FRANKLIN FINANCIAL SERVICES CORP /PA/
Form 10-Q
August 09, 2010

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2010,

OR

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

For the transition period from _________ to _________

Commission file number 0-12126

FRANKLIN FINANCIAL SERVICES CORPORATION
(Exact name of registrant as specified in its charter)

PENNSYLVANIA (State or other jurisdiction of incorporation or organization)	25-1440803 (I.R.S. Employer Identification No.)

20 SOUTH MAIN STREET (P.O. BOX 6010), CHAMBERSBURG, PA 17201-0819
(Address of principal executive offices)

717/264-6116
(Registrant's telephone number, including area code)

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes x   No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o

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

Large accelerated filer o   Accelerated filer x   Non-accelerated filer o   Smaller reporting company o

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Act) Yeso No x

There were 3,888,866 outstanding shares of the Registrant's common stock as of July 30, 2010.

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Part I FINANCIAL INFORMATION

Item 1 Financial Statements

Consolidated Balance Sheets
(Amounts in thousands, except share and per share data)
(unaudited)

	June 30 2010	December 31 2009
Assets		
Cash and due from banks	$ 16,881	$ 14,336
Interest-bearing deposits in other banks	20,130	18,912
Total cash and cash equivalents	37,011	33,248
Investment securities available for sale	128,347	143,288
Restricted stock	6,482	6,482
Loans	758,411	739,563
Allowance for loan losses	(9,751)	(8,937)
Net Loans	748,660	730,626
Premises and equipment, net	16,282	15,741
Bank owned life insurance	19,251	18,919
Goodwill	9,016	9,159
Other intangible assets	2,232	2,461
Other assets	19,324	19,449
Total assets	$ 986,605	$ 979,373
Liabilities		
Deposits		
Demand (non-interest bearing)	$ 90,324	$ 77,675
Savings and interest-bearing checking	421,671	388,222
Time	218,362	272,468
Total Deposits	730,357	738,365
Securities sold under agreements to repurchase	68,622	55,855
Long-term debt	93,796	94,688
Other liabilities	12,673	11,699
Total liabilities	905,448	900,607
Shareholders' equity		
Common stock $1 par value per share, 15,000,000 shares authorized with 4,298,904 shares issued, and 3,888,368 shares and 3,863,066 shares outstanding at June 30, 2010 and December 31, 2009, respectively	4,299	4,299
Capital stock without par value, 5,000,000 shares authorized with no shares issued or outstanding	-	-
Additional paid-in capital	32,806	32,832
Retained earnings	56,610	54,566
Accumulated other comprehensive loss	(5,217)	(5,138)
Treasury stock, 410,536 shares and 435,838 shares at cost at June 30, 2010 and December 31, 2009, respectively	(7,341)	(7,793)

Total shareholders' equity	81,157	78,766
Total liabilities and shareholders' equity	$ 986,605	$ 979,373

The accompanying notes are an integral part of these financial statements.

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Consolidated Statements of Income
(Amounts in thousands, except per share data)
(unaudited)

	For the Three Months Ended June 30		For the Six Months Ended June 30	
	2010	2009	2010	2009
Interest income				
Loans, including fees	$ 9,691	$ 9,463	$ 19,242	$ 18,655
Interest and dividends on investments:				
Taxable interest	758	1,017	1,628	2,106
Tax exempt interest	397	463	869	937
Dividend income	10	39	27	96
Federal funds sold	-	6	-	6
Deposits and obligations of other banks	10	1	16	1
Total interest income	10,866	10,989	21,782	21,801
Interest expense				
Deposits	2,204	2,535	4,563	5,018
Securities sold under agreements to repurchase	40	45	77	90
Short-term borrowings	-	-	-	11
Long-term debt	977	1,050	1,951	2,105
Total interest expense	3,221	3,630	6,591	7,224
Net interest income	7,645	7,359	15,191	14,577
Provision for loan losses	625	426	1,250	1,019
Net interest income after provision for loan losses	7,020	6,933	13,941	13,558
Noninterest income				
Investment and trust services fees	1,007	862	2,024	1,757
Loan service charges	272	378	469	653
Mortgage banking activities	11	118	81	91
Deposit service charges and fees	593	653	1,171	1,232
Other service charges and fees	351	339	677	641
Increase in cash surrender value of life insurance	166	160	332	324
Other	22	29	70	325
OTTI losses on securities	-	(212)	(689)	(421)
Loss recognized in other comprehensive income (before taxes)	-	-	(434)	-
Net OTTI losses recognized in earnings	-	(212)	(255)	(421)
Securities gains, net	20	42	268	54
Total noninterest income	2,442	2,369	4,837	4,656
Noninterest Expense				
Salaries and benefits	3,322	3,126	6,762	6,279
Net occupancy expense	496	476	1,019	956
Furniture and equipment expense	191	213	382	429

