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POTOMAC BANCSHARES INC
Form 10-K
March 28, 2002

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-KSB

(Mark one)

XXX Annual Report Under Section 13 or 15(d) of the Securities Exchange Act
--- of 1934

For the fiscal year ended December 31, 2001

___ Transition report under Section 13 or 15(d) of the Securities Exchange
Act of 1934

For the transition period from _____ to _____

Commission File No. 0-24958

Potomac Bancshares, Inc.
(Name of Small Business Issuer in Its Charter)

West Virginia
(State or Other Jurisdiction of
Incorporation or Organization)

55-0732247
(I.R.S. Employer
Identification No.)

111 East Washington Street
PO Box 906, Charles Town WV
(Address of Principal Executive Offices)

25414-0906
(Zip Code)

304-725-8431
(Issuer's Telephone Number, Including Area Code)

Securities registered under Section 12(b) of the Exchange Act:

Title of Each Class -----	Name of Each Exchange on Which Registered -----
NONE -----	-----
-----	-----

Securities registered under Section 12(g) of the Exchange Act:

Common Stock, \$1.00 Par Value
(Title of Class)

Check whether the issuer: (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been

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subject to such filing requirements for past 90 days.

Yes ☒ No ☐

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Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. ☒ XX

State issuer's revenues for its most recent fiscal year.

\$12,313,495

State the aggregate market value of the voting stock held by non-affiliates computed by reference to the price at which the stock was sold, or the average bid and asked prices of such stock, as of a specified date within the past 60 days. \$21,424,371

ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PAST FIVE YEARS

Check whether the issuer has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Exchange Act after the distribution of securities under a plan confirmed by a court.

Yes ☐ No ☐ Not Applicable ☒ XXX

APPLICABLE ONLY TO CORPORATE REGISTRANTS

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date. 600,000

Transitional Small Business Disclosure Format (check one):

Yes ☐ No ☒ XXX

DOCUMENTS INCORPORATED BY REFERENCE

The following lists the documents which are incorporated by reference in the Form 10-KSB Annual Report, and the Parts and Items of the Form 10-KSB into which the documents are incorporated.

Document

Part of the Form 10-KSB Int
the Document is Incorpor

Portions of Potomac Bancshares, Inc.'s 2001 Annual
Report to Shareholders for the year ended December 31, 2001

Part II, Items 6 and 7

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Portions of Potomac Bancshares, Inc.'s Proxy Statement for
the 2002 Annual Meeting of Shareholders

Part III, Items 9, 10, 11 a

PART I

Item 1. Description of Business.

History and Operations

The Board of Directors of Bank of Charles Town (the "bank") caused Potomac Bancshares, Inc. ("Potomac") to be formed on March 2, 1994, as a single-bank holding company. To date, Potomac's only activities have involved the acquisition of the Bank. Potomac acquired all of the shares of common stock of the bank on July 29, 1994.

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Bank of Charles Town is a West Virginia state-chartered bank that formed and opened for business in 1871. The bank's deposits are insured by the Federal Deposit Insurance Corporation. The bank is engaged in general banking business primarily in Jefferson County and Berkeley County, West Virginia. The bank also provides services to Washington County and Frederick County, Maryland and Loudoun County, Frederick County and Clarke County, Virginia. The main office is in Charles Town, West Virginia at 111 East Washington Street, with branch offices in

- . Harpers Ferry, West Virginia,
- . Kearneysville, West Virginia and
- . Martinsburg, West Virginia.

The bank provides consumers, businesses, and governments with a broad range of banking services. These services include

- . lines of credit,
- . home equity lines of credit,
- . commercial, agricultural, real estate, installment loans,
- . checking, savings, NOW, money market accounts,
- . certificates of deposit, and
- . individual retirement accounts.

