
Total interest and fee income	5,991,218	5,994,291
Interest expense		
Interest on deposits	449,820	557,039
Interest on short-term borrowings	—	8,610
Total interest expense	449,820	565,649
Net interest income	5,541,398	5,428,642
Provision for loan losses	240,000	230,000
Net interest income after provision for loan losses	5,301,398	5,198,642
Other income		
Service charges, fees and commissions	474,210	511,619
Mortgage banking income	321,647	370,580
Gain on sale of securities	58,186	—
Other non-interest income	14,364	12,139
Total other income	868,407	894,338
Other expense		
Salaries and employee benefits	2,348,392	2,298,380
Net occupancy expense	664,816	644,917
Other operating expenses	1,129,104	1,032,925
Total other expense	4,142,312	3,976,222
Income before income tax expense	2,027,493	2,116,758
Income tax expense	610,099	661,049
Net income	\$ 1,417,394	\$ 1,455,709
Basic earnings per share	\$ 0.32	\$ 0.33
Diluted earnings per share	\$ 0.32	\$ 0.33
Weighted average shares outstanding		
Basic	4,454,969	4,405,633
Diluted	4,454,969	4,405,633
Cash Dividend Per Share	\$ 0.20	\$ 0.20

All share and per share data have been restated to reflect a 10% stock dividend declared on August 26, 2010.

See accompanying notes to consolidated financial statements

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BANK OF SOUTH CAROLINA CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME
(UNAUDITED)
FOR SIX MONTHS ENDED JUNE 30, 2011 AND 2010

	Common Stock	Additional Paid In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income	Total
December 31, 2009	\$—	\$23,511,560	\$4,968,336	\$(1,692,964)	\$ 780,265	\$27,567,197
Comprehensive income:						
Net income	—	—	1,455,709	—	—	1,455,709
Net unrealized loss on securities (net of tax effect of \$136,116)	—	—	—	—	(231,766)	(231,766)
Comprehensive income	—	—	—	—	—	1,223,943
Exercise of stock options	—	146,482	—	—	—	146,482
Stock-based compensation expense	—	23,600	—	—	—	23,600
Cash dividends (\$0.20 per common share)	—	—	(802,220)	—	—	(802,220)
June 30, 2010	\$—	\$23,681,642	\$5,621,825	\$(1,692,964)	\$ 548,499	\$28,159,002
December 31, 2010	\$—	\$28,202,939	\$2,167,927	\$(1,902,439)	\$ 250,455	\$28,718,882
Comprehensive income:						
Net income	—	—	1,417,394	—	—	1,417,394
Net unrealized gain on securities (net of tax effect of \$512,184)	—	—	—	—	872,098	872,098
Reclassification adjustment for gains included in income (net of tax effect of \$21,529)	—	—	—	—	(36,657)	(36,657)

Total comprehensive income	—	—	—	—	—	2,252,835
Exercise of stock options	—	117,724	—	—	—	117,724
Stock-based compensation expense	—	21,964	—	—	—	21,964
Cash dividends (\$0.20 per common share)	—	—	(887,680)	—	—	(887,680)
June 30, 2011	\$—	\$28,342,627	\$2,697,641	\$(1,902,439)	\$ 1,085,896	\$30,223,725

See accompanying notes to consolidated financial statements.

BANK OF SOUTH CAROLINA CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Six months Ended June 30,	
	2011	2010
Cash flows from operating activities:		
Net income	\$1,417,394	\$1,455,709
Adjustments to reconcile net income to net cash provided (used) by operating activities:		
Depreciation	107,466	127,331
Gain on sale of securities	(58,186)	—
Provision for loan losses	240,000	230,000
Stock-based compensation expense	21,964	23,600
Net (accretion) and amortization of unearned discounts and premiums on investments	(62,394)	19,423
Origination of mortgage loans held for sale	(22,487,584)	(29,941,324)
Proceeds from sale of mortgage loans held for sale	24,774,966	29,365,640
(Increase) decrease in accrued interest receivable and other assets	49,523	(173,125)
Increase in accrued interest payable and other liabilities	88,115	717
Net cash provided by operating activities	4,091,264	1,107,971
Cash flows from investing activities:		
Purchase of investment securities available for sale	(33,789,626)	(2,430,705)
Maturities and calls of investment securities available for sale	9,160,000	420,000
Net (increase) decrease in loans	(4,633,958)	9,315,237
Purchase of premises and equipment	(72,771)	(63,801)
Proceeds from the sale of available for sale securities	12,088,125	—
Purchase of other real estate owned	—	(101,300)
Proceeds from the sale of other real estate owned	—	65,000
Net cash (used) provided by investing activities	(17,248,230)	7,204,431
Cash flows from financing activities:		
Net increase in deposit accounts	16,924,871	3,439,274
Net decrease in short-term borrowings	(363,211)	(7,721,456)
Dividends paid	(443,252)	(400,291)
Stock options exercised	117,724	146,482
Net cash provided (used) by financing activities	16,236,132	(4,535,991)
Net increase in cash and cash equivalents	3,079,166	3,776,411
Cash and cash equivalents, beginning of period	24,430,785	9,582,502
Cash and cash equivalents, end of period	\$27,509,951	\$13,358,913
Supplemental disclosure of cash flow data:		
Cash paid during the period for:		
Interest	\$514,377	\$546,441

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Income taxes	\$164,111	\$725,404
Supplemental disclosure for non-cash investing and financing activity:		
Change in dividends payable	\$444,428	\$400,291
Transfer of loans to other real estate owned	\$—	\$183,340
Change in unrealized gains (losses) on available for sale securities	\$872,098	\$(231,766)

See accompanying notes to consolidated financial statements.

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BANK OF SOUTH CAROLINA CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
JUNE 30, 2011

NOTE 1: Basis of Presentation

The Bank of South Carolina (the "Bank") was organized on October 22, 1986 and opened for business as a state-chartered financial institution on February 26, 1987, in Charleston, South Carolina. The Bank was reorganized into a wholly-owned subsidiary of Bank of South Carolina Corporation (the "Company"), effective April 17, 1995. At the time of the reorganization, each outstanding share of the Bank was exchanged for two shares of Bank of South Carolina Corporation Stock. The Company operates as a commercial bank from four banking houses located at: 256 Meeting Street, Charleston, SC, 100 North Main Street, Summerville, SC, 1337 Chuck Dawley Boulevard, Mt. Pleasant, SC and 2027 Sam Rittenberg Boulevard, Charleston, SC.