Advertising	343	418	655	734
Legal and professional fees	350	293	745	545
Data processing	502	435	879	836
Pennsylvania bank shares tax	152	143	308	288
Intangible amortization	114	117	229	234
FDIC insurance	288	683	580	914
Other	767	1,062	1,627	1,900
Total noninterest expense	6,525	6,966	13,186	13,115
Income before federal income taxes	2,937	2,336	5,592	5,099
Federal income tax expense	778	697	1,459	1,359
Net income	$ 2,159	$ 1,639	$ 4,133	$ 3,740
Per share				
Basic earnings per share	$ 0.56	$ 0.43	$ 1.07	$ 0.98
Diluted earnings per share	$ 0.56	$ 0.43	$ 1.07	$ 0.98
Cash dividends declared per share	$ 0.27	$ 0.27	$ 0.54	$ 0.54

The accompanying notes are an integral part of these financial statements.

Consolidated Statements of Changes in Shareholders' Equity
For the Six Months Ended June 30, 2010 and 2009
(unaudited)

(Dollars in thousands, except share and per share data)	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total
Balance at December 31, 2008	$ 4,299	$ 32,883	$ 52,126	$ (7,757)	$ (8,492)	$ 73,059
Comprehensive income:						
Net income	-	-	3,740	-	-	3,740
Unrealized gain on securities, net of reclassification adjustments and taxes	-	-	-	114	-	114
Unrealized gain on hedging activities, net of reclassification adjustments and taxes	-	-	-	815	-	815
Total Comprehensive income				-		4,669
Cash dividends declared, $.54 per share	-	-	(2,068)	-	-	(2,068)
Acquisition of 5,640 shares of treasury stock	-	-	-	-	(93)	(93)
Treasury shares issued to dividend reinvestment plan: 23,496 shares	-	(50)	-	-	420	370
Stock option compensation	-	20	-	-	-	20
Balance at June 30, 2009	$ 4,299	$ 32,853	$ 53,798	$ (6,828)	$ (8,165)	$ 75,957
Balance at December 31, 2009	$ 4,299	$ 32,832	$ 54,566	$ (5,138)	$ (7,793)	$ 78,766
Comprehensive income:						
Net income	-	-	4,133	-	-	4,133
Unrealized gain on securities, net of reclassification adjustments and taxes	-	-	-	482	-	482
Unrealized loss on hedging activities, net of reclassification adjustments and taxes	-	-	-	(435)	-	(435)
Pension adjustment, net of tax				(126)		(126)
Total Comprehensive income				-		4,054
Cash dividends declared, $.54 per share	-	-	(2,089)	-	-	(2,089)
Treasury shares issued under stock option plans: 1,051 shares	-	(2)	-	-	18	16
Treasury shares issued to dividend reinvestment plan: 24,251 shares	-	(24)	-	-	434	410
Balance at June 30, 2010	$ 4,299	$ 32,806	$ 56,610	$ (5,217)	$ (7,341)	$ 81,157

The accompanying notes are an integral part of these financial statements.