Automated teller machines are located at each of the four offices. Touchline 24 is an interactive voice response system available at 1-304-728-2424 that provides certain services to customers on a twenty-four hour basis. Bill paying and certain other banking services are available online through any touch tone telephone and/or the World Wide Web. The trust and financial services department provides financial management, investment and trust services.

Lending Activities. The bank offers installment, term, and real estate loans for consumer, business and commercial purposes. These loans can be unsecured, secured by collateral being purchased or secured by other collateral.

Underwriting standards for all lending include

- . sound credit analysis,
- . proper documentation according to the bank's loan documentation checklist,
- . promotion of profitable customer relationships with cross-

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- selling of bank services,
- . avoidance of loan concentrations to a single industry or with a single class of collateral, and
- . diligent maintenance of past due and nonaccrual loans.

The bank's loan policy designates particular loan-to-value limits for real estate loans in accordance with recommendations in Section 304 of the Federal Deposit Insurance Corporation Improvement Act of 1991. As stated in the loan policy, there may be certain lending situations not subject to these loan-to-value limits and from time to time the Board of Directors may permit exceptions to the established limits. Any exceptions are sufficiently documented.

Loans secured by real estate are made to individuals and businesses

- . for the purchase of raw land,
- . for land development,
- . for commercial, multi-family and other non-residential construction,
- . to purchase improved property,
- . to purchase owner occupied one to four family residential property,
- . for lines of credit and
- . for home equity loans.

Approximately 76% of the bank's loans are secured by real estate. These loans had an average delinquency rate of .62% and a loss rate of .01% during 2001. The average delinquency rate and loss rate is based on comparisons to 2001 average total loans.

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As of December 31, 2001, aggregate dollar amounts in loan categories secured by real estate are as follows:

Construction and land development	\$ 530,000
Secured by farmland	1,801,165
Secured by 1-4 family residential	56,283,230
Other	19,275,005

	\$ 77,889,400
	=====

Loans to individuals for personal expenditures are approximately 21% of the bank's total loans at December 31, 2001. The aggregate balance of these loans was \$21,213,959 at December 31, 2001. The majority of these loans are installment loans with the remainder made as term loans.

The bank's loan policy states that evaluation of applications for installment loans will consider place and length of residence, place and length of employment, and credit history. Although these are considered, verification of employment is usually not done, since it is recognized that unless immediate decisions on applications can be made, a lender may be unable to secure a fair share of loan business since instant credit is available from many sources in the market place. This may make installment lending more risky than real estate lending; however, installment loans had an average delinquency rate of .22% and a loss rate of .11% in 2001 (based on comparisons to 2001 average total loans). This delinquency rate for installment loans is lower than the comparable rate for real estate loans.

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The bank's policy for evaluating term loans involves consideration of credit history and current financial statements if the loan is of a certain amount and is unsecured. If loans are not paid at original scheduled maturity, a loan officer must review the loan before a renewal can be approved. The average delinquency rate was -0-% and the loss rate was .01% for term loans compared to average total loans in 2001.

The remaining aggregate dollar amount of the bank's loans is \$3,286,309 at December 31, 2001. The amount includes:

- | | |
|--|----|
| (1) Dealer wholesale loans with generally no delinquencies or losses | \$ |
| (2) Term loans for business and commercial purposes | 1, |
| (3) Industrial revenue bond loans secured by real estate | |
| (4) Term loans for agricultural purposes | |
| (5) Other loans | |

Investment Activities. The bank's investment activities are governed by its investment policy.

The policy states that excess daily funds are to be invested in federal funds sold and securities purchased under agreements to resell. The daily funds are used to cover deposit draw downs by customers, to fund loan commitments, and to help maintain the bank's asset/liability mix.

According to the policy, funds in excess of those invested in federal funds sold and securities purchased under agreements to resell are to be invested in U.S. Treasury bills, notes or bonds, obligations of U.S. Government agencies, obligations of political subdivisions of the State of West Virginia with a rating of not less than AAA and, with prior approval of the Board of Directors, bank qualified local industrial revenue bonds to be carried in the bank's loan portfolio.