The consolidated financial statements in this report are unaudited, except for the December 31, 2010 consolidated balance sheet. All adjustments consisting of normal recurring accruals which are, in the opinion of management, necessary for fair presentation of the interim consolidated financial statements have been included and fairly and accurately present the financial position, results of operations and cash flows of the Company. The results of operations for the three and six months ended June 30, 2011, are not necessarily indicative of the results which may be expected for the entire year.

The preparation of the consolidated financial statements is in conformity with accounting principles generally accepted in the United States of America (GAAP) which requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. In addition, they affect the reported amounts of income and expense during the reporting period. Actual results could differ from these estimates and assumptions.

In preparing these financial statements, the Company has evaluated events and transactions for potential recognition or disclosure through the date the financial statements were available to be issued.

NOTE 2: Reclassifications

Certain captions and amounts in the financial statements in the Company's Form 10-Q for the quarter ended June 30, 2010 and the year ended December 31, 2010 were reclassified to conform to the June 30, 2011 presentation.

NOTE 3: Investment Securities

The Company classifies investments into three categories as follows: (1) Held to Maturity - debt securities that the Company has the positive intent and ability to hold to maturity, which are reported at amortized cost, adjusted for the amortization of any related premiums or the accretion of any related discounts into interest income using a methodology which approximates a level yield of interest over the estimated remaining period until maturity; (2) Trading - debt and equity securities that are bought and held principally for the purpose of selling them in the near term, which are reported at fair value, with unrealized gains and losses included in earnings; and (3) Available for Sale - debt and equity securities that may be sold under certain conditions, which are reported at fair value, with unrealized gains and losses excluded from earnings and reported as a separate component of shareholders' equity, net of income taxes. Unrealized losses on securities due to fluctuations in fair value are recognized when it is determined that an other than temporary decline in value has occurred. Realized gains or losses on the sale of investments are recognized on a specific identification, trade date basis. All securities were classified as available for sale for the three and six months ended June 30, 2011 and 2010. The Company does not have any mortgage-backed securities nor has it ever invested in mortgage-backed securities.

Note 4: Mortgage Loans to be Sold:

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated market value in the aggregate. Net unrealized losses are provided for in a valuation allowance by charges to operations as a component of mortgage banking income. At June 30, 2011 and December 31, 2010, the Company had approximately \$3.6 million and \$5.9 million in mortgage loans held for sale, respectively. Gains or losses on sales of loans are recognized when control over these assets has been surrendered and are included in mortgage banking income in the consolidated statements of income.

Note 5: Loans and Allowance for Loan Losses:

Loans are carried at principal amounts outstanding. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment to yield. Interest income on all loans is recorded on an accrual basis. The accrual of interest is generally discontinued on loans which become 90 days past due as to principal or interest. The accrual of interest on some loans, however, may continue even though they are 90 days past due if the loans are well secured, in the process of collection, and management deems it appropriate. Non-accrual loans are reviewed individually by management to determine if they should be returned to accrual status. The Company defines past due loans based on contractual payment and maturity dates.

The Company accounts for nonrefundable fees and costs associated with originating or acquiring loans and direct costs of leases by requiring that loan origination fees be recognized over the life on the related loan as an adjustment on the loan's yield. Certain direct loan origination costs shall be recognized over the life of the related loan as a reduction of the loan's yield. This statement changed the practice of recognizing loan origination and commitment fees prior to inception of the loan.

The Company accounts for impaired loans by requiring that all loans for which it is estimated that the Company will be unable to collect all amounts due according to the terms of the loan agreement be recorded at the loan's fair value. Fair value may be determined based upon the present value of expected cash flows, market price of the loan, if available, or value of the underlying collateral. Expected cash flows are required to be discounted at the loan's effective interest rate.

Additional accounting guidance allows the Company to use existing methods for recognizing interest income on an impaired loan and by requiring additional disclosures about how the Company estimates interest income related to impaired loans.

When the ultimate collectability of an impaired loan's principal is in doubt, wholly or partially, all cash receipts are applied to principal. Once the recorded principal balance has been reduced to zero, future cash receipts are applied to interest income, to the extent that any interest has been foregone. Further cash receipts are recorded as recoveries of any amounts previously charged off. When this doubt does not exist, cash receipts are applied under the contractual terms of the loan agreement first to interest income and then to principal.

A loan is also considered impaired if its terms are modified in a troubled debt restructuring. For these accruing impaired loans, cash receipts are typically applied to principal and interest receivable in accordance with the terms of the restructured loan agreement. Interest income is recognized on these loans using the accrual method of accounting, provided they are performing in accordance with their restructured terms.

Management believes that the allowance is adequate to absorb inherent losses in the loan portfolio; however, assessing the adequacy of the allowance is a process that requires considerable judgment. Management's judgments are based on numerous assumptions about current events which management believes to be reasonable, but which may or may not be valid. Thus there can be no assurance that loan losses in future periods will not exceed the current allowance

amount or that future increases in the allowance will not be required. No assurance can be given that management's ongoing evaluation of the loan portfolio in light of changing economic conditions and other relevant circumstances will not require significant future additions to the allowance, thus adversely affecting the operating results of the Company.

The allowance is also subject to examination by regulatory agencies, which may consider such factors as the methodology used to determine adequacy and the size of the allowance relative to that of peer institutions, and other adequacy tests. In addition, such regulatory agencies could require the Company to adjust its allowance based on information available to them at the time of their examination.

The methodology used to determine the reserve for unfunded lending commitments, which is included in other liabilities, is inherently similar to that used to determine the allowance for loan losses adjusted for factors specific to binding commitments, including the probability of funding and historical loss ratio.

The following is a summary of the non-accrual loans as of June 30, 2011 and December 31, 2010.

Loans Receivable on Non-Accrual at June 30, 2011

Commercial	\$ 5,599
Commercial Real Estate:	
Commercial Real Estate - Construction	-
Commercial Real Estate - Other	838,117
Consumer Real Estate	67,981
Total	\$ 911,697

Loans Receivable on Non-Accrual at December 31, 2010

Commercial	\$ 6,702
Commercial Real Estate:	
Commercial Real Estate - Construction	-
Commercial Real Estate - Other	938,626
Total	\$ 945,328

The following schedules summarize the Bank's delinquent loans, excluding mortgage loans held for sale and deferred loan fees, as of June 30, 2011 and December 31, 2010.

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans Receivable	Recorded Investment > 90 Days and Accruing
June 30, 2011							
Commercial	\$4,330	119,477	-	123,807	52,685,562	52,809,459	-
Commercial Real Estate:							
Commercial Real Estate	465,178	1,157,072	488,739	2,110,989	105,183,296	107,294,285	-
Commercial Real Estate -Construction	-	-	-	-	4,802,531	4,802,531	-
Consumer:							
Consumer- Real Estate	-	-	-	-	42,499,017	42,499,017	-
Consumer-Other	44,670	4,027	-	48,697	4,881,104	4,929,801	-
Total	\$514,178	1,280,576	488,739	2,283,493	210,019,776	212,335,093	-
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans Receivable	Recorded Investment > 90 Days and Accruing
December 31, 2010							
Commercial	\$7,056	8,038	-	15,094	50,603,851	50,618,945	-
Commercial Real Estate:							
Commercial Real Estate -Construction	-	-	-	-	-	-	-
Commercial Real Estate -Other	134,072		589,225	723,297	107,281,613	108,004,910	-
Consumer:							
Consumer-Other	309,684	5,864		315,548	49,086,261	49,401,809	-
Total	\$450,812	13,902	589,225	1,053,939	206,971,725	208,025,664	-

As of June 30, 2011 and December 31, 2010 loans individually evaluated and considered impaired are presented in the following tables:

Impaired and Restructured Loans
For the Three Months Ended June 30, 2011

With no related allowance recorded:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
Commercial	\$ 83,350	\$ 5,626	\$ -	\$ 9,186	\$ 34,138
Commercial Real Estate	1,747,543	1,773,158	-	1,764,246	353,341
Consumer Real Estate	417,286	415,713	-	416,381	59,824
Total	\$ 2,248,179	\$ 2,194,497	\$ -	\$ 2,189,813	\$ 447,303

With an allowance recorded:

Commercial	\$ 1,211,163	\$ 1,198,663	\$ 1,198,663	\$ 1,206,996	\$ 65,713
Commercial Real Estate	426,000	359,551	90,591	378,045	52,372
Consumer Real Estate	725,000	721,542	263,215	721,542	259,481
Total	\$ 2,362,163	\$ 2,279,756	\$ 1,552,469	\$ 2,306,583	\$ 377,566

Impaired Loans
For the Year Ended December 31, 2010

With no related allowance recorded:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
Commercial	\$ 83,350	\$ 6,702	\$ -	\$ 12,230	\$ 33,997
Commercial Real Estate	2,317,543	2,020,682	-	833,939	391,574
Consumer Real Estate	230,250	230,022	-	836,169	425,571
Total	\$ 2,631,143	\$ 2,257,406	\$ -	\$ 1,682,338	\$

With an allowance recorded

Commercial	\$ 1,211,163	\$ 1,207,163	\$ 1,207,163	\$ 807,846	\$ 41,714
Commercial Real Estate	126,000	94,959	86,084	87,431	17,702
Consumer Real Estate	-	-	-	-	-
Total	\$ 1,337,163	\$ 1,302,122	\$ 1,293,247	\$ 895,277	\$ 59,416

The following tables illustrate credit risks by category and internally assigned grades at June 30, 2011 and December 31, 2010.

June 30, 2011	Commercial	Commercial Real Estate Construction	Commercial Real Estate	Residential – Real Estate	Consumer – Other
Pass	\$46,373,920	\$ 4,328,257	\$98,906,185	40,967,803	4,301,202
Watch	2,543,687	474,274	4,366,305	87,425	198,109
OAEM	2,577,697	-	423,252	216,522	325,110
Sub-Standard	1,314,155	-	3,598,543	1,227,267	104,226
Doubtful	-	-	-	-	1,154
Loss	-	-	-	-	-
Total	\$52,809,459	\$ 4,802,531	\$107,294,285	42,499,017	4,929,801

December, 31, 2010	Commercial	Commercial Real Estate Construction	Commercial Real Estate	Residential – Real Estate	Consumer – Other
Pass	\$44,264,102	\$ 2,226,325	\$97,949,596	42,017,198	4,915,583
Watch	3,070,186	475,225	3,516,001	338,614	363,798
OAEM	1,934,919	-	116,277	379,092	234,007
Sub-Standard	1,349,738	-	3,721,487	1,071,100	79,985
Doubtful	-	-	-	-	2,431
Loss	-	-	-	-	-
Total	\$50,618,945	\$ 2,701,550	\$105,303,361	43,806,004	5,595,804

The following tables set forth the changes in the allowance and an allocation of the allowance by loan category at June 30, 2011 and December 31, 2010. The allocation of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged-off. The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired. The general component covers non-impaired loans and is based on historical loss experience adjusted for current economic factors described above.

June 30, 2011	Commercial	Commercial Real Estate	Consumer	Residential	Unallocated	Total
Allowance for Loan Losses						
Beginning Balance	\$1,502,298	\$128,334	\$27,200	\$218,897	\$1,061,859	\$2,938,588
Charge-offs	17,943	303,403	50,630	-	-	371,976
Recoveries	22,357	24,990	100	-	-	47,447
Provisions	(11,221)	381,285	62,392	236,448	(428,905)	239,999
Ending Balance	1,495,491	231,206	39,062	455,345	632,954	2,854,058
Ending Balances:						
Individually evaluated for impairment	1,204,289	2,132,709	-	1,137,255	-	4,474,253
Collectively evaluated for impairment	\$51,605,170	\$109,964,107	\$4,929,801	\$41,361,762	\$-	\$207,860,840

December 31, 2010	Commercial	Commercial Real Estate	Consumer	Residential	Unallocated	Total
Allowance for Loan Losses						
Beginning Balance	\$1,456,332	\$42,448	\$15,651	\$197,428	\$1,315,138	\$3,026,997
Charge-offs	417,078	21,356	55,257	285,128	-	778,819
Recoveries	14,427	5,484	500	-	-	20,411
Provisions	448,617	101,758	66,306	306,597	(253,279)	669,999
Ending Balance	1,502,298	128,334	27,200	218,897	1,061,859	2,938,588
Ending Balances:						
Individually evaluated for impairment	1,213,865	2,115,641	-	230,022	-	3,559,528
Collectively evaluated for impairment	\$49,405,080	\$105,889,270	\$5,595,804	\$43,575,982	\$-	\$204,466,136

Restructured loans (loans, still accruing interest, which have been renegotiated at below-market interest rates or for which other concessions have been granted) were \$117,764 and \$153,015 at June 30, 2011 and December 31, 2010, respectively. At June 30, 2011, all restructured loans were performing as agreed.

Note 6: Premises, Equipment and Leasehold Improvements and Depreciation:

Buildings and equipment are carried at cost less accumulated depreciation, calculated on the straight-line method over the estimated useful life of the related assets - 40 years for buildings and 3 to 15 years for equipment. Amortization of leasehold improvements is recorded using the straight-line method over the lesser of the estimated useful life of the asset or the term of the lease. Maintenance and repairs are charged to operating expenses as incurred.

Note 7: Other Real Estate Owned:

Other real estate owned is recorded at the lower of fair value less estimated selling costs or cost. The balance of other real estate owned at June 30, 2011 was \$659,430 compared with \$659,492 at December 31, 2010. Gains and losses on the sale of other real estate owned and subsequent write-downs from periodic reevaluation are charged to other operating income.

Note 8: Income Taxes: The Company accounts for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in 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. Net deferred tax assets are included in other assets in the consolidated balance sheet.

Accounting standards require the accounting for uncertainty in income taxes recognized in an enterprise's financial statements. These standards also prescribe a recognition threshold and measurement of a tax position taken or expected to be taken in an enterprise's tax return.

NOTE 9: Stock Based Compensation

The shareholders of the Company voted at the Company's Annual Meeting, April 13, 2010, to approve the 2010 Omnibus Stock Incentive Plan, including 330,000 shares (adjusted for a 10% stock dividend declared on August 26, 2010) reserved under the plan (copy of the plan was filed with 2010 Proxy Statement). This plan is intended to assist the Company in recruiting and retaining employees with ability and initiative by enabling employees to participate in its future success and to associate their interest with those of the Company and its shareholders. Under the Omnibus Stock Incentive Plan, options are periodically granted to employees at a price not less than 100% of the fair market value of the shares at the date of the grant. All employees are eligible to participate in this plan if the Executive Committee, in its sole discretion, determines that such person has contributed or can be expected to contribute to the profits or growth of the Company or its subsidiary. Options may be exercised in whole at any time or in part from time to time at such times and in compliance with such requirements as the Executive Committee shall determine. The maximum period in which an Option may be exercised is determined at the date of grant and shall not exceed 10 years from the date of grant.

The options are not transferable except by will or by the laws of descent and distribution. On March 24, 2011, the Executive Committee granted options to purchase 5,000 shares of stock to 1 employee. Fair value was estimated at the date of grant using the Black-Scholes option pricing model with the following assumptions used for the grant: dividend yield 4.02%, historical volatility 54.43%, risk free interest rate of 3.42%, and an expected life of 10 years. The Executive Committee also granted on June 23, 2011, options to purchase 96,000 shares to 22 employees. Fair value was estimated at the date of grant using the Black-Scholes option pricing model with the following assumptions used for the grant: dividend yield 4.02%, historical volatility 54.43%, risk free interest rate of 2.93%, and an expected life of 10 years.

On April 14, 1998 the Company adopted the 1998 Omnibus Stock Incentive Plan which expired on April 14, 2008. Options can no longer be granted under the 1998 Plan. Options granted before April 14, 2008, shall remain valid in accordance with their terms. On April 14, 2011, options to purchase 741 shares of stock were forfeited. The options were granted on April 14, 2001 and were forfeited in accordance with the plan.

Under both plans employees become 20% vested after five years and vest 20% each year until fully vested. The right to exercise each such 20% of the options is cumulative and will not expire until the tenth anniversary of the date of the

grant.

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The following is a summary of the activity under the 1998 and 2010 Omnibus Stock Incentive Plans for the three and six months ended June 30, 2011 and the 1998 Omnibus Stock Incentive Plan for the three months ended June 30, 2010.

Three Months Ended June 30, 2011	Options	Weighted Average Exercise Price
Balance at April 1, 2011	92,000	\$ 11.59
Granted	96,000	10.42
Exercised	(12,578)	8.18
Forfeited	(741)	8.11
Balance at June 30, 2011	174,681	\$ 11.21

Six Months Ended June 30, 2011	Options	Weighted Average Exercise Price
Balance at January 1, 2011	88,831	\$ 11.51
Granted	5,000	11.67
Granted	96,000	10.42
Exercised	(14,409)	8.17
Forfeited	(741)	8.11
Balance at June 30, 2011	174,681	\$ 11.21
Options exercisable at June 30, 2011	5,197	\$ 8.54

Three months Ended June 30, 2010	Options	Weighted Average Exercise Price
Balance at April 1, 2010	86,995	\$ 10.61
Exercised	(18,028)	8.13
Balance at June 30, 2010	68,967	\$ 10.18

Six months Ended June 30, 2010	Options	Weighted Average Exercise Price
Balance at January 1, 2010	86,995	\$ 10.61
Exercised	(18,028)	8.13
Balance at June 30, 2010	68,967	\$ 10.18
Options exercisable at June 30, 2010	29,798	\$ 8.19

All share and per share data have been restated to reflect a 10% stock dividend declared on August 26, 2010.

NOTE 10: Shareholders' Equity

Regular quarterly cash dividends of \$.10 per share were declared on March 24, 2011 and June 23, 2011 for shareholders of record on April 8, 2011 and July 8, 2011, respectively, payable April 29, 2011 and July 29, 2011, respectively. Income per common share for the three and six months ended June 30, 2011 and for the three and six months ended June 30, 2010 were calculated as follows:

	FOR THE THREE MONTHS ENDED JUNE 30, 2011		
	INCOME (NUMERATOR)	SHARES (DENOMINATOR)	PER SHARE AMOUNT
Net income	\$ 768,025		
Basic income available to common shareholders	\$ 768,025	4,460,218	\$.17
Effect of dilutive options		-	
Diluted income available to common shareholders	\$ 768,025	4,460,218	\$.17
	FOR THE SIX MONTHS ENDED JUNE 30, 2011		
	INCOME (NUMERATOR)	SHARES (DENOMINATOR)	PER SHARE AMOUNT
Net income	\$ 1,417,394		
Basic income available to common shareholders	\$ 1,417,394	4,454,969	\$.32
Effect of dilutive options		-	
Diluted income available to common shareholders	\$ 1,417,394	4,454,969	\$.32
	FOR THE THREE MONTHS ENDED JUNE 30, 2010		
	INCOME (NUMERATOR)	SHARES (DENOMINATOR)	PER SHARE AMOUNT
Net income	\$ 728,842		
Basic income available to common shareholders	\$ 728,842	4,408,037	\$.17

Effect of dilutive options			-
Diluted income available to common shareholders	\$728,842	4,408,037	\$.17

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FOR THE SIX MONTHS ENDED JUNE
30, 2010

	INCOME (NUMERATOR)	SHARES (DENOMINATOR)	PER SHARE AMOUNT
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Net income	\$1,455,709		
Basic income available to common shareholders	\$1,455,709	4,405,633	\$.33
Effect of dilutive options		-	
Diluted income available to common shareholders	\$1,455,709	4,405,633	\$.33

All share and per share data have been restated to reflect a 10% stock dividend declared on August 26, 2010.

The future payment of cash dividends is subject to the discretion of the Board of Directors and depends upon a number of factors, including future earnings, financial condition, cash requirements, and general business conditions. Cash dividends when declared, are paid by the Bank to the Company for distribution to shareholders of the Company. Certain regulatory requirements restrict the amount of dividends which the Bank can pay to the Company.

NOTE 11: Comprehensive Income

The Company applies accounting standards which establish guidance for the reporting and display of comprehensive income and its components in a full set of general purpose financial statements. Comprehensive income consists of net income and net unrealized gains or losses on securities and is presented in the consolidated statements of shareholders' equity and comprehensive income.

Comprehensive income totaled \$2,252,835 at June 30, 2011 and \$1,223,943 at June 30, 2010.

NOTE 12: Fair Value Measurements

Effective January 1, 2008, the Company adopted accounting standards which provide a framework for measuring and disclosing fair value under generally accepted accounting principles. The guidance requires disclosures about the fair value of assets and liabilities recognized in the balance sheet in periods subsequent to initial recognition, whether the measurements are made on a recurring basis (for example, available-for-sale investment securities) or on a nonrecurring basis (for example, impaired loans).

The standard defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The standard also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

- Level 1 Valuation is based upon quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. Level 1 assets and liabilities include debt and equity securities and derivative contracts that are traded in an active exchange market, as well as US Treasuries and money market funds.
- Level 2 Valuation is based upon quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset or liability (other than quoted prices), such as interest rates, foreign exchange rates, and yield curves that are observable at commonly quoted intervals. Level 2 assets and liabilities include debt securities with quoted prices that are traded less frequently than exchange-traded instruments, mortgage-backed securities, municipal bonds, corporate debt securities and derivative contracts whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data. This category generally includes certain derivative contracts and impaired loans.
- Level 3 Valuation is generated from model-based techniques that use at least one significant assumption based on unobservable inputs for the asset or liability, which are typically based on an entity's own assumptions, as there is little, if any, related market activity. In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

The following is a description of the valuation methodologies used for assets and liabilities recorded at fair value.

Investment Securities Available for Sale

Securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange such as the New York Stock Exchange, Treasury Securities that are traded

by dealers or brokers in active over-the counter markets and money market funds. Level 2 securities include mortgage backed securities issued by government sponsored entities, municipal bonds and corporate debt securities. Securities classified as Level 3 include asset-backed securities in less liquid markets.

Mortgage Loans Held for Sale

The Company originates fixed rate residential loans on a servicing released basis in the secondary market. Loans closed but not yet settled with other investors, are carried in the Company's loans held for sale portfolio. These loans are fixed rate residential loans that have been originated in the Company's name and have closed. Virtually all of these loans have commitments to be purchased by investors and the majority of these loans were locked in by price with the investors on the same day or shortly thereafter that the loan was locked in with the Company's customers. Therefore, these loans present very little market risk for the Company. The Company usually delivers to, and receives funding from, the investor within 30 days. Commitments to sell these loans to the investor are considered derivative contracts and are sold to investors on a "best efforts" basis. The Company is not obligated to deliver a loan or pay a penalty if a loan is not delivered to the investor. As a result of the short-term nature of these derivative contracts, the fair value of the mortgage loans held for sale in most cases is the same as the value of the loan amount at its origination. These loans are classified as Level 2.

Assets and liabilities measured at fair value on a recurring basis at June 30, 2011 and December 31, 2010 are as follows:

	Quoted Market Price in active markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at June 30, 2011
US Treasury Notes	\$12,331,876	\$-	\$ -	\$12,331,876
Government Sponsored Enterprises	\$-	\$12,435,100	\$ -	\$12,435,100
Municipal Securities	\$-	\$28,476,026	\$ -	\$28,476,026
Mortgage loans to be sold	\$-	\$3,620,934	\$ -	\$3,620,934
Total	\$12,331,876	\$44,532,060	\$ -	\$56,863,936

	Quoted Market Price in active markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2010
US Treasury Notes	\$9,023,437	\$-	\$ -	\$9,023,437
Government Sponsored Enterprises	\$-	\$6,100,545	\$ -	\$6,100,545
Municipal Securities	\$-	\$24,255,631	\$ -	\$24,255,631
Mortgage loans to be sold	\$-	\$5,908,316	\$ -	\$5,908,316
Total	\$9,023,437	\$36,264,492	\$ -	\$45,287,929

Other Real Estate Owned (OREO)

Loans, secured by real estate, are adjusted to fair value upon transfer to other real estate owned (OREO). Subsequently, OREO is carried at the lower of carrying value or fair value. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraisal, the Company records the OREO as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the asset as nonrecurring Level 3.

Impaired Loans

The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and an allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment in accordance with ASC 310-10, "Accounting by Creditors for Impairment of a Loan".

In accordance with this standard, the fair value is estimated using one of the following methods: fair value of the collateral less estimated costs to sell, discounted cash flows, or market value of the loan based on similar debt. The fair value of the collateral less estimated costs to sell is the most frequently used method. Typically, the Company reviews the most recent appraisal and if it is over 12 months old will request a new third party appraisal. Depending on the particular circumstances surrounding the loan, including the location of the collateral, the date of the most recent appraisal and the value of the collateral relative to the recorded investment in the loan, management may order an independent appraisal immediately or, in some instances, may elect to perform an internal analysis. Specifically as an example, in situations where the collateral on a nonperforming commercial real estate loan is out of the Company's primary market area, management would typically order an independent appraisal immediately, at the earlier of the date the loan becomes nonperforming or immediately following the determination that the loan is impaired. However, as a second example, on a nonperforming commercial real estate loan where management is familiar with the property and surrounding areas and where the original appraisal value far exceeds the recorded investment in the loan, management may perform an internal analysis whereby the previous appraisal value would be reviewed and adjusted for recent conditions including recent sales of similar properties in the area and any other relevant economic trends. These valuations are reviewed at a minimum on a quarterly basis.

Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At June 30, 2011 and December 31, 2010, substantially all of the total impaired loans were evaluated based on the fair value of the collateral. In accordance with ASC 820, impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3.

Certain assets and liabilities are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an on going basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). The following table presents the assets and liabilities carried on the balance sheet by caption and by level within the valuation hierarchy (as described above) as of June 30, 2011 and December 31, 2010 for which a nonrecurring change in fair value has been recorded during the six months ended June 30, 2011 and twelve months ended December 31, 2010.

	Quoted Market Price in active markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at June 30, 2011
Impaired loans	\$-	\$ 2,921,784	\$ -	\$2,921,784
Other real estate owned	\$-	\$ 659,430	\$ -	\$659,430
Total	\$-	\$ 3,581,214	\$ -	\$3,581,214

	Quoted Market Price in active markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2010
Impaired loans	\$-	\$ 2,266,281	\$ -	\$2,266,281
Other real estate owned	\$-	\$ 659,492	\$ -	\$659,492
Total	\$-	\$ 2,925,773	\$ -	\$2,925,773

The Company has no assets or liabilities whose fair values are measured using level 3 inputs.

Accounting standards require disclosure of fair value information about financial instruments whether or not recognized on the balance sheet, for which it is practicable to estimate fair value. Fair value estimates are made as of a specific point in time based on the characteristics of the financial instruments and the relevant market information. Where available, quoted market prices are used. In other cases, fair values are based on estimates using present value or other valuation techniques. These techniques involve uncertainties and are significantly affected by the assumptions used and the judgments made regarding risk characteristics of various financial instruments, discount rates, prepayments, estimates of future cash flows, future expected loss experience and other factors. Changes in assumptions could significantly affect these estimates. Derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, may or may not be realized in an immediate sale of the instrument.

Under the accounting standards, fair value estimates are based on existing financial instruments without attempting to estimate the value of anticipated future business and the value of the assets and liabilities that are not financial instruments. Accordingly, the aggregate fair value amounts of existing financing instruments do not represent the underlying value of those instruments on the books of the Company.

The following describes the methods and assumptions used by the Company in estimating the fair values of financial instruments:

a. **Cash and due from banks, interest bearing deposits in other banks and federal funds sold**
The carrying value approximates fair value. All mature within 90 days and do not present unanticipated credit concerns.

b. **Investment securities available for sale**
The fair value of investment securities is derived from quoted market prices.

c. **Loans**
The carrying values of variable rate consumer and commercial loans and consumer and commercial loans with remaining maturities of three months or less, approximate fair value. The fair values of fixed rate consumer and commercial loans with maturities greater than three months are determined using a discounted cash flow analysis and assume the rate being offered on these types of loans by the Company at June 30, 2011 and December 31, 2010, approximate market.

The carrying value of mortgage loans held for sale approximates fair value.

For lines of credit, the carrying value approximates fair value.

d. **Deposits**
The estimated fair value of deposits with no stated maturity is equal to the carrying amount. The fair value of time deposits is estimated by discounting contractual cash flows, by applying interest rates currently being offered on the deposit products. The fair value estimates for deposits do not include the benefit that results from the low cost funding provided by the deposit liabilities as compared to the cost of alternative forms of funding (deposit base intangibles).

e. **Short-term borrowings**
The carrying amount approximates fair value due to the short-term nature of these instruments.

The estimated fair values of the Company's financial instruments at June 30, 2011 and December 31, 2010 are as follows:

	June 30, 2011 Carrying Amount	Estimated Fair Value
Cash and due from banks	\$ 5,148,410	\$ 5,148,410
Interest bearing deposits in other banks	22,361,541	22,361,541
Investments available for sale	53,243,002	53,243,002
Loans (1)	215,956,027	217,163,965
Deposits	267,361,846	267,607,973
Short-term borrowings	404,286	404,286

	December 31, 2010	
	Carrying Amount	Estimated Fair Value
Cash and due from banks	\$ 4,697,450	\$ 4,697,450
Interest bearing deposits in other banks	715,231	715,231
Federal funds sold	19,018,104	19,018,104
Investments available for sale	39,379,613	39,379,613
Loans (1)	213,916,674	218,670,423
Deposits	250,436,975	250,750,331
Short-term borrowings	767,497	767,497

(1) Includes mortgage loans to be sold

NOTE 13: Recently Issued Accounting Pronouncements

The following is a summary of recent authoritative pronouncements that could impact the accounting, reporting and/or disclosure of financial information by the Company.

In July 2010, the Receivables topic of the Accounting Standards Codification (“ASC”) was amended by Accounting Standards Update (“ASU”) 2010-20 to require expanded disclosures related to a company’s allowance for credit losses and the credit quality of its financing receivables. The amendments require the allowance disclosures to be provided on a disaggregated basis. The Company is required to include these disclosures in their interim and annual financial statements. See Note 4.

Disclosures about Troubled Debt Restructurings (“TDRs”) required by ASU 2010-20 were deferred by the Financial Accounting Standards Board (“FASB”) in ASU 2011-01 issued in January 2011. In April 2011 FASB issued ASU 2011-02 to assist creditors with their determination of when a restructuring is a TDR. The determination is based on whether the restructuring constitutes a concession and whether the debtor is experiencing financial difficulties as both events must be present. Disclosures related to TDRs under ASU 2010-20 will be effective for reporting periods beginning after June 15, 2011.

In April 2011, the criteria used to determine effective control of transferred assets in the Transfers and Servicing topic of the ASC was amended by ASU 2011-03. The requirement for the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms and the collateral maintenance implementation guidance related to that criterion were removed from the assessment of effective control. The other criteria to assess effective control were not changed. The amendments are effective for the Company beginning January 1, 2012 but are not expected to have a material effect on the financial statements.

ASU 2011-04 was issued in May 2011 to amend the Fair Value Measurement topic of the ASC by clarifying the application of existing fair value measurement and disclosure requirements and by changing particular principles or requirements for measuring fair value or for disclosing information about fair value measurements. The amendments will be effective for the Company beginning January 1, 2012 but are not expected to have a material effect on the financial statements.

The Comprehensive Income topic of the ASC was amended in June 2011. The amendment eliminates the option to present other comprehensive income as a part of the statement of changes in stockholders’ equity. The amendment requires consecutive presentation of the statement of net income and other comprehensive income and requires an entity to present reclassification adjustments from other comprehensive income to net income on the face of the

financial statements. The amendments will be applicable to the Company on January 1, 2012 and will be applied retrospectively.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company's financial position, results of operations or cash flows.

NOTE 14: Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Non-recognized subsequent events are events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date. Management has reviewed events occurring through the date the financial statements were available to be issued and no subsequent events have occurred requiring accrual or disclosure.

ITEM 2
MANAGEMENT'S DISCUSSION AND ANALYSIS
OR PLAN OF OPERATION

Management's discussion and analysis is included to assist shareholders in understanding the Company's financial condition, results of operations, and cash flow. This discussion should be reviewed in conjunction with the consolidated financial statements (unaudited) and notes included in this report and the supplemental financial data appearing throughout this report. Since the primary asset of the Company is its wholly-owned subsidiary, most of the discussion and analysis relates to the Bank.

Management's Discussion and Analysis of Financial Condition and Results of Operations and other portions of this quarterly report contain certain "forward-looking statements" concerning the future operations of the Bank of South Carolina Corporation. Management desires to take advantage of the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1996 and is including this statement for the express purpose of availing the Company of protections of such safe harbor with respect to all "forward-looking statements" contained in this Form 10-Q. The Company has used "forward-looking statements" to describe future plans and strategies including its expectations of the Company's future financial results. The following are cautionary statements. Management's ability to predict results or the effect of future plans or strategies is inherently uncertain. A variety of factors may affect the operations, performance, business strategy and results of the Company including, but not limited to the following:

- Risk from changes in economic, monetary policy, and industry conditions
- Changes in interest rates, shape of the yield curve, deposit rates, the net interest margin and funding sources
- Market risk (including net income at risk analysis and economic value of equity risk analysis) and inflation
 - Risk inherent in making loans including repayment risks and changes in the value of collateral
- Loan growth, the adequacy of the allowance for loan losses, provisions for loan losses, and the assessment of problem loans
 - Level, composition, and re-pricing characteristics of the securities portfolio
 - Deposit growth, change in the mix or type of deposit products and services
 - Continued availability of senior management
 - Technological changes
 - Ability to control expenses
 - Changes in compensation
 - Risks associated with income taxes including potential for adverse adjustments
 - Changes in accounting policies and practices
 - Changes in regulatory actions, including the potential for adverse adjustments

- Recently enacted or proposed legislation
- Current disarray in the financial service industry.

All forward-looking statements in this report are based on information available to the Company as of the date of this report. Although Management believes that the expectations reflected in the forward-looking statements are reasonable, Management cannot guarantee that these expectations will be achieved. The Company will undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made to reflect the occurrence of unanticipated events. In addition, certain statements in future filings by the Company with the SEC, in press releases, and in oral and written statements made by or with the approval of the Company, which are not statements of historical fact, constitute forward looking statements.

Overview

Bank of South Carolina Corporation (the Company) is a financial institution holding company headquartered in Charleston, South Carolina, with \$299.1 million in assets as of June 30, 2011 and net income of \$768,025 and \$1,417,394 for the three and six months ended June 30, 2011. The Company offers a broad range of financial services through its wholly-owned subsidiary, The Bank of South Carolina (the Bank). The Bank is a state-chartered commercial bank which operates principally in the Charleston, Dorchester and Berkeley counties of South Carolina. The Bank's original and current concept is to be a full service financial institution specializing in personal service, responsiveness, and attention to detail to foster long standing relationships.

The following is a discussion of the Company's financial condition as of June 30, 2011 as compared to December 31, 2010 and the results of operations for the three and six months ended June 30, 2011 as compared to the three and six months ended June 30, 2010. The discussion and analysis identifies significant factors that have affected the Company's financial position and operating results and should be read in conjunction with the financial statements and the related notes included in this report.

The Company derives most of its income from interest on loans and investments (interest bearing assets). The primary source of funding for making these loans and investments is the Company's interest and non-interest bearing deposits. One of the key measures of the Company's success is the amount of net interest income, or the difference between the income on its interest earning assets, such as loans and investments, and the expense on its interest bearing liabilities, such as deposits. Another key measure is the spread between the yield the Company earns on these interest bearing assets and the yield the Company pays on its interest-bearing liabilities.

There are risks inherent in all loans; therefore, the Company maintains an allowance for loan losses to absorb estimated losses on existing loans that may become uncollectible. The Company established and maintains this allowance based on a methodology representing the lending environment it operates within. For a detailed discussion on the allowance for loan losses see "Provision for Loan Losses".

The Company's results of operations depend not only on the level of its net interest income from loans and investments, but also on its non-interest income and its operating expenses. Net interest income depends upon the volumes, rates and mix associated with interest earning assets and interest bearing liabilities which result in the net interest spread. The Company's net interest spread for the three and six months ended June 30, 2011 were 3.78% and 3.79%, respectively, compared to 4.11% and 4.14% for the three and six months ended June 30, 2010.

Non-interest income includes fees and other expenses charged to customers. A more detailed discussion of interest income, non-interest income and operating expenses follows.

For six months ended June 30, 2011, the Bank has paid \$855,000 to the Company for dividend payments.

CRITICAL ACCOUNTING POLICIES

The Company has adopted various accounting policies that govern the application principles generally accepted in the United States and with general practices within the banking industry in the preparation of its financial statements. The Company's significant accounting policies are described in the footnotes to its unaudited consolidated financial statements as of June 30, 2011 and its notes included in the consolidated financial statements in its 2010 Annual Report on Form 10-K as filed with the SEC.

Certain accounting policies involve significant judgments and assumptions by the Company that have a material impact on the carrying value of certain assets and liabilities. The Company considers these accounting policies to be critical accounting policies. The judgment and assumptions the Company uses are based on historical experience and other factors, which the Company believes to be reasonable under the circumstances. Because of the number of the judgments and assumptions the Company makes, actual results could differ from these judgments and estimates that could have a material impact on the carrying values of its assets and liabilities and its results of operations.

The Company considers its policies regarding the allowance for loan losses to be its most subjective accounting policy due to the significant degree of Management judgment. The Company has developed what it believes to be appropriate policies and procedures for assessing the adequacy of the allowance for loan losses, recognizing that this process requires a number of assumptions and estimates with respect to its loan portfolio. The Company's assessments may be impacted in future periods by changes in economic conditions, the impact of regulatory examinations and the discovery of information with respect to borrowers which were not known by Management at the time of the issuance of the consolidated financial statements. For additional discussion concerning the Company's allowance for loan losses and related matters, see "Allowance for Loan Losses."