Consolidated Statements of Cash Flows
(unaudited)

	For the Six Months Ended June 30	
	2010	2009
(Amounts in thousands)		
Cash flows from operating activities		
Net income	$ 4,133	$ 3,740
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	672	717
Net amortization of loans and investment securities	152	46
Stock option compensation expense	-	20
Amortization and net change in mortgage servicing rights valuation	73	71
Amortization of intangibles	229	234
Provision for loan losses	1,250	1,019
Net realized gains on sales of securities	(268)	(54)
OTTI losses on securities	255	421
Loans originated for sale	(920)	-
Proceeds from sale of loans	952	-
Gain on sales of loans	(32)	-
(Gain) loss on sale or disposal of premises and equipment	(4)	118
Net gain on sale or disposal of other real estate/other repossessed assets	-	(6)
Increase in cash surrender value of life insurance	(332)	(324)
Gain from surrender of life insurance policy	-	(276)
Contribution to pension plan	(525)	(87)
Decrease in interest receivable and other assets	239	841
Increase in interest payable and other liabilities	130	389
Other, net	90	102
Net cash provided by operating activities	6,094	6,971
Cash flows from investing activities		
Proceeds from sales of investment securities available for sale	6,378	7,364
Proceeds from maturities and paydowns of investment securities available for sale	15,341	13,976
Purchase of investment securities available for sale	(6,081)	(21,132)
Net increase in loans	(19,447)	(28,375)
Proceeds from sale of other real estate/other repossessed assets	440	33
Proceeds from surrender of life insurance policy	-	600
Capital expenditures	(1,166)	(896)
Net cash used in investing activities	(4,535)	(28,430)
Cash flows from financing activities		
Net increase in demand deposits, interesting-bearing checking and savings accounts	46,098	17,021
Net (decrease) increase in time deposits	(54,106)	65,631
Net increase (decrease) in short-term borrowings	12,767	(18,146)
Long-term debt payments	(892)	(2,960)
Long-term debt advances	-	260
Dividends paid	(2,089)	(2,068)
Common stock issued to dividend reinvestment plan	410	370

Common stock issued under stock option plans		16		-
Purchase of treasury shares		-		(93)
Net cash provided by financing activities		2,204		60,015
Increase in cash and cash equivalents		3,763		38,556
Cash and cash equivalents as of January 1		33,248		16,713
Cash and cash equivalents as of June 30	$	37,011	$	55,269
Supplemental Disclosures of Cash Flow Information				
Cash paid during the year for:				
Interest on deposits and other borrowed funds	$	6,874	$	7,365
Income taxes	$	2,602	$	1,494
Noncash Activities				
Loans transferred to Other Real Estate	$	-	$	413

The accompanying notes are an integral part of these financial statements.

FRANKLIN FINANCIAL SERVICES CORPORATION and SUBSIDIARIES
UNAUDITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - Basis of Presentation

The consolidated financial statements include the accounts of Franklin Financial Services Corporation (the Corporation), and its wholly-owned subsidiaries, Farmers and Merchants Trust Company of Chambersburg (the Bank), Franklin Financial Properties Corp., and Franklin Future Fund Inc. Farmers and Merchants Trust Company of Chambersburg is a commercial bank that has one wholly-owned subsidiary, Franklin Realty Services Corporation. Franklin Realty Services Corporation is an inactive real-estate brokerage company. Franklin Financial Properties Corp. holds real estate assets that are leased by the Bank. Franklin Future Fund Inc. is a non-bank investment company. The activities of non-bank entities are not significant to the consolidated totals. All significant intercompany transactions and account balances have been eliminated.

In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the consolidated financial position, results of operations, and cash flows as of June 30, 2010, and for all other periods presented have been made.

Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted. It is suggested that these consolidated financial statements be read in conjunction with the audited consolidated financial statements and notes thereto included in the Corporation’s 2009 Annual Report on Form 10-K. The consolidated results of operations for the period ended June 30, 2010 are not necessarily indicative of the operating results for the full year. Management has evaluated subsequent events for potential recognition and/or disclosure through the date these consolidated financial statements were issued.