The policy governs various other factors including maturities, the closeness of purchase price to par, amounts that may be purchased, and percentages of the various types of investments that may be held.

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Deposit Activities. The bank offers noninterest-bearing checking accounts, interest-bearing NOW accounts and interest-bearing money market accounts. Passbook and statement savings accounts and Christmas Club accounts are available. Certificates of deposit are offered in various terms from 91 days to four years and may be automatically renewed if the depositor wishes. Individual retirement accounts in the form of certificates of deposit are also available.

To open a deposit account, the depositor must meet the following requirements:

- . present a valid identification,
- . have a social security number,
- . must not be on record with Chex Systems (credit reporting

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- agency),
- . must be a U.S. citizen or possess evidence of legal alien status, and
- . must be at least 18 years of age or share account with a person at least 18 years of age.

Competition

As of March 7, 2002, there were 62 bank holding companies (including multi-bank and one bank holding companies) operating in the State of West Virginia. These holding companies are headquartered in various West Virginia cities and control banks throughout the State of West Virginia, including banks that compete with the bank in its market area.

The bank's market area is generally defined as Jefferson County and Berkeley County, West Virginia. The following data has not been updated since Berkeley County became part of the bank's primary market area. As of June 30, 2001, there were six banks in Jefferson County with 14 banking offices. The total deposits of those commercial banks as of June 2001 were \$477,886,000 and the bank ranked number one with \$131,144,000 or 27.44% of the total deposits in the market.

For most of the services which the bank performs, there is also competition from financial institutions other than commercial banks. For instance, credit unions and issuers of commercial paper and money market funds actively compete for funds and for various types of loans. In addition, personal and corporate trust and investment counseling services are offered by insurance companies, investment counseling firms and other business firms and individuals. Due to the geographic location of the bank's primary market area, the existence of larger financial institutions in Maryland, Virginia and Washington, D.C. influences the competition in the market area. In addition larger regional and national corporations continue to be increasingly visible in offering a broad range of financial services to all types of commercial and consumer customers. The principal competitive factors in the markets for deposits and loans are interest rates, either paid or charged. The chartering of numerous new banks in West Virginia and the opening of numerous federally chartered savings and loan associations have increased competition for the bank. The 1986 legislation passed by the West Virginia Legislature allowing state-wide branch banking provided increased opportunities for the bank, but it also increased competition for the bank in its service area. With the beginning of reciprocal interstate banking in 1988, bank holding companies (such as Potomac Bancshares, Inc.) also face additional competition in efforts to acquire other subsidiaries throughout West Virginia.

In 1994, Congress passed the Riegle-Neal Interstate Banking and Branching Efficiency Act. Under this Act, bank holding companies are permitted to acquire banks located in states other than the bank holding company's home state without regard to whether the transaction is permitted under state law. Commencing on June 1, 1997, the Act allows national banks and state banks with different home states to merge across state lines, unless the home state of a participating bank enacted legislation prior to May 31, 1997, that expressly prohibits interstate mergers. Additionally, the Act allows banks to branch across state lines, unless the state where the new branch will be located enacted legislation restricting or prohibiting de novo interstate branching on

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or before May 31, 1997. West Virginia adopted legislation, effective May 31, 1997, that allows for interstate branch banking by merger across state lines and allows for de novo branching and branching by purchase and assumption on a

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reciprocal basis with the home state of the bank in question. The effect of this legislation has been increased competition for West Virginia banks, including

the bank.

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Employees

Potomac currently has no employees.

As of March 22, 2002, the bank had 79 full-time employees and 15 part-time employees.

Supervision and Regulation

Introduction. Potomac is a bank holding company within the provisions of the Bank Holding Company Act of 1956, is registered as such, and is subject to supervision by the Board of Governors of the Federal Reserve System ("Board of Governors"). The Bank Holding Company Act requires Potomac to secure the prior approval of the Board of Governors before Potomac acquires ownership or control of more than five percent (5%) of the voting shares or substantially all of the assets of any institution, including another bank.

As a bank holding company, Potomac is required to file with the Board of Governors annual reports and such additional information as the Board of Governors may require pursuant to the Bank Holding Company Act. The Board of Governors may also make examinations of Potomac and its banking subsidiaries. Furthermore, under Section 106 of the 1970 Amendments to the Bank Holding Company Act and the regulations of the Board of Governors, a bank holding company and its subsidiaries are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit or any provision of credit, sale or lease of property or furnishing of services.

Potomac's depository institution subsidiaries are subject to affiliate transaction restrictions under federal law which limit the transfer of funds by the subsidiary banks to their respective parents and any nonbanking subsidiaries, whether in the form of loans, extensions of credit, investments or asset purchases. Such transfers by any subsidiary bank to its parent corporation or any nonbanking subsidiary are limited in an amount to 10% of the institution's capital and surplus and, with respect to such parent and all such nonbanking subsidiaries, to an aggregate of 20% of any such institution's capital and surplus.

Potomac is required to register annually with the Commissioner of Banking of West Virginia ("Commissioner") and to pay a registration fee to the Commissioner based on the total amount of bank deposits in banks with respect to which it is a bank holding company. Although legislation allows the Commissioner to prescribe the registration fee, it limits the fee to ten dollars per million dollars of deposits rounded off to the nearest million dollars. Potomac is also subject to regulation and supervision by the Commissioner.

Potomac is required to secure the approval of the West Virginia Board of Banking before acquiring ownership or control of more than five percent of the voting shares or substantially all of the assets of any institution, including another bank. West Virginia banking law prohibits any West Virginia or non-West Virginia bank or bank holding company from acquiring shares of a bank if the acquisition would cause the combined deposits of all banks in the State of West Virginia, with respect to which it is a bank holding company, to exceed 25% of the total deposits of all depository institutions in the State of West Virginia.

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Depository Institution Subsidiaries. Bank is subject to FDIC deposit insurance assessments. As of January 1, 2002, FDIC set the Financing Corporation (FICO) Bank Insurance Fund (BIF) premium for the bank at the annual rate of 1.820 basis points or .0001820 times the total deposits of the bank. This premium is not tied to the bank's risk classification. The rate of the premium based on the bank's risk classification is at 0.00%. It is possible that BIF insurance assessments will be changed, and it is also possible that there may be a special additional assessment. A large special assessment could have an adverse impact on Potomac's results of operations.

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Capital Requirements. The Federal Reserve Board has issued risk-based capital guidelines for bank holding companies, such as Potomac. The guidelines establish a systematic analytical framework that makes regulatory capital requirements more sensitive to differences in risk profiles among banking organizations, takes off-balance sheet exposures into explicit account in assessing capital adequacy, and minimizes disincentives to holding liquid, low-risk assets. Under the guidelines and related policies, bank holding companies must maintain capital sufficient to meet both a risk-based asset ratio test and leverage ratio test on a consolidated basis. The risk-based ratio is determined by allocating assets and specified off-balance sheet commitments into four weighted categories, with higher levels of capital being required for categories perceived as representing greater risk. The leverage ratio is determined by relating core capital (as described below) to total assets adjusted as specified in the guidelines. Bank is subject to substantially similar capital requirements adopted by applicable regulatory agencies.

Generally, under the applicable guidelines, the financial institution's capital is divided into two tiers. "Tier 1", or core capital, includes common equity, noncumulative perpetual preferred stock (excluding auction rate issues) and minority interests in equity accounts or consolidated subsidiaries, less goodwill. Bank holding companies, however, may include cumulative perpetual preferred stock in their Tier 1 capital, up to a limit of 25% of such Tier 1 capital. "Tier 2", or supplementary capital, includes, among other things, cumulative and limited-life preferred stock, hybrid capital instruments, mandatory convertible securities, qualifying subordinated debt, and the allowance for loan losses, subject to certain limitations, less required deductions. "Total capital" is the sum of Tier 1 and Tier 2 capital.

Financial institutions are required to maintain a risk-based ratio of 8%, of which 4% must be Tier 1 capital. The appropriate regulatory authority may set higher capital requirements when an institution's particular circumstances warrant.

Financial institutions that meet certain specified criteria, including excellent asset quality, high liquidity, low interest rate exposure and the highest regulatory rating, are required to maintain a minimum leverage ratio of 3%. Financial institutions not meeting these criteria are required to maintain a leverage ratio which exceeds 3% by a cushion of at least 100 to 200 basis points, and, therefore, the ratio of Tier 1 capital to total assets should not be less than 4%.

The guidelines also provide that financial institutions experiencing internal growth or making acquisitions will be expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets. Furthermore, the Federal Reserve Board's guidelines indicate that the Federal Reserve Board will continue to consider a "tangible Tier 1 leverage ratio" in evaluating proposals for

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expansion or new activities. The tangible Tier 1 leverage is the ratio of an institution's Tier 1 capital, less all intangibles, to total assets, less all intangibles.

Failure to meet applicable capital guidelines could subject the financial institution to a variety of enforcement remedies available to the federal regulatory authorities, including limitations on the ability to pay dividends, the issuance by the regulatory authority of a capital directive to increase capital and the termination of deposit insurance by the FDIC, as well as to the measures described in the "Federal Deposit Insurance Corporation Improvement Act of 1991" as applicable to undercapitalized institutions.

The Federal Reserve Board, as well as the FDIC, has adopted changes to their risk-based and leverage ratio requirements that require that all intangible assets, with certain exceptions, be deducted from Tier 1 capital. Under the Federal Reserve Board's rules, the only types of intangible assets that may be included in (i.e., not deducted from) a bank holding company's capital are readily marketable purchased mortgage servicing rights ("PMSRs") and purchased credit card relationships ("PCCRs"), provided that, in the aggregate, that total amount of PMSRs and PCCRs included in capital does not exceed 50% of Tier 1 capital. PCCRs are subject to a separate limit of 25% of Tier 1 capital. The amount of PMSRs and PCCRs that a bank holding company may include in its capital is limited to the lesser of (i) 90% of such assets' fair market value (as determined under the guidelines), or (ii) 100% of such assets' book value, each determined quarterly. Identifiable intangible assets (i.e., intangible assets other than goodwill) other than PMSRs and PCCRs, including core deposit intangibles, acquired on or before February 19, 1992 (the date the Federal Reserve Board issued its original proposal for public comment), generally will not be deducted from capital for supervisory purposes, although they will continue to be deducted for purposes of evaluating applications filed by bank holding companies.

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As of December 31, 2001, Potomac had capital in excess of all applicable requirements as shown below:

	Actual	Required	Excess
	-----	-----	-----
	(Amounts in thousands)		
Tier 1 capital:			
Common stock	\$ 600		
Surplus	5,400		
Retained earnings	13,208		

Total tier 1 capital	\$ 19,208	\$ 3,862	\$ 15,346
Tier 2 capital:			
Allowance for loan losses (1)	1,209		

Total risk-based capital	\$ 20,417	\$ 7,724	\$ 12,693
	=====	=====	=====
Risk-weighted assets	\$ 96,545		
	=====		
Tier 1 capital	\$ 19,208	\$ 5,099	\$ 14,109

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	=====	=====	=====
Average total assets	\$ 169,982		
	=====		
Capital ratios:			
Tier 1 risk-based capital ratio	19.90%	4.00%	15.90%
Total risk-based capital ratio	21.15%	8.00%	13.15%
Tier 1 capital to average total assets (leverage)	11.30%	4.00%	7.30%

(1) Limited to 1.25% of gross risk-weighted assets.

Gramm-Leach-Bliley Act of 1999. On November 4, 1999, Congress adopted the Gramm-Leach-Bliley Act of 1999. This Act, also known as the Financial Modernization Law, repealed a number of federal limitations on the powers of banks and bank holding companies originally adopted in the 1930's. Under the Act, banks, insurance companies, securities firms and other service providers may now affiliate. In addition to broadening the powers of banks, the Act created a new form of entity, called a financial holding company, which may engage in any activity that is financial in nature or incidental or complimentary to financial activities.

The Federal Reserve Board provides the principal regulatory supervision of financial services permitted under the Act. However, the Securities and Exchange Commission and state insurance and securities regulators also assume substantial supervisory powers and responsibilities.

The Act addresses a variety of other matters, including customer privacy issues. The obtaining of certain types of information by false or fraudulent pretenses is a crime. Banks and other financial institutions must notify their customers about their policies on sharing information with certain third parties. In some instances, customers may refuse to permit their information to be shared. The Act also requires disclosures of certain automatic teller machine fees and contains certain amendments to the federal Community Reinvestment Act.

Permitted Non-Banking Activities. Under the Gramm-Leach-Bliley Act, bank holding companies may become financial holding companies and engage in certain non-banking activities. Potomac has not yet filed to become a financial holding company and presently does not engage in, nor does it have any immediate plans to engage in, any such non-banking activities.

A notice of proposed non-banking activities must be furnished to the Federal Reserve and the Banking Board before Potomac engages in such activities, and an application must be made to the Federal Reserve and Banking Board concerning acquisitions by Potomac of corporations engaging in those activities. In addition, the Federal Reserve may, by order issued on a case-by-case basis, approve additional non-banking activities.

The Bank. The bank is a state-chartered bank that is not a member of the Federal Reserve system and is subject to regulation and supervision by the FDIC and the Commissioner.

Compliance with Environmental Laws. The costs and effects of compliance with federal, state and local environmental laws will not have a material effect or impact on Potomac or the bank.

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Item 2. Description of Property.

Potomac currently has no property.

The bank owns the land and buildings of the main office and the branch office facilities in Harpers Ferry and Kearneysville.

Main office property is located at 111 East Washington Street, Charles Town, West Virginia. This property consists of two separate two story buildings located side by side with adjoining corridors. During 2000 the construction of the newer of these two buildings was completed. The first floor of the new building houses the Trust and Financial Services Division. The second floor of the new building houses certain administrative and loan offices. Both of these floors open into the older bank premises. The basement of the new building is used for record storage.

The older premises, constructed in 1967, was renovated at the same time the new building was constructed. The renovation includes all new lighting, new ceilings, new floor and wall coverings as well as some minor structural changes for more efficient operations.

The Harpers Ferry branch office is located at 1318 Washington Street, Bolivar, West Virginia. The office is a one story brick building constructed in 1975. There is another building on this property which existed at the time of the bank's purchase. This building is rented to others by the bank.

The branch facility in Kearneysville, West Virginia was erected in 1985. This one story brick building opened for business in April of 1985. During 1993, an addition was constructed, doubling the size of this facility.

The bank leases the facilities housing the branch office in Martinsburg, West Virginia. The three year lease expires in February, 2004. Renewals are an option. This branch opened for business in July, 2001.

The bank has an option to buy property in Hedgesville, West Virginia. If purchased, a fourth full service branch will be constructed on the sight.

There are no encumbrances on any of these properties. In the opinion of management, these properties are adequately covered by insurance.

Item 3. Legal Proceedings.

Currently Potomac is involved in no legal proceedings.

The bank is involved in various legal proceedings arising in the normal course of business, and in the opinion of the bank, the ultimate resolution of these proceedings will not have a material effect on the financial position or operations of the bank.

Item 4. Submission of Matters to a Vote of Security Holders.

Not Applicable.

PART II

Item 5. Market for Common Equity and Related Stockholder Matters.

The following information reflects comparative per share data for the periods indicated for Potomac common stock for (a) trading values, and (b) dividends. As of March 15, 2002, there were approximately 1,100 shareholders.

Potomac Common Stock is not traded on any stock exchange or over the counter. Potomac (symbol PTBS) is now on the OTC Bulletin Board, a network available to brokers. Scott and Stringfellow, a regional securities firm with an office in Winchester, Virginia, is a market maker for Potomac common stock. A market maker is one who makes a market for a particular stock. Information about sales (but not necessarily all sales) of Potomac common stock is available on the Internet through many of the stock information services using Potomac's symbol. Shares of Potomac common stock are occasionally bought and sold by private individuals, firms or corporations, and, in many instances, Potomac does not have knowledge of the purchase price or the terms of the purchase. The trading values for 2000 and 2001 are based on information available as a result of our participation on the Bulletin Board described above and information gathered on the Internet. No attempt was made by Potomac to verify or determine the accuracy of the representations made to Potomac or gathered on the Internet.

		Price Range		Cash Dividends*
		High	Low	Paid per Share
2000	First Quarter	\$ 33.500	\$ 28.250	\$ N/A
	Second Quarter	30.000	26.125	.50
	Third Quarter	28.500	24.000	N/A
	Fourth Quarter	28.000	22.000	.75
2001	First Quarter	\$ 28.750	\$ 25.000	\$ N/A
	Second Quarter	33.500	25.250	.50
	Third Quarter	34.500	32.000	N/A
	Fourth Quarter	38.500	33.000	.85

* Dividends have been declared traditionally by Potomac on a semi-annual basis.

The primary source of funds for dividends paid by Potomac is the dividend income received from the bank. The bank's ability to pay dividends is subject to restrictions under federal and state law, and under certain cases, approval by the FDIC and Commissioner could be required. Management of Potomac anticipates that the dividends paid by Potomac will likely be similar to those paid in the past, but dividends will only be paid when and as declared by the board of directors.

Item 6. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The information contained on pages 4-11 of the Annual Report to Shareholders for the year ended December 31, 2001, is incorporated herein by reference.

Item 7. Financial Statements.

The information contained on pages 13-31 of the Annual Report to Shareholders for the year ended December 31, 2001, is incorporated herein by reference.

Item 8. Changes In and Disagreements with Accountants on Accounting and Financial Disclosure.

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Not Applicable.

PART III

Item 9. Directors, Executive Officers, Promoters and Control Persons; Compliance with Section 16(a) of the Exchange Act.

The information contained on pages 5-6 and 13 of the Proxy Statement dated March 29, 2002, for the April 23, 2002 Annual Meeting under the captions "Management Nominees to the Board of Potomac," "Directors Continuing to Serve Unexpired Terms," and "Section 16(a) Beneficial Ownership Reporting Compliance" is incorporated herein by reference.

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The Executive Officers are as follows:

Name	Position Since	Age	Principal Occupation
Robert F. Baronner, Jr.	President & CEO 2001	43	Employed by bank as of 1/1/00 & CEO; former Senior Credit Northern West Virginia May 2000; former Executive Vice Valley Bank East September 1 2000; Senior Vice President Lending Division One Valley 1994 - September 1997.
William R. Harner	Sr. Vice President, Secretary & Treasurer 1994	61	Employed at bank since 1967; President & Cashier since 1994
Gayle Marshall Johnson	Vice President & Chief Financial Officer 1994	52	Employed with the bank 1977- internal auditor. Rejoined bank as Financial Officer. Vice President Financial Officer of bank since 1994
Donald S. Smith	Vice President & Assistant Secretary 1994	73	Employed at bank 1947 to 1991 1979 to 1991 (retired).

Item 10. Executive Compensation.

