

*Atlantic Central Bankers Bank and
Subsidiary*

Financial Statements

December 31, 2009 and 2008

Atlantic Central Bankers Bank and Subsidiary

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Independent Auditors' Report

To the Board of Directors and Shareholders
Atlantic Central Bankers Bank
Camp Hill, Pennsylvania

We have audited the accompanying consolidated balance sheets of Atlantic Central Bankers Bank and subsidiary as of December 31, 2009 and 2008, and the related consolidated statements of income, shareholders' equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Atlantic Central Bankers Bank and subsidiary as of December 31, 2009 and 2008, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 15 to the consolidated financial statements, the Bank adopted the new accounting guidelines related to accounting for deferred compensation and postretirement aspects of endorsement split-dollar insurance agreements on January 1, 2008.

ParenteBeard LLC

Harrisburg, Pennsylvania
March 16, 2010

Atlantic Central Bankers Bank and Subsidiary

Consolidated Balance Sheets

December 31, 2009 and 2008

	<u>2009</u>	<u>2008</u>
Assets		
(Dollars in Thousands, Except Share Data)		
Cash and due from banks	\$145,759	\$ 81,655
Interest bearing demand deposits	4,076	15,333
Federal funds sold	<u>68,619</u>	<u>30,617</u>
Cash and Cash Equivalents	218,454	127,605
Term federal funds sold	100,000	50,000
Securities available for sale	54,479	41,335
Restricted investment in bank stock	378	363
Loans, net of allowance for loan losses 2009 \$14,061; 2008 \$9,379	276,652	327,635
Premises and equipment, net	3,810	4,144
Accrued interest receivable	1,479	2,073
Cash surrender value of life insurance	13,179	10,635
Foreclosed real estate	4,450	3,357
Other assets	<u>8,806</u>	<u>13,792</u>
Total Assets	<u><u>\$681,687</u></u>	<u><u>\$580,939</u></u>
Liabilities and Shareholders' Equity		
Liabilities		
Deposits:		
Non-interest bearing demand deposits	\$138,469	\$125,936
Time deposits	30,294	4,854
Escrow accounts	<u>7,097</u>	<u>-</u>
Total Deposits	175,860	130,790
Federal funds purchased	447,035	391,999
Dividends payable	119	497
Capital lease obligations	2,328	3,211
Derivative liability	750	1,324
Other liabilities	<u>3,708</u>	<u>3,466</u>
Total Liabilities	<u><u>629,800</u></u>	<u><u>531,287</u></u>
Shareholders' Equity		
Common stock, \$250 par value; 20,000 shares authorized; 12,120 shares issued; 2009 11,929 shares and 2008 11,561 shares outstanding	3,030	3,030
Paid-in capital	9,774	9,192
Retained earnings	39,660	38,086
Treasury stock, at cost, 2009 191 shares and 2008 559	(287)	(839)
Accumulated other comprehensive income (loss)	<u>(290)</u>	<u>183</u>
Total Shareholders' Equity	<u><u>51,887</u></u>	<u><u>49,652</u></u>
Total Liabilities and Shareholders' Equity	<u><u>\$681,687</u></u>	<u><u>\$580,939</u></u>

See notes to consolidated financial statements.

Atlantic Central Bankers Bank and Subsidiary

Consolidated Statements of Income Years Ended December 31, 2009 and 2008

	2009	2008
	(Dollars in Thousands, Except per Share Data)	
Interest and Dividend Income		
Loans, including fees	\$16,989	\$19,794
Securities, taxable	2,203	2,585
Federal funds sold	634	1,030
Other	92	117
Total Interest Income	19,918	23,526
Interest Expense		
Deposits	163	979
Federal funds purchased	1,261	6,277
Other	260	305
Total Interest Expense	1,684	7,561
Net Interest Income	18,234	15,965
Provision for Loan Losses	9,791	5,569
Net Interest Income after Provision for Loan Losses	8,443	10,396
Other Income		
Clearing and analysis fees	2,585	2,471
Agency federal funds fees	261	222
Earnings on cash surrender value of life insurance	391	380
Loss on sale of foreclosed real estate	-	(99)
Sale of BITS membership units	-	100
Gain on sale of securities available for sale	831	18
BITS revenue, net of direct costs	4,053	2,181
Other	38	63
Total Other Income	8,159	5,336
Other Expenses		
Salaries and employee benefits	5,777	5,316
Occupancy and equipment	1,526	1,467
Data processing and servicing fees	2,858	2,228
Professional fees	967	793
Pennsylvania bank shares tax	403	403
(Gains) losses on derivatives	(65)	1,178
FDIC insurance	618	83
Other	2,073	1,226
Total Other Expenses	14,157	12,694
Income before Income Taxes	2,445	3,038
Income Tax Expense	752	1,030
Net Income	\$ 1,693	\$ 2,008
Basic Earnings per Share	\$143.91	\$176.12

See notes to consolidated financial statements.

Atlantic Central Bankers Bank and Subsidiary

Consolidated Statements of Shareholders' Equity

Years Ended December 31, 2009 and 2008

	Common Stock	Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
(Dollars in Thousands, except Per Share Data)						
Balance, January 1, 2008	\$3,030	\$8,682	\$36,841	\$(966)	\$ 49	\$47,636
Cumulative adjustment for change in accounting principle	-	-	(266)	-	-	(266)
Purchase of 255 shares of treasury stock	-	-	-	(383)	-	(383)
Reissuance of 340 shares of treasury stock	-	510	-	510	-	1,020
Comprehensive income:						
Net income	-	-	2,008	-	-	2,008
Other comprehensive income	-	-	-	-	134	134
Total Comprehensive Income						2,142
Dividend declared, \$43 per share	-	-	(497)	-	-	(497)
Balance, December 31, 2008	3,030	9,192	38,086	(839)	183	49,652
Reissuance of 368 shares of treasury stock	-	582	-	552	-	1,134
Comprehensive income:						
Net income	-	-	1,693	-	-	1,693
Other comprehensive loss	-	-	-	-	(473)	(473)
Total Comprehensive Income						1,220
Dividend declared, \$10 per share	-	-	(119)	-	-	(119)
Balance, December 31, 2009	\$3,030	\$9,774	\$39,660	\$(287)	\$(290)	\$51,887

See notes to consolidated financial statements.