The consolidated balance sheet at December 31, 2009 has been derived from the audited consolidated financial statements at that date, but does not include all of the information and footnotes required by GAAP for complete consolidated financial statements.

For purposes of reporting cash flows, cash and cash equivalents include Cash and due from banks, Interest-bearing deposits in other banks and Federal funds sold. Generally, Federal funds are purchased and sold for one-day periods.

Earnings per share is computed based on the weighted average number of shares outstanding during each period end. A reconciliation of the weighted average shares outstanding used to calculate basic earnings per share and diluted earnings per share follows:

(In thousands, except per share data)	For the Three Months Ended June 30 2010	For the Three Months Ended June 30 2009	For the Six Months Ended June 30 2010	For the Six Months Ended June 30 2009
Weighted average shares outstanding (basic)	3,880	3,837	3,874	3,832
Impact of common stock equivalents	3	-	2	-
Weighted average shares outstanding (diluted)	3,883	3,837	3,876	3,832
Anti-dilutive options excluded from the calculation	76	109	76	110
Net income	$ 2,159	$ 1,639	$ 4,133	$ 3,740
Basic earnings per share	$ 0.56	$ 0.43	$ 1.07	$ 0.98
Diluted earnings per share	$ 0.56	$ 0.43	$ 1.07	$ 0.98

Note 2 – Recent Accounting Pronouncements

Receivables and the Allowances for Credit Losses. In July 2010, the FASB issued Accounting Standards Update No. (ASU) 2010-20, Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowances for Credit Losses. This Update requires expanded disclosures to help financial statement users understand the nature of credit risks inherent in a creditor’s portfolio of financing receivables; how that risk is analyzed and assessed in arriving at the allowance for credit losses; and the changes, and reasons for those changes, in both the receivables and the allowance for credit losses. The disclosures should be prepared on a disaggregated basis and provide a roll-forward schedule of the allowance for credit losses and detailed information on financing receivables including, among other things, recorded balances, nonaccrual status, impairments, credit quality indicators, details for troubled debt restructurings and an aging of past due financing receivables. Disclosures required as of the end of a reporting period are effective for interim and annual reporting periods ending after December 15, 2010. Disclosures required for activity occurring during a reporting period are effective for interim and annual reporting periods beginning after December 15, 2010. This Update is not expected to have a material impact on the Corporation’s financial position or consolidated financial statements.

Fair Value Measurements and Disclosures. The FASB has issued ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements. This ASU requires some new disclosures and clarifies some existing disclosure requirements about fair value measurement as set forth in Codification Subtopic 820-10. The FASB’s objective is to improve these disclosures and, thus, increase the transparency in financial reporting. Specifically, ASU 2010-06 amends Codification Subtopic 820-10 to now require a reporting entity to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers; and in the reconciliation for fair value measurements using significant unobservable inputs, a reporting entity should present separately information about purchases, sales, issuances, and settlements. ASU 2010-06 is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The Corporation early adopted ASU 2010-09 effective with the quarter end June 30, 2010.

Transfers and Servicing. In October 2009, the FASB issued ASU 2009-16, Transfers and Servicing (Topic 860) - Accounting for Transfers of Financial Assets. This Update amends the Codification for the issuance of FASB Statement No. 166, Accounting for Transfers of Financial Assets-an amendment of FASB Statement No. 140. The amendments in this Update improve financial reporting by eliminating the exceptions for qualifying special-purpose entities from the consolidation guidance and the exception that permitted sale accounting for certain mortgage securitizations when a transferor has not surrendered control over the transferred financial assets. In addition, the amendments require enhanced disclosures about the risks that a transferor continues to be exposed to because of its continuing involvement in transferred financial assets. Comparability and consistency in accounting for transferred financial assets will also be improved through clarifications of the requirements for isolation and limitations on portions of financial assets that are eligible for sale accounting. This Update was effective January 1, 2010 for the Corporation and there was no material affect on its operating results, financial position or consolidated financial statements.