The information contained on pages 8-9 and 12 of the Proxy Statement dated March 29, 2002, for the April 23, 2002 Annual Meeting under the captions "Executive Compensation," "Employment Agreement," and "Compensation of Directors" is incorporated herein by reference.

Item 11. Security Ownership of Certain Beneficial Owners and Management.

The information contained on pages 6-8 of the Proxy Statement dated March 29, 2002, for the April 23, 2002 Annual Meeting under the captions "Principal Holders of Voting Securities" and "Ownership of Securities by Nominees, Directors and Officers" is incorporated herein by reference.

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Item 12. Certain Relationships and Related Transactions.

The information contained on page 12 of the Proxy Statement dated March 29, 2002, for the April 23, 2002 Annual Meeting under the caption "Certain Transactions with Directors, Officers and Their Associates" is incorporated herein by reference.

Item 13. Exhibits List and Reports on Form 8-K.

(a) 2.1 Agreement and Plan of Merger dated March 8, 1994, by and between Potomac Bancshares, Inc., and Bank of Charles Town filed with and incorporated by reference from the Registration on Form S-4 filed with the Securities and Exchange Commission on June 10, 1994: Registration no. 33-80092.

3.1 Articles of Incorporation of Potomac Bancshares, Inc. filed with and incorporated by reference from the Registration on Form S-4 filed with the Securities and Exchange Commission on June 10, 1994: Registration no. 33-80092.

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3.2 Amendments to Articles of Incorporation of Potomac Bancshares, Inc. adopted by shareholders on April 25, 1995 and filed with the West Virginia Secretary of State on May 23, 1995, and incorporated by reference from Potomac's Form 10-KSB for the year ended December 31, 1995 and filed with the Securities and Exchange Commission, file no. 0-24958.

3.3 Bylaws of Potomac Bancshares, Inc. filed with and incorporated by reference from the Registration on Form S-4 filed with the Securities and Exchange Commission on June 10, 1994: Registration no. 33-80092.

3.4 Amended and Restated Bylaws of Potomac Bancshares, Inc. adopted by shareholders April 25, 1995 and incorporated by reference from Potomac's Form 10-KSB for the year ended December 31, 1995 and filed with the Securities and Exchange Commission, file no. 0-24958.

10.2 Employment Agreement

13 2001 Annual Report to Shareholders

21 Subsidiaries of the Registrant

99 Proxy Statement for the 2002 Annual Meeting for Potomac

(b) No Form 8-K reports were filed during the last quarter of 2001.

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SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

POTOMAC BANCSHARES, INC.

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By /s/ Robert F. Baronner, Jr. March 22, 2002

Robert F. Baronner, Jr.
President & Chief Executive Officer

By /s/ L. Gayle Marshall Johnson March 22, 2002

L. Gayle Marshall Johnson
Vice President & Chief Financial Officer

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature & Title -----	Date ----
By /s/ J. Scott Boyd ----- J. Scott Boyd, Director	March 22, 2002 ---
By /s/ John P. Burns, Jr. ----- John P. Burns, Jr., Director	March 22, 2002 ---
By /s/ Robert W. Butler ----- Robert W. Butler, Director	March 22, 2002 ---
By /s/ Guy Gareth Chicchirichi ----- Guy Gareth Chicchirichi, Director	March 22, 2002 ---
By /s/ Thomas C. G. Coyle ----- Thomas C. G. Coyle, Director	March 22, 2002 ---

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Signature & Title -----	Date ----
By /s/ William R. Harner ----- William R. Harner, Director, Sr. Vice President, Secretary & Treasurer	March 22, 2002 ---
By /s/ E. William Johnson ----- E. William Johnson, Director	March 22, 2002 ---
By /s/ John C. Skinner, Jr. ----- John C. Skinner, Jr., Director	March 22, 2002 ---
By /s/ Donald S. Smith -----	March 22, 2002 ---

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Donald S. Smith, Director