BALANCE SHEET**LOANS**

The Company focuses its lending activities on small and middle market businesses, professionals and individuals in its geographic markets. At June 30, 2011 outstanding loans (plus deferred loan fees of \$31,824) totaled \$212,335,093 which equaled 79.42% of total deposits and 70.99% of total assets. Substantially all loans were to borrowers located in the Company's market areas in the counties of Charleston, Dorchester and Berkeley in South Carolina.

Because lending activities comprise such a significant source of revenue, the Company's main objective is to adhere to sound lending practices. The Loan Committee of the Board of Directors meets monthly to evaluate the adequacy of the Allowance for Loan Losses and to review all loans resulting in credit exposure in excess of \$10,000.

The breakdown of total loans by type and the respective percentage of total loans are as follows:

	June 30, 2011	June 30, 2010	December 31, 2010
Commercial loans	\$52,777,635	\$45,808,932	\$50,601,639
Commercial real estate	112,096,816	106,897,372	108,004,910
Residential mortgage	15,590,884	17,084,580	16,071,839
Consumer loans	4,748,317	5,302,864	5,361,197
Personal banklines	26,908,133	29,170,312	27,734,166
Other	181,484	235,032	234,607
Total	212,303,269	204,499,092	208,008,358
Deferred loan fees (net)	31,824	9,412	17,306

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Allowance for loan losses	(2,854,059)	(3,116,222)	(2,938,588)
Loans, net	\$209,481,034	\$201,392,282	\$205,087,076

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Percentage of Loans	June 30,		December 31,	
	2011	2010	2010	2010
Commercial loans	24.86 %	22.40 %	24.33 %	
Commercial real estate	52.80 %	52.27 %	51.92 %	
Residential mortgage	7.34 %	8.36 %	7.73 %	
Consumer loans	2.24 %	2.59 %	2.58 %	
Personal banklines	12.67 %	14.27 %	13.33 %	
Other	.09 %	.11 %	0.11 %	
Total	100.00 %	100.00 %	100.00 %	

As the result of the recessionary economic conditions which began in the latter half of 2007, the Company experienced a decrease in loan demand in the first quarter of 2011. This trend appears to be improving with an increase in loan demand in the second quarter of 2011 resulting in an increase in outstanding loans as shown in the table above. Loans have increased 3.82% or approximately \$7,804,177 from June 30, 2010 to June 30, 2011.

INVESTMENT SECURITIES AVAILABLE FOR SALE

The Company uses the investment securities portfolio for several purposes. It serves as a vehicle to manage interest rate and prepayment risk, to generate interest and dividend income from investment of funds, to provide liquidity to meet funding requirements, and to provide collateral for pledges on public funds. Investments are classified into three categories (1) Held to Maturity (2) Trading and (3) Available for Sale. Management believes that maintaining its securities in the Available for Sale category provides greater flexibility in the management of the overall investment portfolio. The average yield on investments at June 30, 2011 was 2.45% compared to 3.90% at December 31, 2010. The amortized cost of the investments available for sale at June 30, 2011 and December 31, 2010 and percentage of each category to total investments are as follows:

	INVESTMENT PORTFOLIO	
	June 30, 2011	December 31, 2010
US Treasury Notes	\$ 12,166,711	\$ 9,055,078
Government-Sponsored Enterprises	12,398,216	6,013,897
Municipal Securities	26,954,432	23,913,091
	\$ 51,519,359	\$ 38,982,066
US Treasury Note	23.62 %	23.23 %
Government-Sponsored Enterprises	24.06 %	15.43 %
Municipal Securities	52.32 %	61.34 %
	100.00 %	100.00 %

All investment securities were classified as Available for Sale (debt and equity securities that may be sold under certain conditions), at June 30, 2011 and December 31, 2010. The securities were reported at fair value, with unrealized gains and losses excluded from earnings and reported as a separate component of shareholders' equity, net of income taxes. Unrealized losses on securities due to fluctuations in fair value are recognized when it is determined that an other than temporary decline in value has occurred. Gains or losses on the sale of securities are recognized on a specific identification, trade date basis.

The amortized cost and fair value of investment securities available for sale are summarized as follows as of June 30, 2011 and December 31, 2010:

	JUNE 30, 2011			ESTIMATED FAIR VALUE
	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	
U.S. Treasury Notes	\$ 12,166,711	\$ 165,164	\$ -	\$ 12,331,875
Government-Sponsored Enterprises	12,398,216	36,884	-	12,435,100
Municipal Securities	26,954,432	1,521,615	20	28,476,027
Total	\$ 51,519,359	\$ 1,723,663	\$ 20	\$ 53,243,002

	DECEMBER 31, 2010			ESTIMATED FAIR VALUE
	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	
U.S. Treasury Notes	\$ 9,055,078	\$ 8,784	\$ 40,425	\$ 9,023,437
Government-Sponsored Enterprises	6,013,897	86,648	-	6,100,545
Municipal Securities	23,913,091	577,462	234,922	24,255,631
Total	\$ 38,982,066	\$ 672,894	\$ 275,347	\$ 39,379,613

The amortized cost and estimated fair value of investment securities available for sale at June 30, 2011 and December 31, 2010 by contractual maturity are as follows:

	JUNE 30, 2011	
	AMORTIZED COST	ESTIMATED FAIR VALUE
Due in one year or less	\$ 1,272,137	\$ 1,284,504
Due in one year to five years	29,973,190	30,499,163
Due in five years to ten years	9,491,424	10,191,431
Due in ten years and over	10,782,608	11,267,904
Total	\$ 51,519,359	\$ 53,243,002

	DECEMBER 31, 2010	
	AMORTIZED COST	ESTIMATED FAIR VALUE
Due in one year or less	\$ 9,619,604	\$ 9,719,581
Due in one year to five years	9,465,147	9,608,773
Due in five years to ten years	8,832,440	9,137,645

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Due in ten years and over	11,064,875	10,913,614
Total	\$ 38,982,066	\$ 39,379,613

The amortized cost and estimated fair value of investment securities available for sale at June 30, 2011 and December 31, 2010 are as follows:

JUNE 30, 2011

Description of Securities	Less than 12 months		12 months or longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury Notes	\$-	\$ -	\$-	\$ -	\$-	\$ -
Government-Sponsored Enterprises	-	-	-	-	-	-
Municipal Securities	499,980	20	-	-		