Note 3 – Comprehensive Income

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on available-for-sale securities and derivatives and the change in plan assets and benefit obligations on the Bank’s pension plan, net of tax, that are recognized as separate components of shareholders’ equity.

The components of comprehensive income and related tax effects are as follows:

(Amounts in thousands)	For the Three Months Ended June 30		For the Six Months Ended June 30	
	2010	2009	2010	2009
Net Income	$ 2,159	$ 1,639	$ 4,133	$ 3,740
Securities:				
Unrealized (losses) gains arising during the period	(690)	1,882	744	(196)
Reclassification adjustment for losses (gains) included in net income	(20)	170	(13)	367
Net unrealized (losses) gains	(710)	2,052	731	171
Tax effect	241	(698)	(249)	(57)
Net of tax amount	(469)	1,354	482	114
Derivatives:				
Unrealized (losses) gains arising during the period	(677)	777	(1,015)	885
Reclassification adjustment for losses included in net income	174	177	354	350
Net unrealized (losses) gains	(503)	954	(661)	1,235
Tax effect	171	(323)	226	(420)
Net of tax amount	(332)	631	(435)	815
Pension:				
Change in plan assets and benefit obligations	-	-	(191)	-
Reclassification adjustment for losses included in net income	-	-	-	-
Net unrealized losses	-	-	(191)	-
Tax effect	-	-	65	-
Net of tax amount	-	-	(126)	-
Total other comprehensive (loss) income	(801)	1,985	(79)	929
Total Comprehensive Income	$ 1,358	$ 3,624	$ 4,054	$ 4,669

The components of accumulated other comprehensive loss included in shareholders' equity are as follows:

(Amounts in thousands)	June 30 2010	December 31 2009
Net unrealized losses on securities	$ (1,098)	$ (1,829)
Tax effect	373	622
Net of tax amount	(725)	(1,207)
Net unrealized losses on derivatives	(1,924)	(1,263)
Tax effect	655	429
Net of tax amount	(1,269)	(834)
Accumulated pension adjustment	(4,883)	(4,692)
Tax effect	1,660	1,595
Net of tax amount	(3,223)	(3,097)

Total accumulated other comprehensive loss	$	(5,217)	$	(5,138)

Note 4 – Guarantees

The Corporation does not issue any guarantees that would require liability recognition or disclosure, other than its standby letters of credit. Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Generally, all letters of credit, when issued, have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as those that are involved in extending loan facilities to customers. The Bank generally holds collateral and/or personal guarantees supporting these commitments. The Bank had $28.3 million and $26.7 million of standby letters of credit as of June 30, 2010 and December 31, 2009, respectively. Management believes that the proceeds obtained through a liquidation of collateral and the enforcement of guarantees would be sufficient to cover the potential amount of future payments required under the corresponding guarantees. The amount of the liability as of June 30, 2010 and December 31, 2009 for guarantees under standby letters of credit issued was not material.

Note 5 - Investments

The amortized cost and estimated fair value of investment securities available for sale as of June 30, 2010 and December 31, 2009 are:

(Amounts in thousands) June 30, 2010	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
Equity securities	$ 5,401	$ 65	$ (1,444)	$ 4,022
U.S. Treasury securities and obligations of U.S. Government agencies	22,723	414	(95)	23,042
Obligations of state and political subdivisions	40,852	1,186	(46)	41,992
Corporate debt securities	8,611	26	(1,787)	6,850
Mortgage-backed securities				
Agency	46,726	1,408	(11)	48,123
Non-Agency	5,051	-	(786)	4,265
Asset-backed securities	81	-	(28)	53
	$ 129,445	$ 3,099	$ (4,197)	$ 128,347

(Amounts in thousands) December 31, 2009	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
Equity securities	$ 5,400	$ 37	$ (1,462)	$ 3,975
U.S. Treasury securities and obligations of U.S. Government agencies	28,258	618	(161)	28,715
Obligations of state and political subdivisions	42,611	1,332	(62)	43,881
Corporate debt securities	9,603	-	(2,343)	7,260
Mortgage-backed securities				
Agency	53,214	1,576	(47)	54,743
Non-Agency	5,947	-	(1,279)	4,668
Asset-backed securities	84	-	(38)	46
	$ 145,117	$ 3,563	$ (5,392)	$ 143,288

The book value of securities pledged as collateral to secure various funding sources was $116.5 million at June 30, 2010 and $134.6 million at December 31, 2009.