Atlantic Central Bankers Bank and Subsidiary

Consolidated Statements of Cash Flows Years Ended December 31, 2009 and 2008

	2009	2008
	(In Thousands)	
Cash Flows from Operating Activities		
Net income	\$ 1,693	\$ 2,008
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of premises and equipment	727	706
Amortization of investment securities	66	8
Provision for loan losses	9,791	5,569
Earnings on cash value of life insurance	(391)	(380)
Deferred income taxes	(1,548)	(1,387)
Net realized gain on sale of securities	(831)	(18)
Net realized (gain) loss on sale of foreclosed real estate	(103)	99
(Increase) decrease in accrued interest receivable	594	(198)
(Increase) decrease in other assets	6,713	(1,838)
Derivatives trading activity	(574)	1,083
Increase in dividends payable and other liabilities	361	260
Net Cash Provided by Operating Activities	16,498	5,912
Cash Flows from Investing Activities		
Increase in term federal funds sold	(50,000)	(50,000)
Activity in available for sale securities:		
Proceeds from maturities, calls and principal repayments	11,176	17,479
Sales	31,316	43,115
Purchases	(55,642)	(31,200)
Net (increase) decrease in loans	39,127	(40,412)
Net increase in restricted stock	(15)	(15)
Purchases of premises and equipment	(190)	(177)
Proceeds from sale of premises and equipment	67	-
Proceeds from sale of foreclosed real estate	1,075	405
Investment in cash value of life insurance	(2,153)	(161)
Net Cash Used in Investing Activities	(25,239)	(60,966)
Cash Flows from Financing Activities		
Net increase in deposits	45,070	12,121
Net increase in federal funds purchased	55,036	103,555
Payment on capital lease obligations	(1,153)	(1,000)
Proceeds from reissuance of treasury stock	1,134	1,020
Payments for purchases of treasury stock	-	(383)
Payment of dividends	(497)	(494)
Net Cash Provided by Financing Activities	99,590	114,819
Net Increase in Cash and Cash Equivalents	90,849	59,765
Cash and Cash Equivalents - Beginning	127,605	67,840
Cash and Cash Equivalents - Ending	\$218,454	\$127,605
Supplementary Cash Flows Information		
Interest paid	\$ 1,641	\$ 7,524
Income taxes paid	2,619	2,954
Called securities not settled	-	6,700
Other real estate acquired in settlement of loans	2,065	2,855
Equipment acquired under capital leases	270	1,377

See notes to consolidated financial statements.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Summary of Significant Accounting Policies

Organization and Nature of Operations

Atlantic Central Bankers Bank (Bank) provides correspondent banking services, both credit and noncredit, to financial institutions in the Mid-Atlantic region of the United States of America. The Bank is subject to regulation and supervision by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Pennsylvania Department of Banking. The Bank's majority-owned subsidiary, ACBB-BITS, LLC (BITS), provides enhanced communication services through a hosted communications platform solely for community financial institutions. BITS is a manager managed limited liability company and the Bank controls its operations and, accordingly, the results of operations and financial condition of BITS are included in these consolidated financial statements. At December 31, 2009 and 2008, BITS was owned primarily by the Bank, however, operational plans project the Bank's ownership to be reduced in the future, although never below a voting majority.

The Bank participates in commercial and commercial real estate loans with other financial institutions throughout the Mid-Atlantic Region of the United States of America and makes direct loans to financial institutions and officers and directors of financial institutions. In addition, the Bank accepts deposits and purchases federal funds from financial institutions. The Bank performs various services for its customers in an agency capacity and, therefore, these items are excluded from the Bank's financial statements since they do not constitute assets of the Bank. The Bank had agency federal funds of \$232,885,000 and \$609,668,000 as of December 31, 2009 and 2008, respectively, that are excluded from these financial statements.

Principles of Consolidation

The consolidated financial statements include the accounts of Atlantic Central Bankers Bank and its majority-owned subsidiary, ACBB-BITS, LLC. All intercompany accounts and transactions are eliminated in the consolidation.

As the Bank guarantees BITS' borrowings, given their accumulated deficit and net loss to date, BITS balance sheet and results of operations are presented on a consolidated basis with no minority interest presentation.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the evaluation of other than temporary impairment of securities, and the valuation of deferred tax assets.

Significant Group Concentrations of Credit Risk

Most of the Bank's activities are with customers located within the Mid-Atlantic Region of the United States of America. The Bank participates in commercial and commercial real estate loans with other financial institutions throughout the Mid-Atlantic Region and makes direct loans to officers and directors of financial institutions. The loan portfolio is generally collateralized by assets of the borrower. A substantial portion of the Bank's loan portfolio is concentrated in the real estate industry. Therefore, its debtors' ability to honor their contracts is dependent upon the real estate sector of the economy. The concentration of credit by type of loan is set forth in Note 4.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Summary of Significant Accounting Policies (Continued)

Presentation of Cash Flows

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks and federal funds sold, all of which have initial maturities of ninety days or less. Generally, federal funds are purchased or sold for one day periods, but for those that exceed one day, are presented as term federal funds sold on the consolidated balance sheet.

Securities

Management determines the appropriate classification of debt securities at the time of purchase and re-evaluates such designation as of each balance sheet date.

Securities classified as available for sale are those securities that the Bank intends to hold for an indefinite period of time but not necessarily to maturity. Securities available for sale are carried at fair value. Any decision to sell a security classified as available for sale would be based on various factors, including significant movement in interest rates, changes in maturity mix of the Bank's assets and liabilities, liquidity needs, regulatory capital considerations and other similar factors. Unrealized gains and losses are reported as increases or decreases in other comprehensive income (loss). Realized gains or losses, determined on the basis of the cost of the specific securities sold, are included in earnings. Premiums and discounts are recognized in interest income using the interest method over the terms of the securities.

Effective April 1, 2009, the Bank adopted new accounting guidance related to recognition and presentation of other-than-temporary impairment. This recent accounting guidance amends the recognition guidance for other-than-temporary impairments of debt securities and expands the financial statement disclosures for other-than-temporary impairment losses on debt and equity securities. The recent guidance replaced the "intent and ability" indication in current guidance by specifying that (a) if a company does not have the intent to sell a debt security prior to recovery and (b) it is more likely than not that it will not have to sell the debt security prior to recovery, the security would not be considered other-than-temporarily impaired unless there is a credit loss. When an entity does not intend to sell the security, and it is more likely than not, the entity will not have to sell the security before the recovery of its cost basis, it will recognize the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income. The Bank has not recognized any other-than-temporary impairment losses in the years ended December 31, 2009 or 2008.

Restricted Investment in Bank Stock

The required investment in Federal Reserve Bank stock is carried at cost.

Loans

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at their outstanding unpaid principal balances and any deferred fees or costs, net of an allowance for loan losses. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the yield (interest income) of the related loans. The Bank is generally amortizing these amounts over the contractual life of the loan.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Summary of Significant Accounting Policies (Continued)

Loans (Continued)

The accrual of interest is discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectibility of principal or interest, even though the loan is currently performing. Past due status is based on the contractual terms of the loan. A loan may remain on accrual status if it is in the process of collection and is either guaranteed or well secured. When a loan is placed on nonaccrual status, unpaid interest credited to income in the current year is reversed and unpaid interest accrued in prior years is charged against the allowance for loan losses. Payments received on nonaccrual loans generally is either applied against principal or reported as interest income, according to management's judgment as to the collectibility of principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time and the ultimate collectibility of the total contractual principal and interest is no longer in doubt.

Allowance for Loan Losses

The allowance for loan losses is established through provisions for loan losses charged against income. Loans deemed to be uncollectible are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is maintained at a level considered adequate to provide for losses that can be reasonably anticipated. Management's periodic evaluation of the adequacy of the allowance is based on known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change.

The allowance consists of specific, general, and unallocated components. The specific component relates to loans that are classified as either doubtful, substandard, or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

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

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Summary of Significant Accounting Policies (Continued)

Transfers of Financial Assets

Transfers of financial assets, including loan and loan participation sales, are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Bank, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Foreclosed Real Estate

Foreclosed real estate is comprised of property acquired through a foreclosure proceeding or an acceptance of a deed in lieu of foreclosure. Balances are initially reflected at the estimated fair value less any estimated disposition costs, with subsequent adjustments made to reflect further declines in value. Any loss upon disposition of the property and holding costs, prior thereto, are charged against income.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed on the straight-line method over the estimated useful lives of the related assets. The estimated useful lives of the building and improvements range from 10 to 30 years, from 3 to 10 years for furniture and equipment, and 10 years for enhanced communication services equipment.

Cash Surrender Value of Life Insurance

Cash surrender value of life insurance is carried at its net cash surrender value as determined by the insurance companies. The value represents the amount of premiums invested and earnings thereon. Premiums for purchases of life insurance with a cash surrender value are capitalized. Earnings on the cash surrender value of life insurance are included in other income while expenses are recorded as a component of other expenses in the consolidated statements of income.

Derivative Financial Instruments

Derivative financial instruments are recognized as assets and liabilities on the balance sheet and measured at fair value.

For asset/liability purposes, the Bank uses interest rate swap agreements to hedge various exposures or to modify interest rate characteristics of various balance sheet accounts. Interest rate swaps are contracts in which a series of interest rate flows are exchanged over a prescribed period. The notional amount on which the interest payments are based is not exchanged. The swap agreement is a derivative instrument that converts a portion of the Bank's variable-rate debt to a fixed rate (cash flow hedge). The effective portion of the gain or loss on a derivative designated and qualifying as a cash flow hedge instrument is initially reported as a component of other comprehensive income and subsequently reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. The ineffective portion of the gain or loss on the derivative instrument is recognized currently in earnings.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Summary of Significant Accounting Policies (Continued)

Derivative Financial Instruments (Continued)

Interest rate derivative financial instruments receive hedge accounting treatment only if they are designated as a hedge and are expected to be, and are, effective in substantially reducing interest rate risk arising from the assets and liabilities identified as exposing the Bank to risk. Those derivative financial instruments that do not meet specified hedging criteria would be recorded at fair value with changes in fair value recorded in income. If the periodic assessment indicates the derivative no longer provides an effective hedge, the derivative contracts would be closed out and settled, or classified as trading activity.

Cash flows resulting from the derivative financial instruments that are accounted for as hedges of assets and liabilities are classified in the statement of cash flows in the same category as the cash flows of the items being hedged.

Marketing and Promotion Expense

The Bank follows the policy of charging the costs of marketing and promotion to expense as incurred.

Income Taxes

Deferred income taxes are provided on the liability method whereby deferred tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and net operating loss carryforwards and their tax basis. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is uncertain if the deferred tax asset will be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Effective January 1, 2009, the Bank adopted recent accounting guidance related to accounting for uncertainty in income taxes, which sets out a consistent framework to determine the appropriate level of tax reserves to maintain for uncertain tax positions. The Bank had no material unrecognized tax benefits or accrued interest and penalties as of December 31, 2009 and 2008. The Bank's policy is to account for interest as a component of interest and penalties as a component of other expense. With few exceptions, the Bank is no longer subject to U.S. federal or state income tax authorities for years before 2006.

Share Based Compensation

The Bank accounts for its share based compensation under Financial Accounting Standards Board ("FASB") FASB ASC 718-10 (prior authoritative literature: FASB Statement No. 123(R), *Share-Based Payments*). Under this method, the share-based compensation cost includes compensation cost for all share-based payments granted based on the estimated grant date fair value. Compensation cost is recognized ratably using the straight-line attribution method over the expected vesting period or to the retirement eligibility date, if less than the vesting period when vesting is not contingent upon any future performance.

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities and cash flow hedges, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 1 - Summary of Significant Accounting Policies (Continued)

Common Stock Ownership

Ownership of the Bank's common stock is limited to other depository institutions in the Continental United States. The number of shares for which an investor may subscribe is limited to 10% of the investor's capital and surplus. The maximum number of shares that any investor may vote is limited to 4.99% of the issued and outstanding shares of the Bank.

Treasury Stock

Purchases of shares are recorded at cost as a reduction of shareholders' equity. Reissuances of shares are recorded using the first-in, first-out method. Differences between the reissuance price and cost are recorded as changes in paid-in capital.

Revenue Recognition

BITS recognizes Enhanced Communications Services revenue based upon customer usage of the network and facilities as contracted. Generally these services are billed monthly and are recognized in the month the fees are earned. Installation revenue, including hardware and installation fees, is recognized when the equipment has been installed in accordance with contracted specifications and ready for customer use.

Earnings per Share

The Bank has a simple capital structure. Basic earnings per share represents net income divided by the weighted average number of common shares outstanding of 11,764 and 11,401 for the years ended December 31, 2009 and 2008, respectively.

Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Bank has entered into off-balance sheet financial instruments consisting of commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the balance sheet when they are funded.

Reclassifications

Certain amounts in the 2008 consolidated financial statements have been reclassified to conform to the 2009 presentation. Such reclassifications had no impact on net income.

Subsequent Events

The Bank has evaluated events and transactions occurring subsequent to the balance sheet date of December 31, 2009 for items that should potentially be recognized or disclosed in these financial statements. The evaluation was conducted through March 16, 2010, the date these financial statements were available to be issued.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 2 - Restrictions on Cash and Due from Banks

In return for service obtained through correspondent banks, the Bank is required to maintain noninterest bearing cash balances in certain correspondent banks. At December 31, 2009 and 2008, the Federal Reserve Bank required the Bank to maintain an average balance of approximately \$32,182,000 and \$10,733,000, respectively. In addition, the Bank was required to maintain a \$1,500,000 interest-bearing deposit with its counterparty in connection with the Bank's derivatives activities.

Note 3 - Securities Available for Sale

Amortized cost and fair value at December 31 were as follows:

	2009			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
		(In Thousands)		
U. S. Treasury	\$18,488	\$ 96	\$ -	\$18,584
U. S. Government agencies	15,000	-	(296)	14,704
Mortgage-backed securities:				
U.S. Government sponsored enterprises (GSE)-residential	20,529	68	(74)	20,523
Private label residential	712	-	(44)	668
	<u>\$54,729</u>	<u>\$164</u>	<u>\$(414)</u>	<u>\$54,479</u>
		2008		
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(In Thousands)		
U. S. Treasury	\$ 9,000	\$188	\$ -	\$ 9,188
U. S. Government agencies	20,009	222	-	20,231
Mortgage-backed securities:				
GSE-residential	10,802	155	-	10,957
Private label residential	1,004	-	(45)	959
	<u>\$40,815</u>	<u>\$565</u>	<u>\$(45)</u>	<u>\$41,335</u>

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 3 - Securities Available for Sale (Continued)

The following tables reflect temporary impairment in the investment portfolio, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position for the years ended December 31, 2009 and 2008:

	2009					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In Thousands)					
U.S. Government agencies	\$14,704	(\$296)	\$ -	\$ -	\$14,704	(\$296)
Mortgage-backed securities:						
GSE residential	12,169	(74)	-	-	12,169	(74)
Private label residential	-	-	668	(44)	668	(44)
	<u>\$26,873</u>	<u>\$(370)</u>	<u>\$668</u>	<u>\$(44)</u>	<u>\$27,541</u>	<u>\$(414)</u>
	2008					
Mortgage-backed securities:						
Private label residential	<u>\$ -</u>	<u>\$ -</u>	<u>\$959</u>	<u>\$(45)</u>	<u>\$959</u>	<u>\$(45)</u>

Gross unrealized losses of \$414,000 at December 31, 2009 pertain to ten securities. Management believes that unrealized losses on debt securities were primarily the result of changes in market interest rates. No credit risk issues have been identified that cause management to believe the declines in fair value are other than temporary. Management has the intent and ability to hold impaired securities until maturity or recovery in value, and does not anticipate that it will have to sell the securities prior to recovery.

Amortized cost and fair value at December 31, 2009 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay with or without penalties.

	2009	
	Amortized Cost	Fair Value
	(In Thousands)	
Due in one year or less	\$ 4,500	\$ 4,545
Due after one year through five years	13,988	14,039
Due after five years through ten years	5,000	4,861
Due after ten years	10,000	9,843
Mortgage-backed securities	<u>21,241</u>	<u>21,191</u>
	<u>\$54,729</u>	<u>\$54,479</u>

The Bank had gross realized gains on securities of \$831,277 in 2009 and \$18,000 in 2008.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 4 - Loans

The composition of loans receivable at December 31, 2009 and 2008 is as follows:

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Commercial and industrial	\$ 4,793	\$ 8,359
Tax exempt	2,000	5,294
Personal	16,808	27,938
Real estate:		
Construction and land development	52,402	65,159
Residential	18,116	13,806
Commercial	165,423	196,266
All other	31,503	20,495
Total Loans	291,045	337,317
Less:		
Deferred loan fees	332	303
Allowance for loan losses	14,061	9,379
Net Loans	<u>\$276,652</u>	<u>\$327,635</u>

The changes in the allowance for loan losses for the years ended December 31, 2009 and 2008 are as follows:

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Balance, beginning	\$ 9,379	\$6,543
Provision for loan losses	9,791	5,569
Loans charged-off	(5,326)	(2,733)
Recoveries	217	-
Balance, ending	<u>\$14,061</u>	<u>\$9,379</u>

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 4 - Loans (Continued)

The following is a summary of information pertaining to impaired and non-accrual loans at and for the years ended December 31, 2009 and 2008:

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Impaired loans without a valuation allowance	\$ 2,196	\$ 4,829
Impaired loans with a valuation allowance	<u>16,388</u>	<u>11,212</u>
Total Impaired Loans	<u>18,584</u>	<u>16,041</u>
Valuation allowance related to impaired loans	<u>\$ 3,785</u>	<u>\$ 2,352</u>
Average investment in impaired loans	<u>\$19,906</u>	<u>\$10,153</u>
Interest income earned but not recognized on impaired loans	<u>\$ 1,070</u>	<u>\$ 656</u>
Interest income recognized on impaired loans	<u>\$ 579</u>	<u>\$ 692</u>
Total non-accrual loans	<u>\$17,105</u>	<u>\$13,129</u>

Note 5 - Premises and Equipment

The components of premises and equipment at December 31, 2009 and 2008 are as follows:

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Land	\$ 125	\$ 125
Buildings and improvements	1,402	1,393
Furniture, fixtures and equipment	2,580	2,374
Enhanced communication services equipment	<u>3,512</u>	<u>3,336</u>
	7,619	7,228
Accumulated depreciation	<u>(3,809)</u>	<u>(3,084)</u>
	<u>\$3,810</u>	<u>\$4,144</u>

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 6 - Deposits

In return for services provided by the Bank, member banks are required to maintain noninterest bearing demand deposits at the Bank. In lieu of paying interest on these demand deposit accounts, the Bank provides an earnings credit to member banks to reduce the overall expense to member banks for using the Bank's services. Due to the nature of the Bank's operations, it is not uncommon for the member banks demand deposit account balances to exceed \$100,000. At December 31, 2009 and 2008, almost all deposits were for \$100,000 or more.

At December 31, 2009, the scheduled maturities of certificates of deposit are as follows (in thousands):

Years ending December 31:	
2010	\$ 8,426
2011	10,225
2012	<u>11,643</u>
	<u>\$30,294</u>

Note 7 - Federal Funds

Federal funds are reported on a gross basis. Federal funds sold are stated as assets and federal funds purchased are stated as liabilities. Federal funds purchased had interest rates ranging from 0.32% to 0.44% throughout the year ended December 31, 2009, and at December 31, 2009 the federal funds purchase rate was 0.32%. Federal funds purchased mature daily.

Note 8 - Borrowings

The Bank has a \$104,401,000 line of credit available through the Federal Reserve Bank (FRB) secured by a blanket floating lien on all qualifying loans. At December 31, 2009 and 2008, the Bank had no balance outstanding with the FRB on this line of credit. At December 31, 2009, the Bank also had \$34,630,000 available under line of credit agreements with other financial institutions. There were no advances outstanding on these lines at December 31, 2009 and 2008.

Note 9 - Derivative Instruments and Hedging Activities

The Bank uses short-term variable rate federal funds purchased as a source of funds for the Bank's lending and investment activities and other general business purposes. These funds expose the Bank to variability in interest payments due to changes in interest rates. If interest rates increase, interest expense increases. Conversely, if interest rates decrease, interest expense decreases. Management believed it was prudent to limit the variability of a portion of its interest payments and, therefore, initially hedged a portion of its variable-rate interest payments. To meet this objective, management entered into a stand alone interest rate swap on September 8, 2008 whereby the Bank received variable interest rate payments (federal funds effective rate as published by the Federal Reserve) and made fixed interest rate payments (3.51%) during the contract period. The interest rate swap's termination date is September 8, 2013. The interest rate swap calls for quarterly settlements with the counterparty.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 9 - Derivative Instruments and Hedging Activities (Continued)

An interest rate swap agreement derives its value from the underlying interest rates, and involves both credit and market risk. An interest rate swap's notional amount is the amount in which calculations, payments, and the value of the derivative is based, and does not represent direct credit exposure. The direct credit exposure is limited to the net difference between the calculated amounts to be received and paid, if any. Such difference, which represents the fair value of the derivative instrument, is reflected in the Bank's balance sheet as a liability at December 31, 2009 and 2008.

The Bank is exposed to credit-related losses in the event of nonperformance by the counterparties to these agreements. The Bank controls the credit risk of its financial contracts through credit approvals, limits and monitoring procedures, and does not expect any counterparties to fail their obligations. The counterparty is also exposed to credit risk with the Bank, and to mitigate its risk, requires collateral sufficient to cover any unrealized losses on the derivatives be held at the counterparty bank.

Initially, when the Bank entered into its interest rate swap, it was designated as a cash flow hedge and was deemed to be effective. However, due to market conditions in the financial services industry in the fourth quarter, the Bank introduced a floor interest rate on its federal funds purchased to remain competitive with offerings from competitors. Upon introduction of the floor on October 10, 2008, the Bank's management concluded that the interest rate swap was no longer effective, and no longer qualified for hedge accounting treatment. On this date, the unrealized loss on the interest rate swap was \$253,000 and will be amortized over the remaining life of the instrument. Amortization of the unrealized loss totaled \$51,000 and \$12,000 for the years ended December 31, 2009 and 2008, respectively. The cash settlement that the Bank paid under the fixed rate portion of the swap, that exceeded the amounts to be received from the counterparty on the variable rate portion during the effective hedge period in 2008, totaled \$25,000, and is included in interest expense in the income statement.

Once the interest rate swap was no longer designated as an effective hedge, changes in fair value are recorded in noninterest expense, and totaled (\$65,000) and \$1,178,000 for the years ended December 31, 2009 and 2008, respectively. The cash settlement that the Bank paid to the counterparty after the swap was deemed to no longer be effective totaled \$509,000 and \$98,000 for the years ended December 31, 2009 and 2008, respectively. The fair value of this trading instrument at December 31, 2009 and 2008 is a liability of \$750,000 and \$1,324,000, respectively, and is included in liabilities.

Note 10 - Lease Commitments

BITS has entered into operating leases for its office and secured operating space for its Enhanced Communications Services equipment. The leases have terms of twelve to sixty-two months. The Bank is a guarantor for BITS on these leases. Operating lease expense totaled \$450,000 and \$410,000 for 2009 and 2008, respectively.

Long-term lease transactions relating to the financing of equipment and other assets are accounted for as capital leases. Capital lease obligations reflect future lease payments, less an interest amount implicit in the lease.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 10 - Lease Commitments (Continued)

At December 31, 2009, minimum future lease obligations under operating and captive lease obligations are as follows:

	<u>Operating Lease Obligations</u>	<u>Capital Lease Obligations</u>
	(In Thousands)	
Years ended December 31:		
2010	\$414	\$1,381
2011	310	681
2012	55	309
2013	17	134
2014	-	46
	<u>\$796</u>	<u>2,551</u>
Amounts representing interest		<u>(223)</u>
Capital Lease Obligations		<u>\$2,328</u>

Note 11 - Income Taxes

Allocation of income tax expense is as follows for the years ended December 31:

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Current	\$2,300	\$2,417
Deferred	<u>(1,548)</u>	<u>(1,387)</u>
	<u>\$ 752</u>	<u>\$1,030</u>

The components of the federal deferred tax asset, included in other assets, at December 31 are as follows:

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Deferred tax assets:		
Allowance for loan losses	\$4,666	\$3,041
Employee benefit plans	881	789
Realized losses on derivative contract	202	380
Investment in subsidiary	-	91
Foreclosed real estate valuation allowance	108	-
Unrealized losses on derivative contract	64	82
Net unrealized losses on securities available for sale	<u>85</u>	<u>-</u>
	<u>6,006</u>	<u>4,383</u>

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 11 - Income Taxes (Continued)

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Deferred tax liabilities:		
Depreciation	\$ 23	\$ 20
Investment in subsidiary	5	-
Net unrealized gains on securities available for sale	-	177
	<u>28</u>	<u>197</u>
 Net Deferred Assets	 <u><u>\$5,978</u></u>	 <u><u>\$4,186</u></u>

Note 12 - Transactions with Executive Officers, Directors and Principal Stockholders

The Bank has had, and may be expected to have in the future, transactions in the ordinary course of business with its directors, their immediate families and their affiliated banks (commonly referred to as related parties), on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with others. Changes in these related-party loans were as follows:

	<u>2009</u>
	(In Thousands)
Balance, January 1	\$4,913
Additions	3,115
Reductions	<u>(1,638)</u>
 Balance, December 31	 <u><u>\$6,390</u></u>

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 13 - Comprehensive Income

The components of other comprehensive income (loss) for the years ended December 31 are as follows:

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Unrealized holding gains on available for sale of securities	\$ 63	\$463
Reclassification adjustment for gains realized in income	<u>(831)</u>	<u>(18)</u>
Net Unrealized Gains (Losses)	(768)	445
Tax effect	<u>262</u>	<u>(151)</u>
Net of Tax Amount	(506)	294
Change in fair value of derivatives used for cash flow hedges until it no longer qualified as a hedge	-	(254)
Reclassification adjustment for amortization realized in income	<u>51</u>	<u>12</u>
	51	(242)
Tax effect	<u>(18)</u>	<u>82</u>
Net of Tax Amount	33	(160)
	<u>\$(473)</u>	<u>\$134</u>

The components of accumulated other comprehensive income (loss), included in shareholders' equity, are as follows at December 31:

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Net unrealized gains (losses) on securities available for sale	\$ (250)	\$520
Tax effect	<u>85</u>	<u>(177)</u>
Net of Tax Amount	(165)	343
Net unrealized loss on derivatives initially used for cash flow hedge	(189)	(242)
Tax effect	<u>64</u>	<u>82</u>
Net of Tax Amount	(125)	(160)
	<u>\$(290)</u>	<u>\$183</u>

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 14 - Financial Instruments with Off-Balance Sheet Risk

The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include personal or commercial real estate, accounts receivable, inventory and equipment.

Stand-by letters of credit written are conditional commitments by the Bank to guarantee the performance of a customer to a third party. The majority of these stand-by letters of credit expire within twelve months. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The amount of the liability for guarantees under standby letters of credit as of December 31, 2009 and 2008 is not material.

The following financial instruments were outstanding whose contract amounts represent credit risk at December 31:

	Contract Amount	
	2009	2008
	(In Thousands)	
Commitments to grant loans	\$12,021	\$10,140
Unfunded commitments under lines of credit and construction agreements	41,361	60,017
Standby letters of credit	4,331	5,740
	<u>\$57,713</u>	<u>\$75,897</u>

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 15 - Employee Benefit Plans

The Bank makes contributions to Simplified Employee Pension plans for the benefit of eligible employees. The Bank's contributions are determined annually by the Board of Directors, subject to legal restrictions that apply to this type of retirement plan. The Bank's contributions totaled \$269,000 and \$260,000 for the years ended December 31, 2009 and 2008, respectively.

The Bank maintains an arrangement for supplemental compensation (the Supplemental Plan) for certain of its executive officers (Executives). The Supplemental Plan provides that the Bank and the Executives share in the rights to the death benefits of bank owned split-dollar life insurance policies (BOLI Policies). The amount of the BOLI Policies has been calculated so that the projected increases in their cash surrender value will partially offset the Bank's expense related to the Supplemental Plan. The Supplemental Plan is designed to provide certain Executives, upon attaining the normal retirement age, as defined within the Supplemental Plan, with projected annual distributions.

The amount of the benefit obligation is increased or decreased each year based on the service cost, interest cost and benefits paid by the Supplemental Plan. The expense associated with the Supplemental Plan was \$434,000 and \$227,000 for the years ended December 31, 2009 and 2008, respectively. The benefit obligation associated with the Supplemental Plan was \$2,737,000 and \$2,467,000 at December 31, 2009 and 2008, respectively.

On January 1, 2008, the Bank adopted FASB ASC 715-60 (prior authoritative literature: Emerging Issues Task Force 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split Dollar Life Insurance Arrangements*). FASB ASC 715-60 requires recognition of a liability for postretirement benefits provided through an endorsed split-dollar life insurance agreement. As a result of recording this liability, shareholders' equity was reduced by \$266,000 as an adjustment to retained earnings as of the adoption date.

Note 16 - Regulatory Matters

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets, and of Tier 1 capital to average assets. Management believes, as of December 31, 2009 and 2008, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2009, the most recent notification from the Federal Deposit Insurance Corporation (FDIC) categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following tables. There are no conditions or events since the notification that Management believes to have changed the Bank's category.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 16 - Regulatory Matters (Continued)

The Bank's actual capital amounts and ratios at December 31, 2009 and 2008 are presented below:

	Actual		For Capital Adequacy Purposes		To be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollar Amounts in Thousands)						
2009:						
Total capital (to risk-weighted assets)	\$56,856	15.58%	≥\$29,194	≥8.0%	≥\$36,492	≥10.0%
Tier 1 capital (to risk-weighted assets)	52,177	14.30	≥14,597	≥4.0	≥21,895	≥ 6.0
Tier 1 capital (to average assets)	52,177	7.26	≥28,762	≥4.0	≥35,952	≥ 5.0
2008:						
Total capital (to risk-weighted assets)	\$54,594	13.45%	≥\$32,466	≥8.0%	≥\$40,583	≥10.0%
Tier 1 capital (to risk-weighted assets)	49,469	12.19	≥16,233	≥4.0	≥24,350	≥ 6.0
Tier 1 capital (to average assets)	49,469	9.33	≥21,203	≥4.0	≥26,504	≥ 5.0

The Bank is subject to certain restrictions on the amount of dividends that it may declare due to regulatory considerations, including maintaining the capital ratios referenced above.

Note 17 - Fair Value Measurements

Management uses its best judgment in estimating the fair value of the Bank's financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts the Bank could have realized in a sales transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective year-ends and have not been re-evaluated or updated for purposes of these financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported at each year-end.

The Bank follows the fair value measurements guidance established by the Financial Accounting Standards Board (FASB) in 2006, as amended. This guidance defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. It applies to other accounting pronouncements that require or permit fair value measurements.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 17 - Fair Value Measurements (Continued)

Fair value is defined as the price that would be received to sell the asset or transfer the liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. Additional guidance is provided in determining fair value when the volume and level of activity for the asset or liability has significantly decreased, including guidance on identifying circumstances when a transaction may not be considered orderly.

A reporting entity should determine whether there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity for the asset or liability. When the reporting entity concludes there has been a significant decrease in the volume and level of activity for the asset or liability, further analysis of the information from that market is needed and significant adjustments to the related prices may be necessary to estimate fair value.

A reporting entity must determine if the decrease in the volume and level of activity for the asset or liability, suggest the transactions may not be orderly. In those situations, the entity must evaluate the weight of the evidence to determine whether the transaction is orderly, considering the circumstances that indicate that a transaction is not orderly. A transaction price that is not associated with an orderly transaction is given little, if any, weight when estimating fair value.

The guidance establishes a fair value hierarchy that prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2: Quoted prices in markets that are not active, or inputs that are observable either directly or indirectly, for substantially the full term of the asset or liability.

Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported with little or no market activity).

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

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 17 - Fair Value Measurements (Continued)

For financial assets and liabilities measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2009 and 2008 are as follows:

Description	Carrying Value	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
		(In Thousands)		
December 31, 2009:				
Securities available for sale	\$54,479	\$18,584	\$35,895	\$ -
Derivative liability	750	-	-	750
December 31, 2008:				
Securities available for sale	\$41,335	\$ 9,188	\$32,147	\$ -
Derivative liability	1,324	-	-	1,324

The following table presents a reconciliation of the derivative liability measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended December 31, 2009:

	2009
	(In Thousands)
Beginning balance, January 1	\$1,324
Total losses (realized/unrealized):	
Included in noninterest income	(65)
Settlements	(509)
Ending balance, December 31	\$ 750

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 17 - Fair Value Measurements (Continued)

For financial assets measured at fair value on a nonrecurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2009 and 2008 are as follows:

Description	Carrying Value	(Level 1)	(Level 2)	(Level 3)
		Quoted Prices in Active Markets for Identical Assets	Significant Other Observable Inputs	Significant Unobservable Inputs
(In Thousands)				
December 31, 2009:				
Impaired loans	\$12,603	\$ -	\$ -	\$12,603
Real estate owned	2,722	-	-	2,722
	<u>\$15,325</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$15,325</u>
December 31, 2008:				
Impaired loans	\$ 8,860	\$ -	\$ -	\$ 8,860

The following information should not be interpreted as an estimate of the fair value of the entire Bank since a fair value calculation is only provided for a limited portion of the Bank's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Bank's disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair values of the Bank's financial instruments at December 31, 2009 and 2008:

Cash and Cash Equivalents (Carried at Cost)

The carrying amounts reported in the balance sheet for cash and short-term instruments approximate those assets' fair values.

Term Federal Funds Sold (Carried at Cost)

The carrying amounts of term federal funds approximate their fair values.

Securities Available for Sale (Carried at Fair Value)

The fair value of securities available for sale are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or matrix pricing (Level 2), which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted prices.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 17 - Fair Value Measurements (Continued)

Loans Receivable (Carried at Cost)

The fair values of loans are estimated using discounted cash flow analyses, using market rates at the balance sheet date that reflect the credit and interest rate-risk inherent in the loans. Projected future cash flows are calculated based upon contractual maturity or call dates, projected repayments and prepayments of principal. Generally, for variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values.

Impaired Loans (Generally Carried at Fair Value)

Impaired loans are those that are accounted for under FASB ASC 310-10-35 (prior authoritative literature: FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan*), in which the Bank has measured impairment generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements. At December 31, 2009, the fair value consists of the loan balances of \$16,388,000, net of valuation allowances of \$3,785,000. Additional provisions for loan losses of \$2,030,000 were recorded during 2009. At December 31, 2008, the fair value consists of loan balances of \$11,212,000, net of valuation allowances of \$2,352,000. Additional provisions for loan losses of \$2,352,000 were recorded during 2008.

Restricted Investment in Bank Stock (Carried at Cost)

The carrying amount of restricted investment in bank stock approximates fair value, and considers the limited marketability of such securities.

Accrued Interest Receivable and Payable (Carried at Cost)

The carrying amount of accrued interest receivable and accrued interest payable approximates its fair value.

Foreclosed Real Estate (Generally Carried at Lower of Cost or Fair Value)

Foreclosed real estate is adjusted to fair value less costs to dispose upon transfer of a loan to foreclosed real estate. Subsequently, foreclosed real estate is carried at the lower of carrying value or fair value less costs to dispose. Fair value is generally based on current appraisals, comparable sales, and other estimates of value principally obtained from third parties. However, management considers other recent developments that could result in adjustments to collateral value and, as such, are classified as Level 3 within the fair value hierarchy. The fair value of foreclosed real estate consists of balances of \$3,040,000, net of a valuation reserve of \$318,000. Provisions for foreclosed real estate losses were \$318,000 during 2009.

Deposit Liabilities (Carried at Cost)

The fair values disclosed for non-interest bearing demand deposits are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amounts). Fair values for fixed-rate time deposits are estimated using a discounted cash flow calculation that applies interest rates currently being offered in the market on time deposits to a schedule of aggregated expected monthly maturities on time deposits.

Federal Funds Purchased (Carried at Cost)

The carrying amounts of federal funds purchased approximate their fair values.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 17 - Fair Value Measurements (Continued)

Derivative Liability (Carried at Fair Value)

Fair values for the derivative liability, consisting of an interest rate swap, are based upon the amounts required to settle the contract in the market, factoring in the amount of collateral the Bank is required to hold with the counterparty.

Off-Balance Sheet Financial Instruments (Disclosed at Cost)

Fair values for the Bank's off-balance sheet financial instruments (lending commitments and letters of credit) are based on fees currently charged in the market to enter into similar agreements, taking into account, the remaining terms of the agreements and the counterparties' credit standing.

The estimated fair values of the Bank's financial instruments were as follows at December 31, 2009 and 2008:

	2009		2008	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets:				
Cash and cash equivalents	\$218,454	\$218,454	\$127,605	\$127,605
Term federal funds sold	100,000	100,008	50,000	49,815
Investment securities	54,479	54,479	41,335	41,335
Loans, less allowance for loan losses	276,652	279,741	327,635	332,997
Accrued interest receivable	1,479	1,479	2,073	2,073
Restricted investment in bank stock	378	378	363	363
Financial liabilities:				
Non-interest bearing demand deposits	138,469	138,469	125,936	125,936
Time deposits	30,294	30,542	4,854	4,856
Escrow accounts	7,097	7,097	-	-
Federal funds purchased	447,035	447,035	391,999	391,999
Accrued interest payable	88	88	45	45
Capital lease obligations	2,328	2,615	3,211	3,654
Derivative liability	750	750	1,324	1,324
Off-balance sheet instruments	-	-	-	-

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 18 - Subsidiary Only Financial Information

The following represents ACBB-BITS financial information as of or for the year ended December 31:

Balance Sheets

Assets	2009	2008
	(In Thousands)	
Cash and cash equivalents	\$ 188	\$ 177
Accounts receivable	667	917
Prepaid expenses	359	526
Premises and equipment, net	2,792	3,078
Other assets	290	294
Total Assets	\$4,296	\$4,992
Liabilities and Members' Equity (Deficit)		
Liabilities		
Capital lease obligations	\$2,328	\$3,211
Advances from the Bank	4,126	3,751
Other liabilities	636	509
Total Liabilities	7,090	7,471
Members' Equity (Deficit)	(2,794)	(2,479)
Total Liabilities and Members' Equity (Deficit)	\$4,296	\$4,992

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 18 - Subsidiary Only Financial Information (Continued)

Statements of Operations and Members' Equity (Deficit)

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Enhanced communications services revenue	\$7,057	\$ 4,189
Installation revenue	2,634	3,632
Direct costs of revenue	<u>(5,638)</u>	<u>(5,640)</u>
Gross Profit	<u>4,053</u>	<u>2,181</u>
Salaries and employee benefits	2,337	2,011
Occupancy and equipment	977	854
Professional and subcontracted services	446	429
Interest expense on loans from the Bank	28	53
Interest expense on capital lease obligations	208	258
Other	<u>372</u>	<u>400</u>
Total Other Expenses	<u>4,368</u>	<u>4,005</u>
Net Loss	(315)	(1,824)
Members' units purchased	-	6
Members' equity (deficit), January 1	<u>(2,479)</u>	<u>(661)</u>
Members' Equity (Deficit)	<u><u>\$(2,794)</u></u>	<u><u>\$(2,479)</u></u>

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 18 - Subsidiary Only Financial Information (Continued)

Statements of Cash Flows

	<u>2009</u>	<u>2008</u>
	(In Thousands)	
Cash Flows from Operating Activities		
Net loss	\$ (315)	\$(1,824)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation	535	514
(Increase) decrease in accounts receivable	250	(499)
(Increase) decrease in prepaid expenses	167	72
(Increase) decrease in other assets	4	(45)
Increase in other liabilities	127	437
Net Cash Provided by (Used in) Operating Activities	<u>768</u>	<u>(1,345)</u>
Cash Flows from Investing Activities		
Purchases of premises and equipment	(46)	(74)
Proceeds from sale of premises and equipment	67	-
Net Cash Provided by (Used in) Investing Activities	<u>21</u>	<u>(74)</u>
Cash Flows from Financing Activities		
Net advances from the Bank	375	2,515
Member units purchased	-	6
Payment on capital lease obligations	(1,153)	(1,000)
Net Cash Provided by (Used in) Financing Activities	<u>(778)</u>	<u>1,521</u>
Net Increase in Cash and Cash Equivalents	11	102
Cash and Cash Equivalents - Beginning	<u>177</u>	<u>75</u>
Cash and Cash Equivalents - Ending	<u>\$ 188</u>	<u>\$ 177</u>
Supplementary Cash Flows Information		
Equipment acquired under capital leases	<u>\$ 270</u>	<u>\$ 1,373</u>

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 18 - Subsidiary Only Financial Information (Continued)

Membership Units and Voting Structure

The membership units and voting structure of ACBB-BITS is as follows at December 31, 2009:

	Number of Units		Ownership Percentage	Voting Rights
	Authorized	Issued		
Class A is for bankers banks and community banks	2,500,000	2,500,000	25%	25%
Class B and C are for Bank (ACBB) and BITS employees, respectively	7,500,000	645,000	75%	-
Class D (a special unit) is for the Bank (ACBB)	1	1	-	75%
	<u>10,000,001</u>	<u>3,145,001</u>	<u>100%</u>	<u>100%</u>

All 2,500,000 Class A membership units were initially issued to the Bank. At December 31, 2009 and 2008, the Bank owned 2,180,000 of the membership units. The Bank sold no membership units in 2009 and 20,000 membership units in 2008 with proceeds of \$100,000 to one community financial institution.

Stock Option Plans

In 2007, the Bank approved the ACBB-BITS, LLC Membership Unit Benefits Plan for Employees of ACBB (ACBB Plan) and the ACBB-BITS, LLC Membership Unit Benefits Plan for Employees of ACBB-BITS, LLC (BITS Plan). These plans were created to enable employees of the Bank and BITS to participate in the long-term success and growth of BITS. The chief executive officer of the Bank serves as the manager of both the ACBB Plan and the BITS Plan (Plan Manager).

Under the ACBB Plan, there are 2,500,000 Class B Units available for grant as of December 31, 2009 and 2008. All employees of the Bank are eligible, but not entitled, to receive options to purchase Class B membership units at a price per share as determined at the date of grant by the Plan Manager, however, this price shall not be less than fair market value on the date the option is granted. Options granted under the ACBB Plan shall vest as determined by the Plan Manager coincident with each option grant and shall be exercisable as determined by the Plan Manager. For 2009 there were no options granted under the ACBB Plan. For 2008, the weighted-average grant-date fair value for the stock options granted was not material to the financial statements.

Atlantic Central Bankers Bank and Subsidiary

Notes to Consolidated Financial Statements

December 31, 2009 and 2008

Note 18 - Subsidiary Only Financial Information (Continued)

Stock Option Plans (Continued)

The fair values were estimated using the Black-Scholes model. Information regarding the ACBB Plan is as follows:

	2009			
	Options	Weighted Average Exercise Price	Weighted Average Remaining Life	Aggregate Intrinsic Value
Options outstanding, January 1	95,000	\$0.02	10.0 years	\$ -
Granted	-	-		-
Exercised	95,000	-		-
Options outstanding and exercisable at December 31	-	\$ -		\$ -
Options available for grant	1,855,000	\$ -		

Under the BITS Plan, there are 5,000,000 Class C Units available for grant as of December 31, 2009 and 2008. All employees of BITS are eligible, but not entitled, to receive options to purchase Class C membership units at a price per share as determined at the date of grant by the Plan Manager, however, this price shall not be less than fair market value on the date the option is granted. Options granted under the BITS Plan shall vest as determined by the Plan Manager coincident with each option grant and shall be exercisable as determined by the Plan Manager. For 2009 and 2008, the weighted-average grant-date fair value for the stock options granted was not material to the financial statements. The fair values were estimated using the Black-Scholes model. Information regarding the BITS Plan is as follows:

	2009			
	Options	Weighted Average Exercise Price	Weighted Average Remaining Life	Aggregate Intrinsic Value
Options outstanding, January 1	3,700,000	\$0.01	8.6 years	\$ -
Granted	520,000	0.02		-
Exercised	-	-		-
Options outstanding and exercisable at December 31	4,220,000	\$0.01	7.7 years	\$ -
Options available for grant	780,000	\$ -		