The amortized cost and estimated fair value of debt securities as of June 30, 2010, by contractual maturity are shown below. Actual maturities may differ from contractual maturities because of prepayment or call options embedded in the securities.

(Amounts in thousands)	Amortized cost	Estimated fair value
Due in one year or less	$ 3,438	$ 3,450
Due after one year through five years	15,043	15,324
Due after five years through ten years	26,228	27,171
Due after ten years	27,558	25,992
	72,267	71,937
Mortgage-backed securities	51,777	52,388
	$ 124,044	$ 124,325

The following table reflects temporary impairment in the investment portfolio (excluding restricted stock), aggregated by investment category, length of time that individual securities have been in a continuous unrealized loss position and the number of securities in each category as of June 30, 2010 and December 31, 2009:

	June 30, 2010								
	Less than 12 months			12 months or more			Total		
(Amounts in thousands)	Fair Value	Unrealized Losses	Number	Fair Value	Unrealized Losses	Number	Fair Value	Unrealized Losses	Number
Equity securities	$ 1,840	$ (287)	2	$ 1,796	$ (1,157)	22	$ 3,636	$ (1,444)	24
U.S. Treasury securities and obligations of U.S. Government agencies	76	-	2	9,654	(95)	20	9,730	(95)	22
Obligations of state and political subdivisions	2,528	(31)	7	292	(15)	1	2,820	(46)	8
Corporate debt securities	-	-	-	6,096	(1,787)	9	6,096	(1,787)	9
Mortgage-backed securities									
Agency	1,727	(9)	3	699	(2)	1	2,426	(11)	4
Non-Agency	-	-	-	4,265	(786)	7	4,265	(786)	7
Asset-backed securities	-	-	-	53	(28)	3	53	(28)	3
Total temporarily impaired securities	$ 6,171	$ (327)	14	$ 22,855	$ (3,870)	63	$ 29,026	$ (4,197)	77

	December 31, 2009								
	Less than 12 months			12 months or more			Total		
(Amounts in thousands)	Fair Value	Unrealized Losses	Number	Fair Value	Unrealized Losses	Number	Fair Value	Unrealized Losses	Number
Equity securities	$ 2,343	$ (395)	7	$ 1,494	$ (1,067)	21	$ 3,837	$ (1,462)	28
U.S. Treasury securities and	63	-	3	13,411	(161)	27	13,474	(161)	30

obligations of U.S. Government agencies									
Obligations of state and political subdivisions	1,843	(41)	6	285	(21)	1	2,128	(62)	7
Corporate debt securities	622	(1)	5	6,537	(2,342)	10	7,159	(2,343)	15
Mortgage-backed securities									
Agency	10,812	(47)	9	-	-	-	10,812	(47)	9
Non-Agency	-	-	-	4,668	(1,279)	7	4,668	(1,279)	7
Asset-backed securities	-	-	-	46	(38)	3	46	(38)	3
Total temporarily impaired securities	$ 15,683	$ (484)	30	$ 26,441	$ (4,908)	69	$ 42,124	$ (5,392)	99

The following table reflects additional information about trust preferred securities as of June 30, 2010:

Trust Preferred Securities
June 30, 2010

(Dollars in thousands)

Deal Name	Single Issuer or Pooled	Class	Amortized Cost	Estimated Fair Value	Gross Unrealized Gain (Loss)	Lowest Credit Rating Assigned	Number of Banks currently Performing	Deferrals and Defaults as % of Original Collateral	Expected Deferral/ Defaults as a Percentage of Remaining Performing Collateral
Huntington Cap Trust	Single	Preferred Stock	$ 926	$ 595	$ (331)	Ba1	1	None	None
Huntingtn Cap Trust II	Single	Preferred Stock	870	565	(305)	Ba1	1	None	None
BankAmerica Cap III	Single	Preferred Stock	954	673	(281)	Baa3	1	None	None
Wachovia Cap Trust II	Single	Preferred Stock	272	230	(42)	Baa2	1	None	None
Corestates Captl Tr II	Single	Preferred Stock	921	619	(302)	Baa1	1	None	None
Chase Cap VI JPM	Single	Preferred Stock	955	779	(176)	A2	1	None	None
Fleet Cap Tr V	Single	Preferred Stock	970	732	(238)	Baa3	1	None	None
			$ 5,868	$ 4,193	$ (1,675)				

The following table provides additional detail about private label mortgage-backed securities as of June 30, 2010:

Private Label Mortgage Backed Securities
June 30, 2010

(Dollars in thousands)

Decscription	Orgination Date	Amortized Cost	Fair Value	Gross Unrealized Gain (Loss)	Collateral Type	Current Rating	Credit Support %	OTTI Charges
RALI 2003-QS15 A1	8/1/2003	$ 715	$ 694	$ (21)	ALT A	Aa2	11.29	$ -
RALI 2004-QS4 A7	3/1/2004	666	652	(14)	ALT A	AAA	13.03	-
MALT 2004-6 7A1	6/1/2004	780	650	(130)	ALT A	AAA	10.52	-
RALI 2005-QS2 A1	2/1/2005	730	608	(121)	ALT A	B	7.70	-
RALI 2006-QS4 A2	4/1/2006	1,044	756	(288)	ALT A	Caa2	0.68	142
GSR 2006-5F	5/1/2006	544	479	(65)	Prime	CCC	4.64	-

2A1								
RALI 2006-QS8 A1	7/28/2006	572	426	(146)	ALT A	Caa2	0.00	113
		$ 5,051	$ 4,265	$ (786)				$ 255

For more information concerning investments, refer to the Investment Securities discussion in the Financial Condition section.

Note 6 – Pensions

The components of pension expense for the periods presented are as follows:

	Three months ended June 30		Six months ended June 30	
(Amounts in thousands)	2010	2009	2010	2009
Components of net periodic (benefit) cost:				
Service cost	$ 91	$ 85	$ 183	$ 170
Interest cost	185	181	371	362
Expected return on plan assets	(209)	(190)	(419)	(380)
Amortization of prior service cost	-	(31)	-	(62)
Recognized net actuarial loss	43	82	86	165
Net periodic cost	$ 110	$ 127	$ 221	$ 255

The Bank expects its pension expense to decrease slightly in 2010 compared to 2009. The Bank expects to contribute $626 thousand to its pension plan in 2010. This amount will meet the minimum funding requirements.

Note 7 – Mortgage Servicing Rights

Activity pertaining to mortgage servicing rights and the related valuation allowance follows:

	Six Months Ended June 30	
(Amounts in thousands)	2010	2009
Cost of mortgage servicing rights:		
Beginning balance	$ 1,190	$ 1,551
Originations	10	3
Amortization	(134)	(214)
Ending balance	$ 1,066	$ 1,340
Valuation allowance:		
Beginning balance	$ (476)	$ (689)
Valuation charges	-	-
Valuation reversals	60	143
Ending balance	$ (416)	$ (546)
Mortgage servicing rights cost	$ 1,066	$ 1,340
Valuation allowance	(416)	(546)
Carrying value	$ 650	$ 794
Fair value	$ 650	$ 794

Note 8 – Fair Value Measurements

Management uses its best judgment in estimating the fair value of the Corporation’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 Corporation could have realized in a sales transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective quarter-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 quarter-end.

FASB ASC Topic 825, Financial Instruments, requires disclosure of the fair value of financial assets and liabilities, including those financial assets and liabilities that are not measured and reported at fair value on a recurring and non-recurring basis.

The estimated fair value of the Corporation's financial instruments are as follows: