

FORM 10-Q
UNITED STATES
FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON, D.C. 20329-9900

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

For the quarterly period ended September 30, 2009

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

For the transition period from _____ to _____

FDIC Certificate No.: 58072

USA Bank

(Exact name of registrant as specified in its charter)

New York

(State or other jurisdiction of incorporation
or organization)

20-0646362

(I.R.S. Employer
Identification No.)

601 North Main Street, Port Chester, New York 10573

(Address of principal executive offices)
(Zip Code)

(914) 939-3700

(Registrant's telephone number, including area code)

N/A

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 No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act): Yes No

As of November 18, 2009, 5,750,000 shares of the Issuer's common stock, \$2.00 par value, were outstanding.

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PART I
Financial Information

Item 1. Consolidated Financial Statements

USA BANK
CONSOLIDATED BALANCE SHEETS
September 30, 2009 and December 31, 2008 (unaudited)

	<u>September 30,</u> <u>2009</u>	<u>December 31,</u> <u>2008</u>
ASSETS		
Cash and due from banks	\$ 2,416,761	\$ 1,286,237
Federal funds sold and overnight investments	13,838,996	10,629,616
Cash and cash equivalents	<u>16,255,757</u>	<u>11,915,853</u>
Held to maturity securities, at amortized cost (fair value \$893,989 in 2009 and \$1,181,876 in 2008)	856,380	1,146,972
Available for sale securities, at fair value	<u>37,416,087</u>	<u>40,877,380</u>
Total investment securities	<u>38,272,467</u>	<u>42,024,352</u>
Loans, net of the allowance for loan losses of \$7,154,000 in 2009 and \$2,044,000 in 2008	164,588,678	151,013,117
Leasehold improvements and equipment, net	609,492	691,560
Other real estate owned	1,995,000	2,370,250
Accrued interest receivable	1,245,143	1,638,089
Other assets	188,739	279,585
Total assets	<u><u>\$ 223,155,276</u></u>	<u><u>\$ 209,932,806</u></u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Deposits		
Noninterest-bearing deposits	\$ 5,776,698	\$ 8,435,324
Interest-bearing deposits	<u>183,381,135</u>	<u>161,332,857</u>
Total deposits	<u>189,157,833</u>	<u>169,768,181</u>
Securities sold under repurchase agreements	23,000,000	23,000,000
Accrued expenses and other liabilities	<u>1,148,256</u>	<u>1,030,820</u>
Total liabilities	<u>213,306,089</u>	<u>193,799,001</u>
Commitments and Contingencies		
Shareholders' Equity		
Common stock, par value \$2; 5,750,000 shares authorized, issued and outstanding at September 30, 2009, and December 31, 2008	11,500,000	11,500,000
Additional paid-in capital	21,116,774	21,116,774
Accumulated other comprehensive loss:	(21,882,200)	(13,026,070)
Net unrealized gain (loss) on available for sale securities	315,208	(3,456,899)
Noncredit portion of other-than-temporary impairment losses on available for sale securities	<u>(1,200,595)</u>	<u>—</u>
Total shareholders' equity	<u>9,849,187</u>	<u>16,133,805</u>
Total liabilities and shareholders' equity	<u><u>\$ 223,155,276</u></u>	<u><u>\$ 209,932,806</u></u>

See Accompanying Notes to Consolidated Financial Statements

USA BANK
CONSOLIDATED STATEMENTS OF OPERATIONS
For the Three and Nine Months Ended September 30, 2009 and 2008 (unaudited)

	Three Months Ended		Nine Months Ended September 30,	
	2009	2008	2009	2008
Interest Income				
Interest on Federal funds sold and overnight investments	\$ 3,232	\$ 40,685	\$ 13,953	\$ 178,647
Interest on interest-bearing deposits	-	108	-	114,415
Interest and fees on loans	2,387,084	2,700,140	7,635,539	7,538,544
Interest on investments	494,456	495,431	1,556,797	1,623,936
Interest on loans held for sale	4,070	62,077	11,961	298,751
Total interest income	2,888,842	3,298,441	9,218,250	9,754,293
Interest Expense				
Interest expense on deposits	1,460,660	1,494,108	4,790,452	4,639,835
Interest expense on securities sold under repurchase agreements	266,125	265,650	788,763	791,396
Interest expense on advances	-	-	-	68
Total interest expense	1,726,785	1,759,758	5,579,215	5,431,299
Net interest income	1,162,057	1,538,683	3,639,035	4,322,994
Provision for loan losses	3,714,480	185,030	5,063,114	724,386
Net interest (loss) income after provision for loan losses	(2,552,423)	1,353,653	(1,424,079)	3,598,608
Noninterest Income (loss)				
Total other-than-temporary impairment losses on available for sale securities	(95,868)	-	(3,676,810)	-
Change in impairment losses recognized in accumulated other comprehensive loss	(342,494)	-	1,200,595	-
Net impairment losses on available for sale securities recognized in income (loss)	(438,362)	-	(2,476,215)	-
Gains on sales of securities	660,019	85,565	660,019	401,258
Gains on sales of loans	24,088	8,070	60,067	89,909
Broker fee income	-	4,172	-	68,213
Service charges	24,451	15,806	91,416	51,456
Other	51,000	13,539	99,469	27,058
Total noninterest income (loss)	321,196	127,152	(1,565,244)	637,894
Noninterest Expense				
Salaries and employee benefits	692,887	591,273	2,118,935	2,035,938
Occupancy and equipment	114,535	192,035	365,312	603,632
Professional fees	270,159	208,388	607,065	652,345
Legal	81,208	110,720	302,610	507,077
Commissions	1,613	60,420	9,424	252,937
Contract services	29,729	39,196	94,955	148,753
Printing, stationery and supplies	25,828	14,844	52,737	46,246
Advertising	63,355	44,527	177,547	111,055
Data and item processing	89,825	93,603	277,169	268,150
FDIC Insurance	143,633	88,835	577,559	327,185
Write-down of OREO property	-	-	375,250	-
OREO Expense	41,284	21,969	79,483	31,900
Properties in foreclosure expense	140,569	20,118	288,908	79,445
Other	146,388	113,361	539,853	419,012
Total noninterest expense	1,841,013	1,599,289	5,866,807	5,483,675
Net loss	\$ (4,072,240)	\$ (118,484)	\$ (8,856,130)	\$ (1,247,173)
Basic and diluted loss per share	\$ (0.71)	\$ (0.02)	\$ (1.54)	\$ (0.22)

See Accompanying Notes to Consolidated Financial Statements

USA BANK
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
For the Nine Months Ended September 30, 2009 and 2008 (unaudited)

	Number of Shares	Common Stock	Additional Paid in Capital	Accumulated Deficit	Accumulated Other Comprehensive (Loss) Income	Total
Balance, December 31, 2007	5,750,000	\$11,500,000	\$ 21,116,774	\$ (10,334,178)	\$ 26,618	\$ 22,309,214
Comprehensive loss:						
Net loss	-	-	-	(1,247,173)	-	(1,247,173)
Other comprehensive loss:						
Net unrealized (gains) losses on available for sale securities	-	-	-	-	(1,129,121)	(1,129,121)
Total comprehensive loss						(2,376,294)
Balance, September 30, 2008	<u>5,750,000</u>	<u>\$11,500,000</u>	<u>\$ 21,116,774</u>	<u>\$ (11,581,351)</u>	<u>\$ (1,102,503)</u>	<u>\$ 19,932,920</u>
Balance, December 31, 2008	5,750,000	\$11,500,000	\$ 21,116,774	\$ (13,026,070)	\$ (3,456,899)	\$ 16,133,805
Comprehensive loss:						
Net loss	-	-	-	(8,856,130)	-	(8,856,130)
Other comprehensive loss:						
Unrealized holding gain on available for sale securities	-	-	-	-	2,571,512	2,571,512
Total comprehensive loss						(6,284,618)
Balance, September 30, 2009	<u>5,750,000</u>	<u>\$11,500,000</u>	<u>\$ 21,116,774</u>	<u>\$ (21,882,200)</u>	<u>\$ (885,387)</u>	<u>\$ 9,849,187</u>

See Accompanying Notes to Consolidated Financial Statements

USA BANK
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Nine Months Ended September 30, 2009 and 2008 (unaudited)

	Nine Months Ended September 30,	
	2009	2008
Cash Flows from Operations		
Net loss	\$ (8,856,130)	\$ (1,247,173)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities		
Amortization and accretion of premiums and discounts on investments, net	166,360	(37,116)
Provision for loan losses	5,063,114	724,386
Writedown of OREO property	375,250	-
Other-than-temporary impairment losses recognized in earnings	2,476,215	-
Gain on sale of available for sale securities	(660,019)	(401,258)
Loans originated for sale, net of principal payments received	(7,074,300)	(4,360,057)
Proceeds from sales of loans	7,134,367	6,240,259
Net gains on sales of loans	(60,067)	(89,909)
Depreciation and amortization	149,984	164,244
Changes in assets and liabilities:		
Increase in deferred loan fees	29,128	88,485
Decrease (increase) in accrued interest receivable	392,946	(451,761)
Increase in other assets	90,846	75,184
Increase (decrease) in accrued expenses and other liabilities	117,436	(406,897)
Net cash (used in) provided by operating activities	(654,870)	298,387
Cash Flows from Investing Activities		
Proceeds from maturity of interest-bearing deposit	-	4,835,943
Purchase of available for sale securities	(28,102,085)	(23,796,959)
Proceeds from sale of available for sale securities	19,351,845	23,312,065
Proceeds from call of available for sale securities	3,900,000	-
Principal repayments on available for sale securities	8,895,653	2,903,920
Principal repayments of held to maturity securities	295,428	213,178
Net increase in loans receivable	(18,667,803)	(44,765,859)
Purchase of leasehold improvements and equipment	(67,916)	(45,956)
Net cash used in investing activities	(14,394,878)	(37,343,668)
Cash Flows from Financing Activities		
Net (decrease) increase in time deposits	(5,311,949)	18,801,141
Net increase in other deposits	24,701,601	10,213,830
Net cash provided by financing activities	19,389,652	29,014,971
Net increase (decrease) in cash and cash equivalents	4,339,904	(8,030,310)
Cash and cash equivalents		
Beginning	11,915,853	10,955,671
Ending	\$ 16,255,757	\$ 2,925,361
Supplemental Disclosure of Cash Flow Information		
Cash paid for:		
Interest	\$ 5,761,549	\$ 5,648,900
Supplemental disclosure of noncash investing activities:		
Net unrealized gains (losses) on available for sale securities arising during the period	\$ 2,571,512	\$ (1,129,121)
Transfer of loans held for sale to loans receivable	\$ -	\$ 479,013
Transfer of loans to other real estate owned	\$ -	\$ 2,370,250

See Accompanying Notes to Consolidated Financial Statements

USA Bank
Notes to Consolidated Financial Statements
(Unaudited)

Note 1. Nature of Operations

USA Bank (the “*Bank*”) is a State of New York chartered commercial bank whose deposits are insured by the Federal Deposit Insurance Corporation (“*FDIC*”). The Bank is headquartered in Port Chester, New York, and offers traditional commercial banking deposit services to residents from its “primary market area” of Port Chester, Rye, and Rye Brook, New York, and also attracts loan customers from its primary market area and other towns in Westchester County, New York, and lower Fairfield County, Connecticut.

The Bank’s overall strategy is to provide highly personal, customized and responsive service in the delivery of banking services to businesses and individuals located in the primary market area. The Bank’s main branch is located at 601 North Main Street, Port Chester, NY. The Bank also leases additional space in Greenwich, CT, for general administrative purposes.

Note 2. Significant Risks and Uncertainties

The continued recessionary forces in the national and local economies in general and the local real estate markets, in particular, have had a significant adverse impact on the Bank’s financial condition and results of operations. As reported in the accompanying consolidated financial statements, the Bank has incurred a net loss of \$4,072,000 during the three months ended September 30, 2009 and a net loss of \$8,856,000 for the nine months ended September 30, 2009. Stockholders’ equity decreased from \$16,134,000 or 7.69% of total assets at December 31, 2008 to \$9,849,000 or 4.41% of total assets at September 30, 2009.

The losses for the three month and nine month periods ended September 30, 2009 originate from other-than-temporary impairment charges on four private label collateralized mortgage obligations, provision for loan losses and an increase in nonperforming loans which has reduced the Bank’s interest income. The Bank’s net interest income will continue to be negatively impacted by the level of nonperforming loans and the Bank expects additional losses for the remainder of the year. As a result of the losses, the Bank is deemed to be undercapitalized as of September 30, 2009 under the total risk-based capital ratio standard. Non-accrual loans totaled \$9.0 million, \$9.7 million, \$21.0 million and \$40.6 million at December 31, 2008, March 31, 2009, June 30, 2009 and September 30, 2009, respectively. Nonperforming loans totaled \$55.0 million and \$9.7 million at September 30, 2009 and December 31, 2008, respectively. Total impaired loans were \$40.6 million and \$9.0 million at September 30, 2009 and December 30, 2008, respectively. While the Bank has devoted and will continue to devote substantial management resources toward the resolution of delinquent, impaired and non-accrual loans, no assurance can be made that management’s efforts will be successful.

The Bank’s loan portfolio has a high concentration of construction loans which reached \$80.8 million (47% of total gross loans) at September 30, 2009. When the construction loans were made, they had loan-to-value ratios of 60% or less; however, with the current slowdown in the economy and sales of new homes in the local market area, the property values have generally

declined and the holding period for the developers has expanded beyond what some of them can afford. This has resulted in the Bank being forced to foreclose on certain properties and/or negotiate revised terms with certain of the developers.

These conditions create an uncertainty about material adverse consequences that may occur in the near term. Management of the Bank has taken certain steps in an effort to eliminate or limit any material adverse consequences, such as cost control, income enhancement measures and problem asset management. Within the past few months in order to reduce lending exposure the Bank has lowered loan to value ratios on new loan originations. In addition, on July 13, 2009, in an effort to further reduce its lending exposure, the board of directors adopted a resolution that the Bank not enter into any additional commercial construction loan or speculative construction loans unless the Board or the Loan Committee determines that an extension of additional credit to such borrowers is required under existing loan documents or is reasonably necessary to promote the best interest of the Bank. And prior to renewing or extending any commercial construction or speculative construction loan, a majority of the full Board or the Loan Committee must approve the credit renewal or extension and document why such extension is appropriate to promote the best interest of the Bank.

With the deterioration in total risk-based capital ratio from well capitalized to undercapitalized, the Bank is now in a position that makes it necessary to raise additional capital. The Bank has retained the services of Laidlaw and Company (UK), Ltd., which, after its review of the Bank, has recommended, as disclosed in a November 6, 2009 press release, that the Bank pursue a transaction with either a strategic or financial partner to provide additional capital to take advantage of the strong demographics of the communities it serves. To that end the Bank has authorized Laidlaw to commence efforts to identify a partner for the Bank and to assist in the consummation of such a transaction.

Note 3. Basis of Consolidated Financial Statement Presentation

The Consolidated Balance Sheet at December 31, 2008 has been derived from the audited financial statements of the Bank at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. The interim consolidated financial statements and notes thereto include the accounts of the Bank and its wholly-owned subsidiary, USA MBA, Inc., a Connecticut-based mortgage brokerage company, which is inactive. All significant intercompany balances and transactions have been eliminated in consolidation. The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and general practices within the banking industry and with the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted. In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities as of the dates of the balance sheets and the reported amounts of income and expenses for the reporting periods. Amounts in prior period financial statements are reclassified whenever necessary to conform to current period presentations. The information furnished reflects, in the opinion of management, all normal

recurring adjustments necessary for a fair presentation of the results for the interim periods presented. The results of operations for the three months and nine months ended September 30, 2009, are not necessarily indicative of the results which may be expected for the year as a whole. The accompanying consolidated financial statements and notes thereto should be read in conjunction with the audited consolidated financial statements of the Bank and notes thereto as of December 31, 2008, filed with the FDIC on Form 10-K on April 15, 2009.

In May 2009, the Financial Accounting Standards Board (“FASB”) issued a new standard entitled Subsequent Events. This statement provides guidance on principles and requirements for subsequent events. The guidance sets forth: 1) the period after the balance sheet date during which management of a reporting entity shall evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements; 2) the circumstances under which an entity shall recognize events or transactions occurring after the balance sheet date in its financial statements; and 3) the disclosures that an entity shall make about events or transactions that occurred after the balance sheet date. Two types of subsequent events require consideration by management: (a) recognized subsequent events; and (b) non-recognized subsequent events. Recognized subsequent events consist of those events or transactions that provide additional evidence with respect to conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Non-recognized subsequent events consist of those events that provide evidence with respect to conditions that did not exist at the date of the balance sheet, but arose subsequent to that date. This statement is effective for interim or annual financial periods after June 15, 2009. The Bank has evaluated the subsequent events through November 18, 2009. No material subsequent events have occurred since September 30, 2009 that required recognition or disclosure in these financial statements.

Note 4. Recent Accounting Pronouncements

In February 2008, the FASB issued a staff position which permitted a one-year deferral for the implementation of *Fair Value Measurements* with regard to nonfinancial assets and liabilities that are not recognized or disclosed at fair value in the financial statements on a recurring basis. This staff position was effective as of January 1, 2009. The adoption of this staff position did not have a material impact on the Bank’s consolidated financial statements. See Note 15 for additional information regarding fair value.

In April 2009, the FASB issued a staff position entitled “*Determining Fair Value When the Volume and Level of Activity for the Asset and Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly.*” This staff position provided additional guidance on: (a) determining when the volume and level of activity for the asset and liability has significantly decreased; (b) identifying circumstances in which a transaction is not orderly; and (c) understanding the fair value measurement implications in both (a) and (b). The Bank adopted this guidance during the quarter ended June 30, 2009. See Note 15 for additional information regarding fair value measurement.

In April 2009, the FASB issued a new staff position entitled “*Recognition and Presentation of Other-Than-Temporary Impairments.*” This staff position amends the other-than-temporary impairment guidance for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments in the

financial statements. The most significant change the staff position brings is a revision to the amount of other-than-temporary loss of a debt security recorded in earnings. The Bank adopted this staff position during the quarter ended June 30, 2009 and recorded a credit-related impairment loss of \$2.1 million related to private label mortgage-backed securities. The Bank recognized an other-than-temporary impairment loss in earnings of \$2.5 million for the nine months ended September 30, 2009 relating to the credit portion of the total unrealized loss of \$3.7 million as of September 30, 2009. See Note 5 for additional information regarding this recognition.

In April 2009, the FASB issued a new staff position entitled “*Interim Disclosures about Fair Value of Financial Instruments.*” This staff position requires disclosures about fair value instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. This staff position also requires those disclosures in summarized financial information at interim reporting periods. The Bank adopted this staff position during the quarter ended June 30, 2009. See Note 15 for additional information regarding fair value.

In January 2009, the FASB issued a new staff position which amends the impairment guidance entitled “*Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continue to be Held by a Transferor in Securitized Financial Assets.*” The staff position revises impairment guidance for beneficial interests to make it consistent with the requirements of the FASB statement entitled “*Accounting for Certain Investments in Debt and Equity Securities*” for determining whether an impairment of other debt and equity securities has occurred. The impairment model in this statement enables greater judgment to be exercised in determining whether an other-than-temporary impairment needs to be recorded. The impairment model previously provided for in the guidance limited management’s use of judgment in applying the impairment model. This staff position was effective as of January 1, 2009. The adoption of this staff position did not have a material impact on the Bank’s consolidated financial statements.

In June 2009, the FASB issued a new standard entitled “*Accounting for Transfers of Financial Assets – an amendment of FASB Statement No. 140.*” The objective of this standard is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor’s continuing involvement, if any, in transferred financial assets. Additionally, on and after the effective date, the concept of a qualifying special-purpose entity is no longer relevant for accounting purposes. Therefore, formerly qualifying special-purpose entities (as defined under previous accounting standards) should be evaluated for consolidation by reporting entities on and after the effective date in accordance with the applicable consolidation guidance. If the evaluation on the effective date results in consolidation, the reporting entity should apply the transition guidance provided in the pronouncement that requires consolidation. This standard must be applied as of the beginning of each reporting entity’s first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application is prohibited. This standard must be applied to transfers occurring on or after the effective date. The adoption of this standard is not expected to have a material impact on the Bank’s consolidated financial statements.

In June 2009, the FASB issued a new standard entitled “*The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles – a replacement of FASB Statement No. 162*” to allow the FASB Codification to be the single source of authoritative U.S. accounting and reporting standards, other than guidance issued by the Securities and Exchange Commission. The Bank adopted this standard during the quarter ended September 30, 2009. The adoption of this standard did not have a material impact on the Bank’s consolidated financial statements.

Note 5. Investments

The amortized cost, gross unrealized gains, gross unrealized losses and approximate fair values of available for sale and held to maturity securities at September 30, 2009, and December 31, 2008, are as follows:

September 30, 2009

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities				
Mortgage-backed securities	\$ 38,301,474	\$ 407,548	\$ (1,292,935)	\$ 37,416,087
Held to maturity securities				
Mortgage-backed securities	\$ 856,380	\$ 37,609	\$ –	\$ 893,989

December 31, 2008

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities				
U.S. Government Sponsored Agencies	\$ 3,900,000	\$ 4,875	\$ –	\$ 3,904,875
Mortgage-backed securities	40,434,279	516,655	(3,978,429)	36,972,505
Total available for sale	\$ 44,334,279	\$ 521,530	\$ (3,978,429)	\$ 40,877,380
Held to maturity securities				
Mortgage-backed securities	\$ 1,146,972	\$ 34,904	\$ –	\$ 1,181,876

Management evaluates securities for other-than-temporary impairment (“*OTTP*”) at least on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. All of the Bank’s investment securities classified as available for sale or held to maturity are evaluated for OTTI under FASB Accounting Standards Codification (“*ASC*”) 320-10-35 – Investments – *Debt and Equity Securities – Overall – Subsequent Measurement*.

In determining OTTI, management considers many factors, including:

1. The length of time and the extent to which the fair value has been less than the amortized cost basis;
2. Adverse conditions specifically related to the security, an industry, or a geographic area (e.g., changes in condition of the issuer or underlying loan obligations);
3. The historical and implied volatility of the fair value of the security;

4. The payment structure of the debt security and the likelihood of the issuer's being able to make payments that increase in the future;
5. Failure of the issuer of the security to make scheduled interest or principal payments;
6. Any changes to the rating of the security by a rating agency;
7. Recoveries or additional declines in fair value subsequent to the balance sheet date; and
8. The strength of the government sponsored enterprises' guarantees of the holdings of agency mortgage-backed securities.

The relative importance of this information varies based on the facts and circumstances surrounding the security, as well as the economic environment at the time of assessment. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on information available to management at a point in time. An OTTI loss is deemed to have occurred if there has been an adverse change in the remaining expected future cash flows.

When an OTTI loss occurs under the ASC 320-10-35 model, the amount of the OTTI loss recognized in earnings depends on whether the Bank intends to sell the security or whether it is more likely than not that the Bank will be required to sell the security before recovery of its amortized cost basis less any current period credit loss. If the Bank intends to sell, or more likely than not will be required to sell, the security before recovery of its amortized cost basis less any current period credit loss, the OTTI loss is recognized in earnings equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. If the Bank does not intend to sell the security, and it is not more likely than not that the Bank will be required to sell the security before recovery of its amortized cost basis less any current period loss, the OTTI loss is separated into the amount representing the credit loss and the amount related to all other factors. The amount of total OTTI related to the credit loss is determined based on the present value of cash flows expected to be collected discounted at the original effective yield, and is recognized in earnings. The amount of the total OTTI related to other factors is recognized in other comprehensive income, net of the applicable tax benefit. The previous amortized cost basis less the OTTI loss recognized in earnings becomes the new amortized cost basis of the investment. As of September 30, 2009, the Bank's securities portfolio consisted of 19 securities, of which 8 were in an unrealized loss position. The majority of unrealized losses are related to the Bank's four non-agency collateralized mortgage obligations, which were purchased during the second quarter of 2007, as discussed below.

Non-Agency Collateralized Mortgage Obligations

At September 30, 2009, approximately \$7.1 million (based on amortized cost before impairment charges), or 100%, of the Bank's non-agency collateralized mortgage obligations were rated below investment grade by at least one of the nationally-recognized rating agencies. The aggregate unrealized loss on these securities totaled \$3.7 million before measurement and/or recognition of any OTTI loss. The Bank does not intend to sell these securities, and the Bank further believes that it is not more likely than not that it will be required to sell the securities before recovery of its amortized cost basis. However, due to the explicit credit risk involved

with these non-U.S. government agency securities, the Bank evaluated the impairment to determine if it could expect to recover the entire amortized cost basis of each security. The OTTI evaluation was based on the estimated cash flow projections of the underlying loans collateralizing each security utilizing projected rates of voluntary prepayment and default and the projected loss severities upon liquidation of the defaults. Loss severities are based on the estimated changes in housing prices since inception of the loan and forecasted changes in housing prices over the near- and long-term.

Key assumptions utilized in the evaluation were as follows:

- Prepayment rates – running at a range of 10.28% to 12.27%.
- Default rates – liquidation of 100% of each security’s current real estate owned (“*REO*”) balances, liquidation of 87% to 95% of current foreclosure balances and 90-day delinquent balances, liquidation of 69% to 72% of the 60- to 89-day delinquent balances, and liquidation of 51% to 55% of the 30- to 59-day delinquencies linearly over the next 24 months. Default rates are then ramped to a range of 1.29% to 2.27% beginning in month 37 and are further ramped to a 0% terminal default rate linearly over a period ranging from 164 to 179 months following month 36.
- Loss severities – are initially set at the recent rate being incurred which ranges from 48% to 50%. Severities are adjusted to reflect expected changes in housing prices in 2009 and 2010. Housing prices are then modeled to increase at 3.5% per year resulting in a terminal loss severity of 23% ranging from month 99 to month 105.

The estimated cash flows were discounted at rates ranging from 5.98% to 6.24% based on the Bank’s expected effective yields in order to determine the credit portion of OTTI.

Based on the Bank’s impairment evaluation, all four of the non-agency collateralized mortgage obligation securities were determined to be other-than-temporarily impaired at September 30, 2009, only two of which had additional credit losses charged to earnings during the three months ended September 30, 2009. Unrealized losses on these securities totaled \$1.3 million at September 30, 2009, and estimated credit related losses totaled \$0.4 million for the three months ended September 30, 2009. Estimated credit losses of \$0.4 million and \$2.5 million were charged to current earnings during the three months and nine months ended September 30, 2009, respectively, and the difference between the total unrealized losses and estimated credit losses, or \$1.3 million, was charged against other comprehensive loss within the equity section of the balance sheet. The estimated credit losses were primarily the result of increases in delinquencies within the mortgages collateralizing the four private label securities both for the three months and nine months ended September 30, 2009. The \$1.3 million noncredit related loss as of September 30, 2009 was due to instability in the marketplace and was not charged to current earnings during the three months and nine months ended September 30, 2009 since the Bank does not intend to sell these securities, and the Bank further believes that it is not more likely than not that it will be required to sell the securities before recovery of its amortized cost basis.

Information pertaining to securities with gross unrealized losses at September 30, 2009 and December 31, 2008 aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	Less Than Twelve Months		Over Twelve Months		Total Unrealized Losses	Total Fair Value
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value		
September 30, 2009						
Mortgage-backed securities	\$ 92,340	\$13,826,849	\$ 1,200,595	\$ 3,506,039	\$ 1,292,935	\$17,332,888
Total	\$ 92,340	\$13,826,849	\$ 1,200,595	\$ 3,506,039	\$ 1,292,935	\$17,332,888
	Less Than Twelve Months	Over Twelve Months	Total Unrealized Losses	Total Fair Value		
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Total Unrealized Losses	Total Fair Value
December 31, 2008						
Mortgage-backed securities	\$ 26,136	\$ 3,050,627	\$ 3,952,293	\$ 3,858,356	\$ 3,978,429	\$ 6,908,983
Total	\$ 26,136	\$ 3,050,627	\$ 3,952,293	\$ 3,858,356	\$ 3,978,429	\$ 6,908,983

At September 30, 2009, gross unrealized losses on eight available for sale securities totaled \$1,292,935, an aggregate depreciation of 6.94% from the Bank's amortized cost, which amortized cost includes recognition of cumulative OTTI credit losses of \$2.9 million. Four of these securities are private label whole loan collateralized mortgage obligations ("CMOs") that have been in an unrealized loss position for twelve consecutive months or longer and are accountable for \$1,200,595 (93%) of the total \$1,292,935 gross unrealized loss. The four other securities are securities issued by the Government National Mortgage Association ("GNMA", also known as "Ginnie Mae") that are explicitly 100% guaranteed by the U.S. government and have been in a loss position for less than three months.

At December 31, 2008, gross unrealized holding losses on five available for sale securities totaled \$3,978,429, an aggregate depreciation of 36.5% from the Bank's amortized cost. One of these securities was an agency mortgage-backed security with an implied AAA rating which was called during the period ended June 30, 2009. The other four securities were the private label whole loan CMOs referred to above, which were all rated AAA by Fitch at December 31, 2008. Standard & Poor's (S&P) had downgraded two of these four securities from an AAA rating to an A and BB rating during the fourth quarter of 2008, leaving the other two unchanged at AAA as of December 31, 2008. The unrealized losses on the four private label whole loan CMOs totaled \$3,952,000, and the securities had a fair value of \$3,858,000 at December 31, 2008. At December 31, 2008, these four securities had been in an unrealized loss position for twelve consecutive months or longer; however, they were not considered other-than-temporarily impaired at that time.

The amortized cost and fair value of held to maturity and available for sale debt securities at September 30, 2009 are presented below. Actual maturities of mortgage-backed securities may differ from contractual maturities because the mortgages underlying the securities may be called or repaid without any penalties. Because mortgage-backed securities are not due at a single maturity date, contractual maturity information for such securities is not included in the following summary:

	<u>Amortized Cost</u>	<u>Fair Value</u>
Held to maturity		
Mortgage-backed securities	<u>\$ 856,380</u>	<u>\$ 893,989</u>
Available for sale		
Mortgage-backed securities	<u>\$ 38,301,474</u>	<u>\$ 37,416,087</u>

At September 30, 2009, \$22.9 million of the available for sale securities and the \$0.9 million of held to maturity securities have been pledged as collateral for municipal deposits and securities sold under agreements to repurchase. There were sales of \$18.7 million of investment securities during the three months and nine months ended September 30, 2009, which resulted in gains of \$660,000 for the three and nine months ended September 30, 2009, whereas there were sales of \$4.3 million and \$22.9 million of investment securities during the three months and nine months ended September 30, 2008, respectively, which resulted in gains of \$86,000 and \$401,000, respectively.

The following table displays the Bank's securities for which an other-than-temporary impairment was recognized based on the Bank's impairment analysis of its investment portfolio at September 30, 2009:

	<u>At September 30, 2009</u>			
	<u>Par Value</u>	<u>Amortized Cost</u>	<u>Gross Unrealized Loss</u>	<u>Fair Value</u>
Other-than-temporarily impaired investments				
Private-label MBS	<u>\$8,678,000</u>	<u>\$7,182,849</u>	<u>\$(3,676,810)</u>	<u>\$3,506,039</u>
Total other-than-temporarily impaired securities	<u>\$8,678,000</u>	<u>\$7,182,849</u>	<u>\$(3,676,810)</u>	<u>\$3,506,039</u>

	For the Three Months Ended September 30, 2009			For the Nine Months Ended September 30, 2009		
	<u>Other-Than-Temporary Impairment Related to Credit Loss</u>	<u>Change in Impairment Losses Related to Non-Credit Loss</u>	<u>Total Impairment Loss</u>	<u>Other-Than-Temporary Impairment Related to Credit Loss</u>	<u>Other-Than-Temporary Impairment Related to Non-Credit Loss</u>	<u>Total Impairment Loss</u>
Other-than-temporarily impaired investments						
Private-label MBS	\$ (438,362)	\$ 342,494	\$ (95,868)	\$ (2,476,215)	\$ (1,200,595)	\$ (3,676,810)
Total other-than-temporarily impaired securities	<u>\$ (438,362)</u>	<u>\$ 342,494</u>	<u>\$ (95,868)</u>	<u>\$ (2,476,215)</u>	<u>\$ (1,200,595)</u>	<u>\$ (3,676,810)</u>

During the three months and nine months ended September 30, 2008, there were no securities for which an OTTI loss was recognized.

The following table presents a roll forward of the amounts related to credit losses recognized into earnings. The roll forward relates to the amount of credit losses on investment securities held by the Bank for which a portion of an other-than-temporary impairment charge was recognized into accumulated other comprehensive loss.

	For the Three Months Ended September 30, 2009	For the Nine Months Ended September 30, 2009
Balance as of beginning of period	\$ 2,307,853	\$ —
Additions for the amount related to the credit loss for which other-than-temporary impairment was not previously recognized	<u>438,362</u>	<u>2,476,215</u>
Balance as of September 30, 2009	<u>\$ 2,476,215</u>	<u>\$ 2,476,215</u>

Note 6. Loans and Allowance for Loan Losses

A summary of the Bank's loan portfolio at September 30, 2009, and December 31, 2008, is as follows:

	<u>September 30, 2009</u>	<u>% of Total Portfolio</u>	<u>December 31, 2008</u>	<u>% of Total Portfolio</u>
Real estate loans				
Residential mortgages	\$ 12,754,192	7.42%	\$ 11,650,804	7.60%
Commercial real estate	41,087,745	23.89%	35,378,954	23.08%
Construction	80,795,226	46.98%	75,649,779	49.36%
Home equity	14,463,188	8.41%	13,048,310	8.51%
Total real estate loans	<u>149,100,351</u>	<u>86.70%</u>	<u>135,727,847</u>	<u>88.56%</u>
Commercial and industrial loans	<u>21,707,553</u>	<u>12.62%</u>	<u>15,817,596</u>	<u>10.32%</u>
Consumer loans	<u>1,170,247</u>	<u>0.68%</u>	<u>1,718,019</u>	<u>1.12%</u>
Total gross loans	<u>171,978,151</u>	<u>100.00%</u>	<u>153,263,462</u>	<u>100.00%</u>
Deferred loan fees	(235,473)		(206,345)	
Allowance for loan losses	<u>(7,154,000)</u>		<u>(2,044,000)</u>	
Loans receivable, net	<u>\$ 164,588,678</u>		<u>\$ 151,013,117</u>	

In the normal course of business, the Bank may grant loans to executive officers, directors and members of their immediate families, as defined, and to entities in which these individuals have more than a 10% equity ownership. Such loans are transacted at terms including interest rates, substantially the same as those available to unrelated customers.

Allowance for Loan Losses

The following represents the activity in the allowance for loan losses for the nine months ended September 30, 2009, and September 30, 2008:

	<u>September 30, 2009</u>	<u>September 30, 2008</u>
Balance at beginning of period	\$ 2,044,000	\$ 1,421,000
Provision for loan losses	5,063,114	724,386
Charge-offs	(5,004)	(283,386)
Recoveries	51,890	-
Balance at end of period	<u>\$ 7,154,000</u>	<u>\$ 1,862,000</u>

Non-Accrual, Past Due and Restructured Loans

The following is a summary of non-accrual and past due loans at September 30, 2009 and December 31, 2008:

	<u>September 30, 2009</u>	<u>December 31, 2008</u>
Loans delinquent over 90 days and still accruing	\$ 14,368,658	\$ 664,884
Non-accrual loans	<u>40,616,792</u>	<u>9,046,113</u>
Total nonperforming loans	<u>\$ 54,985,450</u>	<u>\$ 9,710,997</u>
% of Total Loans	31.97%	6.34%
% of Total Assets	29.42%	4.63%
Ratio of allowance for loan losses to nonperforming loans	13.01%	21.05%

The following information relates to impaired loans as of and for the nine months ended September 30, 2009 and the year ended December 31, 2008:

	<u>2009</u>	<u>2008</u>
Impaired loans for which there is a specific allowance	\$ 22,856,060	\$ 2,200,000
Impaired loans for which there is no specific allowance	\$ 17,760,732	\$ 6,846,113
Specific allowance related to impaired loans	\$ 2,917,258	\$ 141,540
Average recorded investment in impaired loans	\$ 15,422,094	\$ 4,372,214

Interest income collected and recognized on impaired loans was \$37,754 and \$9,524 during the nine months ended September 30, 2009 and year ended December 31, 2008, respectively. If impaired loans had been current throughout their terms, additional interest of \$746,676 and \$1,599,844 would have been recognized during the three- and nine-month periods ended September 30, 2009, respectively. For the year 2008, an additional \$426,110 would have been recognized. The Bank has no commitments to lend additional funds to borrowers whose loans are impaired, except for construction loans on a selective basis.

Construction loans comprise \$27.6 million (68.1%) of the \$40.6 million in non-accrual loans at September 30, 2009, for which a specific reserve of \$721,000 has been recorded. This is an increase of \$23.2 million from the \$4.4 million of non-accrual construction loans at December 31, 2008 for which no specific reserve was recorded. In most cases, and based on the strength of the borrower, the Bank requires the establishment of interest reserve accounts that are restricted for the initial term of construction loans. Approved interest reserve amounts on construction loans outstanding aggregated \$6.5 million at December 31, 2008, of which approximately \$3.5 million were held in restricted accounts. At September 30, 2009, approximately \$1.1 million in reserve balances were held in restricted accounts. At September 30, 2009, two of the non-accrual construction loans had restricted interest reserve balances totaling \$45,000. At December 31, 2008 there were no balances in restricted interest reserve accounts related to impaired construction loans.

The Bank's lending activities are conducted principally within 90 miles of its offices in Port Chester, NY, which includes Westchester County, New York, and Fairfield County, Connecticut. The Bank grants commercial and residential real estate loans, commercial business loans and a variety of consumer loans. In addition, the Bank may grant loans for the construction of residential homes, residential developments and for land development projects. All residential and commercial mortgage loans are collateralized by first or second mortgages on real estate. The ability and willingness of borrowers to satisfy their loan obligations is dependent in large part upon the status of the regional economy and regional real estate market. Accordingly, the ultimate collectibility of a substantial portion of the loan portfolio and the recovery of a substantial portion of any resulting real estate acquired is susceptible to changes in market conditions.

The Bank has established credit policies applicable to each type of lending activity in which it engages, evaluates the creditworthiness of each customer on an individual basis and, in most cases, extends credit of up to 65% of the market value of the collateral at the date of the

credit extension depending upon the Bank's evaluation of the borrower's credit worthiness and type of collateral. Collateral varies by each borrower and loan type. The market value of collateral is monitored on an ongoing basis and additional collateral is obtained when warranted. Important types of collateral include business assets, real estate, marketable securities and time deposits. While collateral provides assurance as a secondary source of repayment, the Bank ordinarily requires the primary source of repayment to be based on the borrower's ability to generate continuing cash flows.

The Bank had one loan considered a "troubled debt restructuring" as of September 30, 2009 and December 31, 2008 (see further discussion below), in the amount of \$1.4 million which is included in non-accrual loans.

On July 16, 2008, the Bank entered into a forbearance agreement, which restructured two loans totaling \$1.9 million with one borrower. The agreement covers the period from August 1, 2008, through June 1, 2010. Under the terms of the agreement, the borrower agreed to pay to the Bank an increased interest rate on the principal balance outstanding and assigned rental payments of \$6,800 per month from one of the collateral properties through the term of the agreement. The borrower also agreed that the due date for final payment will be the earlier of the date of sale or refinancing of the premises or June 30, 2010. Based on appraisals dated August 20, 2008, the Bank established a specific reserve of \$139,000 during the third quarter of 2008 within the allowance for loan losses, while the net realizable value of the collateral on the other loan was determined to be sufficient to enable the Bank to collect the balance due.

During the fourth quarter of 2008, the borrower went into arrears on the forbearance agreement. A more recent appraisal on one of the properties, in which the Bank was in a second position, resulted in no value in the collateral available to the Bank and that loan was charged-off in the amount of \$479,000. The other property was placed on non-accrual status and the net realizable value of the collateral on that property is in excess of the outstanding loan balance; therefore, no specific allowance was established for the loan.

Potential Problem Loans

In addition to loans that have been identified as non-accrual or past due 90 days and still accruing at September 30, 2009, the Bank has 6 loans comprising \$12.6 million that management has doubts as to the borrower's ability to comply with the present repayment terms. These loans were identified based upon an analysis of the loan type, collateral and the borrower / guarantor.

The growth of impaired loans in the Bank's loan portfolio is attributable to the decline in real estate values in the principal markets in which the Bank conducts business, coupled with a reduction in the ability of certain borrowers to refinance or repay their obligations. The real estate market for speculative luxury dwellings, that comprise the bulk of the construction portfolio, continues to manifest little sales activity. Both buyers and sellers are frozen and waiting for some indication the market has bottomed out prior to making a bid or accepting an offer.

The Bank's lending department is devoting its resources to managing the loan portfolio until such time as delinquent loans are reduced to a reasonable level. Loan modification and/or restructuring, the principal tool for managing an impaired loan, requires extensive negotiations

with borrowers concerning the loan terms, and new appraisals must be obtained in a declining real estate market, which frequently results in higher LTV's compared to the original underwriting. Consequently, less flexibility is available in advancing new funds for unfinished construction projects incurring cost overruns.

A workout consultant has been hired to assist in modifying and extending loans. The consultant is working full-time and has been assigned specific loans to modify and to negotiate an extension on terms that mitigate the risk of borrower default and ensure repayment of all amounts due the Bank, subject to the approval of the Loan Committee of the Board of Directors on behalf of the Bank. Additionally, a full-time collections clerk has been hired to assist in the collection of delinquent loans.

Note 7. Other Real Estate Owned

Other real estate owned (“*OREO*”) represents the estimated net realizable value of real estate received in satisfaction of a non-performing loan through foreclosure proceedings in June 2008.

A summary of other real estate owned operations for the nine months ended September 30, 2009 and 2008 is as follows:

	<u>2009</u>	<u>2008</u>
Expenses of holding other real estate owned	\$ 79,483	\$ 31,900
Write-down of other real estate owned property	375,250	-
Expense from other real estate owned operations, net	<u>\$ 454,733</u>	<u>\$ 31,900</u>

Note 8. Deposits

At September 30, 2009, and December 31, 2008, deposits consisted of the following:

	<u>September 30, 2009</u>	<u>December 31, 2008</u>
Noninterest-bearing checking	\$ 4,732,538	\$ 4,663,132
Noninterest-bearing money market	1,044,160	3,772,192
Total noninterest-bearing deposits	<u>\$ 5,776,698</u>	<u>\$ 8,435,324</u>
Interest-bearing deposits		
Interest-bearing checking	1,581,764	1,748,985
NOW and money market	31,193,756	6,472,161
Savings	13,079,626	10,273,773
Checking, NOW, money market and savings	<u>45,855,146</u>	<u>18,494,919</u>
Time Certificates under \$100,000	47,133,592	55,569,059
Time Certificates over \$100,000	90,392,397	87,268,879
Time deposits	<u>137,525,989</u>	<u>142,837,938</u>
Total interest-bearing deposits	<u>183,381,135</u>	<u>161,332,857</u>
Total deposits	<u>\$ 189,157,833</u>	<u>\$ 169,768,181</u>

Included in time deposits at September 30, 2009, and December 31, 2008, were brokered deposits totaling \$10,413,165 and \$25,863,763, respectively. Brokered deposits at September 30, 2009, and at December 31, 2008, have original maturities of four weeks to five years.

Note 9. Securities Sold Under Agreements to Repurchase

The following table summarizes the securities sold under agreements to repurchase:

Maturity Date	September 30, 2009	December 31, 2008
May 2017	\$ 4,000,000	\$ 4,000,000
July 2017	7,000,000	7,000,000
July 2017	4,000,000	4,000,000
July 2017	4,000,000	4,000,000
July 2017	4,000,000	4,000,000
Total securities sold under agreements to repurchase	\$ 23,000,000	\$ 23,000,000

Securities sold under agreements to repurchase were collateralized by mortgage-backed securities. The weighted average cost of funds on the repurchase agreements at September 30, 2009, and December 31, 2008, was 4.57% and 4.60%, respectively. The amounts outstanding as of September 30, 2009 and December 31, 2008 have original maturities of ten years and are structured to be callable on scheduled dates from six to eighteen months from inception or on a quarterly basis thereafter at the option of the counterparty. The average outstanding balance was \$23.0 million for both the three-month and nine-month periods ended September 30, 2009 and 2008.

Note 10. Available Borrowings

The Bank has established a secured line of credit facility with M&T Bank. The Bank has the ability to borrow up to \$5 million on an overnight basis from M&T Bank using investments as collateral at 125% of the borrowed amount. The Bank also has an arrangement with the Federal Reserve Bank for secured borrowings of up to \$1 million. There were no borrowings outstanding on these lines of credit as of September 30, 2009 or December 31, 2008.

Note 11. Income Taxes

Since the Bank is in a net operating loss position, the Bank has recorded a full valuation allowance to reduce its net deferred tax asset to zero at September 30, 2009 and December 31, 2008.

Note 12. Loss per Share

The Bank's loss per share for each of the three-month and nine-month periods ended September 30, 2009 and September 30, 2008 was calculated by dividing the net loss for the respective periods by the weighted average shares outstanding. The calculation of the loss per share for the three months and nine months ended September 30, 2009 and September 30, 2008 appears below:

	Three Months Ended September 30, 2009	Three Months Ended September 30, 2008
Net Loss	\$ (4,072,240)	\$ (118,484)
Weighted Average Shares	5,750,000	5,750,000
Basic Loss per share	\$ (0.71)	\$ (0.02)
	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008
Net Loss	\$ (8,856,130)	\$ (1,247,173)
Weighted Average Shares	5,750,000	5,750,000
Basic Loss per share	\$ (1.54)	\$ (0.22)

Note 13. Other Comprehensive Income (Loss)

Other comprehensive income (loss), which is comprised solely of the unrealized gain (loss) on available for sale securities, net of tax, is as follows:

	Nine Months Ended September 30, 2009			Nine Months Ended September 30, 2008		
	Before Tax	Tax Effect	Net-of-Tax Amount	Before Tax	Tax Effect	Net-of-Tax Amount
Unrealized holding gain (loss) arising during period	\$ 755,316	\$ (299,784)	\$ 455,532	\$ (745,242)	\$ 295,785	\$ (449,457)
Add impairment loss on available for sale securities recognized in income	2,476,215	(982,805)	1,493,410	-	-	-
Less reclassification adjustment for gains recognized in income	(660,019)	261,960	(398,059)	(401,258)	159,259	(241,999)
Unrealized holding gain (loss) on available for sale securities	2,571,512	(1,020,629)	1,550,883	(1,146,500)	455,044	(691,456)
Deferred tax valuation allowance allocated to equity	-	1,020,629	1,020,629	-	(437,665)	(437,665)
Unrealized holding gain (loss) on available for sale securities	\$ 2,571,512	\$ -	\$ 2,571,512	\$ (1,146,500)	\$ 17,379	\$ (1,129,121)

Note 14. Related Party Transactions

The aggregate dollar amount of loans to related parties was \$4,402,661 and \$3,208,792 at September 30, 2009, and December 31, 2008, respectively.

Related party deposits aggregated \$1,879,380 and \$924,122 as of September 30, 2009, and December 31, 2008, respectively. The Bank paid \$27,000 during the nine months ended September 30, 2009, for information technology-related services to an IT consulting company, the principal of which is a director of the Bank. The Bank paid rent of \$90,417 for its main branch facility at 601 North Main Street, Port Chester, New York, during the nine months ended September 30, 2009 to a company 10.4% owned by two directors. The Bank also paid \$43,558 for legal services to a legal firm, a principal of which is a director of the Bank.

Note 15. Fair Value

Effective January 1, 2008, the Bank adopted a standard issued by the Financial Accounting Standards Board (“FASB”) entitled “*Fair Value Measurements*,” which defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles, and expands disclosures about fair value measurements. As defined in this standard, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the Bank uses various methods including market, income and cost approaches. Based on these approaches, the Bank often utilizes certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk or the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable inputs. The Bank utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Based on the observability of the inputs used in the valuation techniques, the Bank is required to provide the following information according to the fair value hierarchy described below. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values.

- Level 1:** Quoted prices in active markets for identical assets and liabilities.

- Level 2:** Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities in active markets, quoted prices in markets that are not active, and model-based valuation techniques for which all significant inputs are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

In February 2008, the FASB issued a staff position which permitted a one-year deferral for the implementation of *Fair Value Measurements* with regard to nonfinancial assets and liabilities that are not recognized or disclosed at fair value in the financial statements on a recurring basis. This staff position was effective as of January 1, 2009.

In April 2009, the FASB issued a staff position entitled “*Determining Fair Value When the Volume and Level of Activity for the Asset and Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly.*” This staff position addresses concerns that *Fair Value Measurements* emphasized the use of an observable market transaction even when that transaction may not have been orderly or the market for that transaction may not have been active and provides additional guidance on: (a) determining when the volume and level of activity for the asset and liability has significantly decreased; (b) identifying circumstances in which a transaction is not orderly; and (c) understanding the fair value measurement implications in both (a) and (b).

The adoption of this staff position resulted in impairment charges against earnings related to the credit portion of the unrealized losses on the four other-than-temporarily impaired private label collateralized mortgage obligations in the amount of \$2,476,000 during the nine months ended September 30, 2009, of which \$438,000 was recorded during the three months ended September 30, 2009. The increase in delinquencies within the mortgages securing these investments was the primary cause of these impairment charges. The noncredit portion of the unrealized losses on these same securities totaled \$1,200,595 as of September 30, 2009. The noncredit portion of the unrealized losses relates to disorderly markets in which these securities trade.

A description of the valuation methodologies used for assets and liabilities recorded at fair value, and for estimating fair value for financial instruments not recorded at fair value in accordance with a standard issued by the FASB entitled “*Disclosures About Fair Values of Financial Instruments*” is set forth below:

Cash and due from banks, federal funds sold, overnight investments, interest-bearing deposits, accrued interest receivable and accrued interest payable. The carrying amount is a reasonable estimate of fair value.

Available-for-Sale and Held-to-Maturity Securities: Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include highly liquid government bonds, certain government agency mortgage-backed securities and certificates of deposit. If quoted

prices are not available, then fair values are estimated by using pricing models (i.e., matrix pricing) or quoted prices of securities with similar characteristics and are classified within Level 2 of the valuation hierarchy. Examples of such instruments include government agency and sponsored agency bonds and mortgage-backed securities. Level 3 securities for which significant unobservable inputs are utilized include non-agency collateralized mortgage obligations.

Loans: For variable rate loans which re-price frequently and have no significant change in credit risk, carrying values are a reasonable estimate of fair values, adjusted for credit losses inherent in the portfolios. The fair value of fixed-rate loans is estimated by discounting the future cash flows using the year-end rates, estimated using local market data, at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities, adjusted for credit losses inherent in the portfolios. The Bank does not record loans at fair value on a recurring basis. However, from time to time, non-recurring fair value adjustments to collateral-dependent impaired loans are recorded to reflect partial write-downs based on the observable market price or current appraised value of collateral, which may be discounted to reflect the impact of changes in housing prices since the date of the appraisal. Because of the discounting, the Bank considers this valuation methodology to be Level 3.

Other Real Estate Owned: At time of foreclosure, real estate owned is adjusted to fair value based on current appraisals less costs to sell upon transfer of the loans to real estate owned. Periodically, new appraisals are ordered for other real estate owned and the value is adjusted accordingly to the new appraisal value less cost to sell. The Bank does not record other real estate owned at fair value on a recurring basis.

Deposits: The fair value of demand deposits, regular savings, and certain money market deposits is the amount payable on demand at the reporting date. The fair value of certificates of deposit and other time deposits is estimated using a discounted cash flow calculation that applies interest rates currently being offered for deposits of similar remaining maturities, estimated using local market data, to a schedule of aggregated expected maturities on such deposits.

Off-balance-sheet instruments: Fair values for off-balance-sheet instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standings.

The following table details the financial instruments that are carried at fair value and measured at fair value on a recurring basis as of September 30, 2009 and December 31, 2008, and indicates the fair value hierarchy of the valuation techniques utilized by the Bank to determine fair value:

	<u>Balance as of September 30, 2009</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Securities available for sale	\$ 37,416,087	\$ -	\$ 33,910,048	\$ 3,506,039

	<u>Balance as of December 31, 2008</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Securities available for sale	\$ 40,877,380	\$ -	\$ 40,877,380	\$ -

The following table shows a reconciliation of the beginning and ending balances for Level 3 investments:

	<u>Three Months Ended September 30, 2009</u>	<u>Nine Months Ended September 30, 2009</u>
Level 3 investments, beginning of period	\$ 3,767,214	\$ -
Transfers into Level 3 during the period	-	3,858,356
Unrealized losses included in change in net assets	(261,175)	(352,317)
Level 3 investments, end of period	<u>\$ 3,506,039</u>	<u>\$ 3,506,039</u>

The following table details the financial instruments carried at fair value and measured at fair value on a non-recurring basis as of September 30, 2009 and December 31, 2008, and indicates the fair value hierarchy of the valuation techniques utilized by the Bank to determine the fair value:

	<u>Balance as of September 30, 2009</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Impaired Loans (1)	\$ 40,616,792	\$ -	\$ -	\$ 40,616,792

	<u>Balance as of December 31, 2008</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Impaired Loans (1)	\$ 9,046,113	\$ -	\$ -	\$ 9,046,113

(1) Represents carrying value and related write-downs for which adjustments are based on the appraised value of the collateral.

The following table details the nonfinancial instruments carried at fair value and measured at fair value on a nonrecurring basis as of September 30, 2009 and indicates the fair value hierarchy of the valuation techniques utilized by the Bank to determine fair value:

	<u>Balance as of September 30, 2009</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Other real estate owned	<u>\$ 1,995,000</u>	<u>\$ -</u>	<u>\$ 1,995,000</u>	<u>\$ -</u>

In April 2009, the FASB issued a staff position entitled “*Interim Disclosures about Fair Value of Financial Instruments.*” This staff position amends the FASB statement entitled “*Disclosures about Fair Value of Financial Instruments*” to require disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in

annual financial statements. This staff position also amends previous guidance entitled “Interim Financial Reporting” to require those disclosures in summarized financial information at interim reporting periods. Effective April 1, 2009, the Bank adopted this staff position. See the following table for disclosure of the information required by this staff position.

The following is a summary of the recorded book balances and estimated fair values of the Bank’s financial instruments at September 30, 2009 and December 31, 2008:

	September 30, 2009		December 31, 2008	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial Assets				
Cash and due from banks	\$ 2,416,761	\$ 2,416,761	\$ 1,286,237	\$ 1,286,237
Federal funds sold and overnight investments	13,838,996	13,838,996	10,629,616	10,629,616
Held to maturity securities	856,380	893,989	1,146,972	1,181,876
Available for sale securities	37,416,087	37,416,087	40,877,380	40,877,380
Loans receivable, net	164,588,678	165,225,180	151,013,117	151,537,784
Accrued interest receivable	1,245,143	1,245,143	1,638,089	1,638,089
Other real estate owned	1,995,000	1,995,000	2,370,250	2,370,250
Financial Liabilities				
Noninterest-bearing deposits	\$ 5,776,698	\$ 5,776,698	\$ 8,435,324	\$ 8,435,324
Interest-bearing checking, NOW and money market	32,775,520	32,775,520	8,221,146	8,221,146
Savings	13,079,626	13,079,626	10,273,773	10,273,773
Time deposits	137,525,989	140,849,933	142,837,938	146,538,988
Repurchase agreements	23,000,000	26,193,153	23,000,000	27,210,524
Accrued interest payable	437,224	437,224	619,559	619,559

Unrecognized financial instruments

Loan commitments on which the committed interest rate is less than the current market rate are insignificant at September 30, 2009 and December 31, 2008.

The Bank assumes interest rate risk (the risk that general interest rate levels will change) as a result of its normal operations. As a result, the fair values of the Bank’s financial instruments will change when interest rate levels change and that change may be either favorable or unfavorable to the Bank. Management attempts to match maturities of assets and liabilities to the extent believed necessary to minimize interest rate risk. However, borrowers with fixed rate obligations are less likely to prepay in a rising rate environment and more likely to prepay in a falling rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by adjusting terms of new loans and deposits and by investing in securities with terms that mitigate the Bank’s overall interest rate risk.

Note 16. Financial Instruments with Off-Balance Sheet Risk

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

contractual amounts of these instruments reflect the extent of involvement the Bank has in particular classes of financial instruments.

The contractual amounts of commitments to extend credit represent the amounts of potential accounting loss should the contract be fully drawn upon, the customer default, and the value of any existing collateral become worthless. The Bank uses the same credit policies and procedures in making commitments and conditional obligations as it does for on-balance-sheet instruments and evaluates each customer's creditworthiness on a case-by-case basis. Management believes that the Bank controls the credit risk of these financial instruments through credit approvals, credit limits, monitoring procedures and the receipt of collateral as deemed necessary.

Financial instruments whose contract amounts represent credit risk are as follows at September 30, 2009 (unaudited), and December 31, 2008:

	<u>September 30, 2009</u>	<u>December 31, 2008</u>
Commitments to extend credit:		
Future loan commitments	\$ 12,762,000	\$ 10,272,000
Unused lines of credit	15,389,245	13,791,778
Undisbursed construction loans	6,859,311	14,943,798
Financial standby letters of credit	576,255	468,750
	<u>\$ 35,586,811</u>	<u>\$ 39,476,326</u>

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. Commitments to extend credit generally have fixed expiration dates or other termination clauses and may require payment of a fee by the borrower. Since these commitments could expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The amount of the collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies, but may include residential and commercial property, deposits and securities.

Standby letters of credit are written commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. All guarantees issued or modified that are not derivative contracts have been recorded on the Bank's balance sheet at their fair value at inception. The liability related to guarantees recorded at September 30, 2009, and December 31, 2008, was not significant.

Note 17. Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the Federal banking agencies. Failure to meet minimum capital requirements can result in certain mandatory – and possibly additional discretionary – actions by regulators that, if undertaken, could have a direct material effect on the Bank's consolidated 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 of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). Management believes that as of September 30, 2009, and December 31, 2008, the Bank meets all capital adequacy requirements to which it is subject.

The following table illustrates the Bank's regulatory capital amounts and ratios as of September 30, 2009 and December 31, 2008 (dollars in thousands):

	Actual		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Percent	Amount	Percent
September 30, 2009						
Tier 1 (Leverage) Capital to Average Assets	\$ 10,735	4.81%	\$ 8,924	4.00%	\$ 11,155	5.00%
Tier 1 Capital to Risk-Weighted Assets	\$ 10,735	6.20%	\$ 6,928	4.00%	\$ 10,392	6.00%
Total Capital to Risk-Weighted Assets	\$ 12,962	7.48%	\$ 13,857	8.00%	\$ 17,321	10.00%
December 31, 2008						
Tier 1 (Leverage) Capital to Average Assets	\$ 19,591	9.65%	\$ 8,121	4.00%	\$ 10,152	5.00%
Tier 1 Capital to Risk-Weighted Assets	\$ 19,591	11.51%	\$ 6,807	4.00%	\$ 10,210	6.00%
Total Capital to Risk-Weighted Assets	\$ 21,635	12.71%	\$ 13,613	8.00%	\$ 17,016	10.00%

The FDIC categorizes banks, based on certain capital ratios under the regulatory framework for prompt corrective action. In a letter dated August 19, 2009, the FDIC notified the Bank that as of June 30, 2009, it fell within the adequately capitalized category under the regulatory framework for prompt corrective action. To be categorized as "well capitalized," the Bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios. As of September 30, 2009, the Bank exceeds the "well capitalized" standard for Tier 1 risk-based capital ratio of 6% and the "adequately capitalized" standard for Tier 1 leverage ratio of 4%. As of September 30, 2009, the Bank's total risk-based capital ratio is less than 8%; hence, the Bank is considered "undercapitalized."

The Authorization Certificate issued by the New York State Banking Department requires the Bank to maintain a risk-based ratio of Tier 1 capital to assets of not less than eight percent (8%) for a period of three years, which ended on December 23, 2008. Thereafter, federal regulations require that a "well capitalized" institution must have a Tier 1 risk-based capital ratio of 6% or greater.

On September 1, 2009, the Bank contracted the services of Laidlaw & Company (UK), Ltd., an investment banking firm, to develop a capital plan in order to raise an additional \$15 to \$20 million of capital, pending regulatory and shareholder approval.

Supervisory Action

On October 22, 2007, the New York State Banking Department and the FDIC issued, with the consent of the Bank, parallel Orders to Cease and Desist applicable to the Bank. The Orders, which were substantially identical, were issued as a result of findings made during the regulators' Safety and Soundness Examination conducted as of the close of business on September 30, 2006, and Compliance Examinations conducted as of the close of business on February 20, 2007. None of the findings or the terms of the Orders affect or address the Bank's ability to meet its financial obligations, including the timely payment of customer deposits or the funding of loan commitments, nor do the Orders affect the FDIC level of insurance of the Bank's deposits.

The Orders require the Bank to refrain from certain practices and to take affirmative action to correct identified deficiencies and weaknesses in its operations. The full text of the Orders can be viewed on the FDIC website and the New York State Banking Department website at www.fdic.gov and <http://www.banking.state.ny.us>, respectively.

A summary of the terms and conditions of the Orders follows:

The Orders prohibit the Bank from operating with inadequate management supervision and Board of Directors oversight, inadequately trained and supervised staff and inadequate audit, compliance and information technology and security policies, processes and procedures, and without a current, comprehensive business and strategic plan and budget. They also prohibit violations of the Bank Secrecy Act and various consumer protection statutes.

The Orders require the Bank to adopt a number of policies and procedures designed to strengthen and improve its operations, and to assess and report to the regulators within specified time frames, regarding several aspects of its operations. The Orders require the Bank to engage qualified professionals acceptable to the regulators to prepare or assist with the preparation of some of the required reports. The Orders direct the Bank to prepare and submit the following reports and other materials:

- A Management Report assessing the Bank's management and staffing needs, performance, competence and responsibilities, and recommending staff training and Board of Directors and senior management recruitment and retention plans and a plan to respond to the recommendations contained in the Management Plan;
- A Corporate Governance Review and report by an independent third party assessing the Bank's corporate governance process, including compliance with the corporate governance provisions of the Sarbanes-Oxley Act of 2002;
- An Expense Report detailing and assessing the propriety of fees and expenses paid to the Bank's insiders and a plan for the Bank to seek reimbursement of payments to insiders determined to have been inappropriate;

- A Strategic Plan for at least the next three years, including detailed financial and market assumptions, goals, strategies and policies, and a mission statement;
- A Profit Plan, including plans to improve the Bank's operating performance, as gauged by specific metrics, and a comprehensive budget;
- An effective Corporate Information Security Policy;
- A Disaster Recovery / Business Continuity Plan and a test of such Plan;
- A Compliance Management System, including consumer protection compliance monitoring, testing and training procedures, a Compliance Training Program and appointment of a qualified compliance officer;
- An Audit Program providing for implementation, monitoring and testing of internal audit controls and procedures, consumer protection compliance, information security and anti-money laundering compliance; and
- Quarterly Progress Reports on compliance with the Orders.

The Orders further require the Bank to take the following affirmative actions:

(i) increased, informed Board of Directors participation and oversight, including the adoption of good corporate record-keeping and reporting practices; (ii) correction of legal and regulatory violations; (iii) implementation of recommended Bank Secrecy Act policies and procedures; (iv) implementation of an effective information security policy and a disaster recovery / business continuity plan; and (v) establishment of a Compliance Committee of the Board of Directors.

Actions that have been taken by the Bank since September 30, 2006 (the date as of which the examination was conducted) include the following: (i) the election of Ronald J. Gentile, whose experience includes 19 years with the FDIC and service as chief executive officer of a bank facing similar issues, as President and Chief Executive Officer and a Director; (ii) the hiring of a Chief Compliance Officer with more than five years of experience, (iii) the election of six additional independent directors, resulting in seven of the nine current directors' being independent, and (iv) the retention of independent consultants to prepare or assist in the preparation of a revised strategic plan and budget, a review of expenses paid to the Bank's insiders and a review of the Bank's loan function.

In the third quarter of 2007, the Board of Directors established a Compliance Committee to supervise the implementation of the Orders. This Committee met monthly in 2007 and 2008 and has met periodically in 2009. The Committee is currently composed of the President and Chief Executive Officer, the Chief Financial Officer, four other directors, each of whom is independent, and the Bank's Compliance Officer. The Compliance Committee reports regularly to the Board of Directors.

The Bank has also taken affirmative actions to implement and test its revised Disaster Recovery / Business Continuity Plan, its Information Technology structure and other processes and procedures.

Management believes it has complied with all of the conditions set forth in the 2007 Orders to Cease and Desist; however, the final determination of when to remove the Orders is made by the FDIC and the New York State Banking Department.

Note 18. Commitments and Contingencies

Representations and Warranties Reserves

In the normal course of business, the Bank is subject to potential recourse obligations resulting from standard representations and warranties customary in mortgage loan sales activities. Violations of these representations and warranties may require the Bank to repurchase loans previously sold. For the nine months ended September 30, 2009, and the year December 31, 2008, the Bank sold \$7.1 million and \$6.4 million of loans, respectively. The Bank is contingently liable under representations and warranties made in the contracts relating to these sales, in certain instances for the life of the loans. The Bank has established a reserve for representations and warranties related to these sales which totaled \$5,500 at September 30, 2009, and \$1,200 at December 31, 2008. On an ongoing basis, the Bank monitors the adequacy of the representations and warranties reserve liability, which is established upon the initial sale of the loans, and is included in accrued expenses and other liabilities in the balance sheet. The Bank has not been required to purchase any loans under such representations and warranty obligations.

Legal Proceedings

On May 7, 2007, two actions were begun in the Supreme Court of the State of New York. One naming the Bank as the defendant was brought by Salvatore Pane, Lisa Vitale and Perry Winter, and the other naming Fred DeCaro, Jr., and the Bank as defendants was brought by Salvatore Pane and First Lincoln Mortgage Corp. (formerly USA Mortgage Bankers of America, Inc.). The first suit, which purports to be brought by the plaintiffs as shareholders and as representatives of a class of shareholders, alleges that the offering materials used by the Bank in connection with its offerings of stock in 2005 and 2006 contained various representations that were untrue, that various payments were made to related parties and that various loans were improperly made. While the plaintiffs seek monetary judgments and other relief from Mr. DeCaro, the only judgment demanded against the Bank is “such other relief as to the Court may seem just and proper.”

The suit against the Bank only alleges that the Bank had entered into an agreement to acquire USA Mortgage Bankers of America, Inc., and that the Bank “abandoned” the plan and breached the agreement. The plaintiffs seek damages in an unspecified amount.

The Bank believes that the claims are without merit and intends to defend itself vigorously. The Bank has filed motions to dismiss these suits for failure to prosecute, which motions have been denied. The original counsel for the plaintiffs have withdrawn as counsel in these suits and the plaintiffs have retained new counsel.

On February 14, 2008, the Bank instituted an action against Raymond Carusone in the New York Supreme Court, Queens County, to foreclose a mortgage loan by the Bank to Mr. R. Carusone in the original principal amount of \$406,250 and an action against Maurizio Carusone in the same court to foreclose a mortgage loan by the Bank to Mr. M. Carusone in the original principal amount of \$331,500. On January 20, 2009, the defendants asserted three

counterclaims against the Bank and seek to recover damages in an unspecified amount for each counterclaim.

The first counterclaim alleges misrepresentations and fraudulent inducement by the Bank in making the loans. Mr. R. Carusone alleges that the Bank represented that it would lease the property, that Mr. R. Carusone relied on the representation to make renovations and that the Bank represented that a subsidiary of the Bank would purchase the property from Mr. R. Carusone. In this counterclaim, Mr. R. Carusone further alleges that he was promised warrants to purchase shares of the Bank's stock at the original offering price but did not receive them. Finally, he alleges that the Bank represented that the shares of the Bank would appreciate significantly. The second counterclaim alleges that the Bank violated New York State Banking Department rules and regulations by issuing a letter of intent to M. Carusone and then failing to close the loan and that the Bank applied outdated underwriting guidelines to the application. The third counterclaim by R. Carusone alleges that the Bank was unjustly enriched by the value of "promotional services" provided by R. Carusone in connection with the Bank's formation and its efforts to raise capital.

The Bank is involved in certain other legal proceedings which have arisen in the normal course of business. Management believes that resolution of these matters will not have a material effect on the Bank's financial condition or results of operations.

While the Bank recognizes that these suits may constitute loss contingencies within the meaning of generally accepted accounting principles, an estimate of the amount thereof cannot be made.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis is intended to assist in understanding the financial condition and results of operations of the Bank. This discussion should be read in conjunction with the accompanying unaudited consolidated financial statements as of and for the three months and nine months ended September 30, 2009 and 2008, along with the audited consolidated financial statements as of and for the year ended December 31, 2008, included in the Bank's Annual Report on Form 10-K filed with the FDIC on April 15, 2009.

Summary

As of September 30, 2009, the Bank had total assets of \$223.2 million including \$164.6 million of loans receivable, net of the allowance for loan losses of \$7.2 million, \$38.3 million of investment securities and \$13.8 million of federal funds sold and overnight investments. Funding for these assets was primarily derived from total deposits of \$189.2 million, repurchase agreements of \$23.0 million and shareholders' equity of \$9.85 million. The Bank's Tier 1 leverage ratio was 4.81% at September 30, 2009.

This compares to total assets as of December 31, 2008 of \$209.9 million including \$151.0 million of loans receivable, net of the allowance for loan losses of \$2.0 million, \$42.0 million of investment securities and \$10.6 million of federal funds sold and overnight investments. Funding for these assets as of December 31, 2008 was primarily derived from total

deposits of \$169.8 million, repurchase agreements of \$23.0 million and shareholders' equity of \$16.1 million. The Bank's Tier 1 Leverage Capital Ratio was 9.65% at December 31, 2008.

The Bank had a net loss for the three months ended September 30, 2009 of \$4.1 million (or basic and diluted loss per share of \$0.71), compared to a net loss of \$118,000 (or basic and diluted loss per share of \$0.02) for the three months ended September 30, 2008.

The Bank's operating loss for the three months ended September 30, 2009 was largely attributable to a provision for loan losses of \$3.7 million, compared to a provision of \$185,000 for the same period of 2008; and to the recognition of \$438,000 of credit losses on other-than-temporarily impaired investments primarily due to increased delinquency rates during the quarter within the mortgages collateralizing the investments, as compared to no such losses during the three months ended September 30, 2008. Other factors contributing to the increased operating loss for the three months ended September 30, 2009 as compared to the three months ended September 30, 2008 follow:

- Net interest income was negatively impacted by the increase in non-accrual loans and lower yields on interest earning assets, partially offset by lower costs of interest bearing liabilities and changes in asset and liability volumes.
- The provision for loan losses increased as a result of the increase in impaired and past due loans and the decrease in net realizable values of collateral supporting these loans caused by the weakened economy.
- Non-interest income increased primarily due to increased gains on the sales of investments, which were partially offset by the credit loss recognized on other-than-temporarily impaired investments.
- Non-interest expense increased primarily due to expenses related to properties in the foreclosure process; increased salaries and benefits related to the hiring of two consultants; increased professional fees for the cost of an experienced loan work-out specialist and a collection specialist; and the increase in FDIC insurance reflecting increased deposit balances, the Bank's regulatory capital classification and premiums assessed. Partially offsetting these increases were planned reductions in occupancy expense and commissions paid on loan closings and legal expenses.

The Bank had a net loss of \$8.9 million (or basic and diluted loss per share of \$1.54) for the nine months ended September 30, 2009, compared to a net loss of \$1.2 million (or basic and diluted loss per share of \$0.22) for the nine months ended September 30, 2008.

The Bank's operating loss for the nine months ended September 30, 2009 was largely attributable to the recognition of \$2.5 million of credit losses on other-than-temporarily impaired investments, as compared to no such losses in 2008; and to a provision for loan losses of \$5.1 million, compared to a provision of \$724,000 for the same period in 2008. The significant increase in the provision for loan losses during the first nine months of 2009 is related to a group

of sixteen impaired loans that have been severely impacted by prevailing economic conditions, discussed in more detail under “Allowance for Loan Losses.”

In addition to the impact of the credit losses recognized on other-than-temporarily impaired investments and provision for loan losses, the operating results for the nine months ended September 30, 2009, compared to the nine months ended September 30, 2008, were influenced by the following factors:

- Net interest income was negatively impacted by the increase in non-accrual loans and lower yields on interest earning assets, partially offset by lower costs of interest bearing liabilities and changes in asset and liability volumes.
- Non-interest expense increased primarily due to expenses related to a write-down in the value of one OREO property due to an updated appraisal with a reduced appraised value; expenses related to the increased number of properties in the foreclosure process; increased salaries and benefits related to the hiring of two consultants, who had previously been recorded in professional fees; and increased FDIC insurance reflecting increased deposit balances and premiums assessed, including a special assessment recorded in June 2009. Partially offsetting these increases were planned reductions in occupancy expense and commissions paid on loan closings, and reduced professional fees and legal expenses.

Goals of the Board of Directors and management of the Bank include the raising of additional capital which is subject to regulatory and shareholder approval. To this end, on September 1, 2009, the Bank contracted Laidlaw & Company (UK), Ltd., an investment banking firm, to assist the Bank in considering various strategic alternatives designed to maximize shareholder value.

The results for the three months and nine months ended September 30, 2009, as compared to the three months and nine months ended September 30, 2008, reflect management’s continued focus on leveraging the Bank’s capital with quality commercial loan growth, an emphasis on revenue enhancement and cost reduction strategies and the continuous use of asset liability strategies to lower the Bank’s interest rate sensitivity. The weakened economy has negatively impacted certain loan customers of the Bank resulting in an increase in impaired loans, as well as reductions in real estate values of properties securing certain of these loans. These borrowers are being monitored very closely by in-house staff and by the addition in June 2009 of an experienced loan work-out consultant. In addition, the Bank continues to obtain current, independent appraisals to monitor values of properties securing the loans.

Critical Accounting Policies

The preparation of financial statements in accordance with U.S. generally accepted accounting principles requires the Bank’s management to make a number of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and to disclose contingent assets and liabilities. Actual results could differ significantly from those estimates. The Bank’s significant accounting policies are described in Note 2 to the Consolidated Financial Statements in its Annual Report on Form 10-K filed with the FDIC on April 15, 2009. Management has identified accounting for the allowance for loan losses, the analysis of other-than-

temporary-impairment for its investment securities and valuation of deferred income tax assets and liabilities as the Bank's most critical accounting policies and estimates in that they are important to the portrayal of the Bank's financial condition and results. They require management's most subjective and complex judgment as a result of the need to make estimates about the effect of matters that are inherently uncertain. These accounting policies, including the nature of the estimates and types of assumptions used, are incorporated throughout Management's Discussion and Analysis.

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to operations. Loans are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. During the nine months ended September 30, 2009, the Bank charged-off one loan in the amount of \$5,004 and experienced \$51,890 of recoveries on loans previously charged-off. During the nine months ended September 30, 2008, the Bank charged-off \$283,386 of loans, and there were no recoveries of loans previously charged-off.

The Bank's ongoing allowance for loan losses analysis results in an allowance for loan losses that consists of specific and general components. The specific component relates to allowances established for individual impaired loans. The general component relates to pools of loans segregated by loan type, and is based on historical loss experience adjusted by certain qualitative factors as determined by management and the board of directors.

The Bank had 29 non-accrual loans totaling \$40.6 million that were considered to be impaired loans at September 30, 2009. Based on management's analysis of the net realizable values of the collateral securing these non-accrual loans, a specific allowance of \$2.9 million was required to be established at September 30, 2009, an increase from the \$141,540 specific allowance required at December 31, 2008. Eleven of the non-accrual loans totaling \$13.2 million are in the process of foreclosure. In addition, eight loans totaling \$14.4 million are 90 days past due and accruing. These eight loans are well collateralized and in the process of collection and therefore they are still accruing interest as of September 30, 2009.

The accrual of interest income on loans is discontinued whenever reasonable doubt exists as to its collectibility and generally is discontinued when loans are past due 90 days as to either principal or interest, or are otherwise considered impaired. When the accrual of interest income is discontinued, all previously accrued and uncollected interest is reversed against interest income. The accrual of interest on loans past due 90 days or more may be continued if the loan is well secured, and it is believed all principal and accrued interest income due on the loan will be realized, and the loan is in the process of collection. A non-accrual loan is restored to accrual status when it is no longer delinquent and collectibility of interest and principal is no longer in doubt.

The allowance for loan losses is evaluated on a regular basis by management and is based on management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic

conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

Based upon this evaluation, management believes the allowance for loan losses of \$7,154,000 or 4.16% of total gross loans at September 30, 2009, to be adequate, under prevailing economic conditions, to absorb losses on existing loans. At December 31, 2008, the allowance was \$2,044,000 or 1.33% of total gross loans outstanding. At September 30, 2009, there was a specific allowance of \$2.9 million related to 16 impaired loans with a balance of \$22.9 million, versus a specific allowance of \$141,540 related to one impaired loan with a balance of \$2,200,000 at December 31, 2008.

Management considers all non-accrual loans, other loans past due 90 days or more based on contractual terms, which are either not well secured or in the process of collection, and restructured loans to be impaired. In most cases, loan payments that are past due less than 90 days and the related loans are not considered to be impaired. The Bank considers consumer installment loans to be pools of smaller balance homogeneous loans, which are collectively evaluated for impairment.

Analysis of Other-than-Temporary Impairment of Investment Securities

The Bank's investment securities portfolio is comprised of available-for-sale and held-to-maturity investments. The available-for-sale portfolio is carried at estimated fair value, with any unrealized gains or losses, net of taxes, reported as accumulated other comprehensive income or loss in shareholders' equity. The held-to-maturity portfolio is carried at amortized cost. Management determines the classification of a security at the time of its purchase.

The Bank conducts a periodic review of its investment securities portfolio to determine if the value of any security has declined below its cost or amortized cost, and whether such decline is other-than-temporary. If such decline is deemed other-than-temporary, the security is written down to a new cost basis and the resulting loss is reported within non-interest income in the consolidated statement of income.

Significant judgment is involved in determining when a decline in fair value is other-than-temporary. The factors considered by management include, but are not limited to:

- Whether the Bank intends to sell the security and whether it is more likely than not that the Bank will be required to sell the security before the recovery of its amortized cost basis, which may be maturity;
- The length of time and the extent to which the fair value has been less than the amortized cost basis;
- Adverse conditions specifically related to the security, an industry or a geographic area;
- The historical and implied volatility of the fair value of the security;

- The payment structure of the debt security and the likelihood of the issuer being able to make payment that increase in the future;
- Failure of the issuer of the security to make scheduled interest or principal payments;
- Any changes to the rating of the security by a rating agency;
- Recoveries or additional declines in fair value subsequent to the balance sheet date.

Adverse changes in the factors used by management to determine if a security is OTTI could lead to additional impairment charges. Conditions affecting a security that the Bank determined to be temporary could become other-than-temporary and warrant an impairment charge. Additionally, a security that had no apparent risk could be affected by a sudden or acute market condition and necessitate an impairment charge. The Bank adopted the provisions of the FASB staff position issued in April 2009 relating to OTTI during the second quarter of 2009. Adoption of this staff position resulted in the recognition of an impairment charge relating to credit-related factors in the amount of \$2,476,215 for the nine months ended September 30, 2009; \$438,362 of this impairment charge was recognized during the three months ended September 30, 2009. The non-credit-related amount of OTTI was recognized as a component of other comprehensive loss and is disclosed in Note 5 – Investments.

Income Taxes

The Bank recognizes income taxes under the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and loss carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

Recent Accounting Pronouncements

In February 2008, the FASB issued a staff position which permitted a one-year deferral for the implementation of *Fair Value Measurements* with regard to nonfinancial assets and liabilities that are not recognized or disclosed at fair value in the financial statements on a recurring basis. This staff position was effective as of January 1, 2009. The adoption of this staff position did not have a material impact on the Bank’s consolidated financial statements. See Note 15 for additional information regarding fair value.

In April 2009, the FASB issued a staff position entitled “*Determining Fair Value When the Volume and Level of Activity for the Asset and Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly.*” This staff position provided additional guidance on: (a) determining when the volume and level of activity for the asset and liability has

significantly decreased; (b) identifying circumstances in which a transaction is not orderly; and (c) understanding the fair value measurement implications in both (a) and (b). The Bank adopted this guidance during the quarter ended June 30, 2009. See Note 15 for additional information regarding fair value measurement.

In April 2009, the FASB issued a new staff position entitled “*Recognition and Presentation of Other-Than-Temporary Impairments*.” This staff position amends the other-than-temporary impairment guidance for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments in the financial statements. The most significant change the staff position brings is a revision to the amount of other-than-temporary loss of a debt security recorded in earnings. The Bank adopted this staff position during the quarter ended June 30, 2009 and recorded a credit-related impairment loss of \$2.1 million related to private label mortgage-backed securities. The Bank recognized an other-than-temporary impairment loss in earnings of \$2.5 million for the nine months ended September 30, 2009 relating to the credit portion of the total unrealized loss of \$3.7 million as of September 30, 2009. See Note 5 for additional information regarding this recognition.

In April 2009, the FASB issued a new staff position entitled “*Interim Disclosures about Fair Value of Financial Instruments*.” This staff position requires disclosures about fair value instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. This staff position also requires those disclosures in summarized financial information at interim reporting periods. The Bank adopted this staff position during the quarter ended June 30, 2009. See Note 15 for additional information regarding fair value.

In January 2009, the FASB issued a new staff position which amends the impairment guidance entitled “*Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continue to be Held by a Transferor in Securitized Financial Assets*.” The staff position revises impairment guidance for beneficial interests to make it consistent with the requirements of the FASB statement entitled “*Accounting for Certain Investments in Debt and Equity Securities*” for determining whether an impairment of other debt and equity securities has occurred. The impairment model in this statement enables greater judgment to be exercised in determining whether an other-than-temporary impairment needs to be recorded. The impairment model previously provided for in the guidance limited management’s use of judgment in applying the impairment model. This staff position was effective as of January 1, 2009. The adoption of this staff position did not have a material impact on the Bank’s consolidated financial statements.

In June 2009, the FASB issued a new standard entitled “*Accounting for Transfers of Financial Assets – an amendment of FASB Statement No. 140*.” The objective of this standard is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor’s continuing involvement, if any, in transferred financial assets. Additionally, on and after the effective date, the concept of a qualifying special-purpose entity is no longer relevant for accounting purposes. Therefore, formerly qualifying special-purpose entities (as defined under previous accounting standards) should be evaluated for consolidation by reporting entities

on and after the effective date in accordance with the applicable consolidation guidance. If the evaluation on the effective date results in consolidation, the reporting entity should apply the transition guidance provided in the pronouncement that requires consolidation. This standard must be applied as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application is prohibited. This standard must be applied to transfers occurring on or after the effective date. The adoption of this standard is not expected to have a material impact on the Bank's consolidated financial statements.

In June 2009, the FASB issued a new standard entitled "*Subsequent Events.*" The objective of this standard is to establish general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or available to be issued. This standard defines (i) the period after the balance sheet date during which a reporting entity's management should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements, (ii) the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements, and (iii) the disclosures an entity should make about events or transactions that occurred after the balance sheet date. This standard became effective for the Bank during the quarter ended June 30, 2009. The adoption of this standard did not have a material impact on the Bank's consolidated financial statements.

In June 2009, the FASB issued a new standard entitled "*The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles – a replacement of FASB Statement No. 162*" to allow the FASB Codification to be the single source of authoritative U.S. accounting and reporting standards, other than guidance issued by the Securities and Exchange Commission. The Bank adopted this standard during the quarter ended September 30, 2009. The adoption of this standard did not have a material impact on the Bank's consolidated financial statements.

Comparison of Financial Condition as of September 30, 2009, versus December 31, 2008

General

The Bank's total assets were \$223.2 million at September 30, 2009, an increase of \$13.3 million (6.3%) from \$209.9 million at December 31, 2008. The earning asset categories comprised of federal funds sold and overnight investments, investments, loans held for sale and total gross loans increased \$18.2 million (8.8%) from \$205.9 million at December 31, 2008 to \$224.1 million at September 30, 2009. The earning asset categories with the most growth were federal funds sold and overnight investments, which increased \$3.2 million (30.2%) from \$10.6 million at December 31, 2008 to \$13.8 million at September 30, 2009 and total gross loans, which increased \$18.7 million (12.2%) from \$153.3 million at December 31, 2008 to \$172.0 million at September 30, 2009. Partially offsetting the increases noted was the \$3.8 million (8.9%) decrease in investment securities. The earning asset growth has been negatively impacted by the \$31.6 million increase in non-accrual loans from \$9.0 million at December 31, 2008 to \$40.6 million at September 30, 2009. Therefore, total earning assets, net of non-accrual loans, has decreased \$13.4 million (6.8%) from \$196.9 million at December 31, 2008 to \$183.5 million as of September 30, 2009.

The \$13.4 million of total earning asset growth, net of non-accrual loans, was primarily funded by the \$19.4 million (11.4%) increase in total deposits, which reached \$189.2 million at September 30, 2009 from \$169.8 million at December 31, 2008. This funding reflects management's efforts to increase core deposits, in particular, savings and money market accounts, while reducing its reliance on brokered deposits. Noninterest-bearing deposits decreased \$2.7 million (31.5%), while interest-bearing deposits increased \$22.0 million (13.7%). The growth in interest-bearing deposits primarily reflects a \$24.7 million (382.0%) increase in money market deposits, which reached \$31.2 million at September 30, 2009 from \$6.5 million at December 31, 2008. Savings deposits increased \$2.8 million (27.3%) from \$10.3 million at December 31, 2008 to \$13.1 million at September 30, 2009. Partially offsetting the increases in money market and savings deposits was a \$5.3 million (3.7%) decrease in time deposits. The time deposits decrease reflects a \$15.5 million (59.7%) reduction in brokered deposits from \$25.9 million at December 31, 2008 to \$10.4 million at September 30, 2009, as certain brokered deposits matured, partially offset by a \$10.1 million (8.7%) increase in retail time deposits from \$117.0 million at December 31, 2008 to \$127.1 million at September 30, 2009.

Total equity capital at September 30, 2009 was \$9.85 million, representing a Tier 1 Leverage Capital Ratio of 4.94%, as compared to total equity capital at December 31, 2008 of \$16.1 million, representing a Tier 1 Leverage Capital Ratio of 9.65%.

Federal funds sold and overnight investments

The balance in federal funds sold and overnight investments totaled \$13.8 million at September 30, 2009, which is an increase of \$3.2 million (30.1%) as compared to \$10.6 million at December 31, 2008. These funds provide a source of liquidity to fund portfolio loan growth and are used to cover fluctuations in deposits as they mature, in keeping with the guidelines established by the Bank's Asset and Liability Management Committee. See "Liquidity" for additional discussion related to funding sources, including available lines of credit.

Investment Securities

Investment securities totaled \$38.3 million at September 30, 2009, a decrease of \$3.7 million (8.8%) from \$42.0 million at December 31, 2008. This reduction primarily reflects principal payments received on these securities. Additionally, during the second and third quarters of 2009 the Bank recognized credit losses on other-than-temporarily impaired securities of \$2,038,000 and \$438,000, respectively, on four private label available for sale securities. There remains \$1.2 million of unrealized losses on these securities relating to the noncredit portion of the total unrealized loss, which is recognized in other comprehensive loss as of September 30, 2009.

Loans

Total gross loans reached \$172.0 million at September 30, 2009. The loan portfolio consisted of commercial real estate loans of \$41.1 million, construction loans of \$80.8 million, residential mortgages of \$12.8 million, home equity lines of credit of \$14.5 million, commercial and industrial loans of \$21.7 million and consumer loans of \$1.1 million. The ratio of loans to deposits as of September 30, 2009, was 90.9%, which is consistent with the 90.3% ratio at December 31, 2008. The Bank's targeted loan-to-deposit ratio is from 80% to 90%.

The overall \$18.7 million (12.2%) increase in total gross loans from \$153.3 million at December 31, 2008 to \$172.0 million at September 30, 2009 primarily reflects the net increase in commercial and industrial loans, commercial real estate loans and construction loans of \$5.9 million (37.2%), \$5.7 million (16.1%) and \$5.1 million (6.8%), respectively.

As of September 30, 2009, the Bank had \$80.8 million in construction loans, which represents 47.0% of the Bank's total loan portfolio and 820% of the Bank's total capital position. The Bank's policy states that all construction loans over \$2.0 million will require an additional appraisal by a Bank-approved appraiser to provide further support of value. The Bank utilizes the lower of the two appraisals in determining the loan-to-value ratio to be assigned. Before any disbursement on a construction loan is made, the Bank reviews current engineering construction reports with photographs showing the current status of the construction, updated title reports, the percentage of loan disbursements to total cost and maturity date.

Every month a detailed report on the Bank's construction loans is presented to the Board of Directors at its regularly scheduled board meeting. The report reflects the total loan commitment, outstanding balance, loan type, county where collateral property is located, the percentage of loan balance to project costs and loan-to-value ratio, maturity date, interest reserve, compensating balance required and actual compensating balance on deposit. Concentration reports are prepared and submitted to the Board of Directors quarterly.

Additionally, the Bank's Loan Committee has taken further safeguards within the past few months to monitor and limit the risks inherent in construction loans, such as:

1. Reducing loan-to-value ("LTV") ratios below the previous policy levels of 60% land development, 65% commercial real estate / multi-family by 5-10% or more, in some recently approved construction loans. Generally the new LTV levels approved are between 50% to 55%, depending on the borrower and collateral type. The Bank's policy currently allows for a 50% LTV on raw land, but the Bank has generally refrained from granting any such loans in the current environment;
2. The Bank restricts construction loans to a single borrower (including guarantors) to no more than two. Once one of the two projects has been completed and successfully sold, the Bank will consider making a construction loan for an additional project.

On July 13, 2009, the board of directors passed a resolution that the Bank not enter into any additional commercial construction or speculative construction loans or make additional advances under existing commercial construction or speculative construction loans unless the Board or the Loan Committee determines that an extension of additional credit to such borrowers is required under existing loan documents or is reasonably necessary to promote the best interests of the Bank and that, prior to renewing or extending any commercial construction or speculative construction loan, a majority of the full Board or the Loan Committee must approve the credit renewal or extension and records, in writing, why such extension is appropriate to promote the best interests of the Bank.

Allowance for Loan Losses and Non-Accrual, Past Due and Restructured Loans

The allowance for loan losses consists of the balance at the beginning of the period plus the current year provision of \$5,063,114, less charge-offs of \$5,004, plus recoveries of \$51,890 and totaled \$7,154,000 at September 30, 2009. As of September 30, 2009, there were 43 loans thirty days or more past due totaling \$61.5 million, 29 of which totaling \$40.6 million are ninety days or more past due and have been put on non-accrual status in accordance with the Bank's policy and eight of which totaling \$14.4 million are 90 days past due and still accruing because they are well secured and in the process of collection.

The following represents the activity in the allowance for loan losses for the nine months ended September 30, 2009 and 2008.

	For the Nine Months Ended September 30,	
	2009	2008
Balance at beginning of period	\$ 2,044,000	\$ 1,421,000
Provision for loan losses	5,063,114	724,386
Charge-offs	(5,004)	(283,386)
Recoveries	51,890	-
Balance at end of period	<u>\$ 7,154,000</u>	<u>\$ 1,862,000</u>

Non-Accrual, Past Due and Restructured Loans

The following is a summary of non-accrual and past due loans at September 30, 2009 and December 31, 2008:

	September 30, 2009	December 31, 2008
Loans delinquent over 90 days and still accruing	\$ 14,368,658	\$ 664,884
Non-accrual loans	<u>40,616,792</u>	<u>9,046,113</u>
Total nonperforming loans	<u>\$ 54,985,450</u>	<u>\$ 9,710,997</u>
% of Total Loans	31.97%	6.34%
% of Total Assets	24.42%	4.63%
Ratio of allowance for loan losses to nonperforming loans	13.01%	21.05%

The following information relates to impaired loans as of and for the nine months ended September 30, 2009 and the year ended December 31, 2008:

	2009	2008
Impaired loans for which there is a specific allowance	<u>\$ 22,856,060</u>	<u>\$ 2,200,000</u>
Impaired loans for which there is no specific allowance	<u>\$ 17,760,732</u>	<u>\$ 6,846,113</u>
Specific allowance related to impaired loans	<u>\$ 2,917,258</u>	<u>\$ 141,540</u>
Average recorded investment in impaired loans	<u>\$ 15,422,094</u>	<u>\$ 4,372,214</u>

Interest income collected and recognized on impaired loans was \$37,754 and \$9,524 during the nine months ended September 30, 2009 and year ended December 31, 2008,

respectively. If impaired loans had been current throughout their terms, additional interest of \$746,676 and \$1,599,844 would have been recognized during the three- and nine-month periods ended September 30, 2009, respectively. For the year 2008, an additional \$426,110 would have been recognized. The Bank has no commitments to lend additional funds to borrowers whose loans are impaired, except for construction loans on a selective basis.

At September 30, 2009, 11 of the 29 non-accrual loans totaling \$13.2 million are in the process of foreclosure; however, management's analysis of the net realizable value of the collateral shows no anticipated additional losses. The Bank had one loan considered a "troubled debt restructuring" as of September 30, 2009 and December 31, 2008 in the amount of \$1.4 million, which is included in non-accrual loans.

Potential Problem Loans

In addition to loans that have been identified as non-accrual or past due 90 days and still accruing at September 30, 2009, the Bank has 6 loans comprising \$12.6 million that management has doubts as to the borrower's ability to comply with the present repayment terms. These loans were identified based upon an analysis of the loan type, collateral and the borrower / guarantor.

The growth of impaired loans in the Bank's loan portfolio is attributable to the decline in real estate values in the principal markets in which the Bank conducts business, coupled with a reduction in the ability of certain borrowers to refinance or repay their obligations. The real estate market for speculative luxury dwellings, that comprise the bulk of the construction portfolio, continues to manifest little sales activity. Both buyers and sellers are frozen and waiting for some indication the market has bottomed out prior to making a bid or accepting an offer.

The Bank's lending department is devoting its resources to managing the loan portfolio until such time as delinquent loans are reduced to a reasonable level. Loan modification and/or restructuring, the principal tool for managing an impaired loan, requires extensive negotiations with borrowers concerning the loan terms, and new appraisals must be obtained in a declining real estate market, which frequently results in higher LTV's compared to the original underwriting. Consequently, less flexibility is available in advancing new funds for unfinished construction projects incurring cost overruns.

A workout consultant has been hired to assist in modifying and extending loans. The consultant is working full-time and has been assigned specific loans to modify and to negotiate an extension on terms that mitigate the risk of borrower default and ensure repayment of all amounts due the Bank, subject to the approval of the Loan Committee of the Board of Directors on behalf of the Bank. Additionally, a full-time collections clerk has been hired to assist in the collection of delinquent loans.

Other Real Estate Owned

Other real estate owned represents the estimated net realizable value of real estate received in satisfaction of a non-performing loan through foreclosure proceedings in June 2008.

Deposits

Deposits were \$189.2 million at September 30, 2009, an increase of \$19.4 million (11.4%) from the \$169.8 million in deposits at December 31, 2008. Non-interest-bearing deposits were \$5.8 million at September 30, 2009, compared to \$8.4 million at December 31, 2008. Interest-bearing deposits were \$183.4 million at September 30, 2009, an increase of \$22.1 million (13.7%) from the \$161.3 million in interest-bearing deposits at December 31, 2008. Included in time deposits at September 30, 2009, were brokered deposits totaling \$10.4 million (4.6% of total assets), compared to \$25.9 million (12.3% of total assets) at December 31, 2008. Brokered deposits at September 30, 2009 and December 31, 2008 have original maturities of four weeks to five years. The growth in money market accounts of \$24.7 million (382.0%) during the first nine months of 2009 provided the primary funding source for the growth in total gross loans.

Repurchase Agreements

The Bank entered into repurchase agreements in 2007 and has maintained the balance of \$23.0 million at September 30, 2009 and December 31, 2008. The weighted average cost of funds on the repurchase agreements at September 30, 2009 and December 31, 2008 was 4.57% and 4.60%, respectively.

Accrued expenses and other liabilities

Accrued expenses and other liabilities increased \$117,000 (11.4%) to \$1,148,000 at September 30, 2009, from \$1,031,000 at December 31, 2008. There was an increase in accrued expenses of \$299,000 which was primarily the result of an \$88,000 increase in accounts payable, a \$44,000 increase in the payroll accrual reflecting an increase in the number of days unpaid as of month end, a \$42,000 increase in commitment fees relating to pending loan closings and a \$32,000 increase in the accrual for FDIC insurance, primarily reflecting the increase in premiums due to the increased level of deposit insurance coverage from \$100,000 to \$250,000. The increase noted was partially offset by the reduction in accrued interest payable on deposits of \$182,000, primarily on brokered deposits in view of the reduced balances in this deposit type.

Results of Operations – Comparison of the Results of Operations for the Three Months and Nine Months Ended September 30, 2009 and 2008

General

The Bank experienced a net loss of \$4.1 million (or basic and diluted loss per share of \$0.71) and \$8.9 million (or basic and diluted loss per share of \$1.54) for the three months and nine months ended September 30, 2009, respectively, as compared to a net loss of \$118,000 (or basic and diluted loss per share of \$0.02) and \$1.2 million (or basic and diluted loss per share of \$0.22) for the three months and nine months ended September 30, 2008, respectively.

The \$4.0 million increase in the net loss for the third quarter of 2009 compared to the third quarter of 2008 and the \$7.7 million increase in the net loss for the nine months ended September 30, 2009, as compared to the nine months ended September 30, 2008, were primarily due to the negative impact on certain loan customers resulting from the downturn in the economy, which resulted in a significant increase in non-accrual loans and therefore a reduction in interest income on loans and an increase in the provision for loan losses. It also reflects credit

losses taken on other-than-temporarily impaired investments in both the second and third quarters of 2009, which were partly offset by increased gains taken of the sales of investments and increased operating expenses primarily related to foreclosed property and ORE expenses.

Net interest income

The Bank's net interest income is dependent primarily upon the difference or spread between the average yield earned on federal funds sold and overnight investments, interest-bearing deposits, loans, investment securities, and other earning assets and the average rate paid on deposits and borrowings, as well as the relative amounts of such interest-earning assets and interest-bearing liabilities. The Bank, like other banking institutions, is subject to interest rate risk to the degree that its interest-bearing liabilities re-price at different times than its interest-earning assets. The Bank's Asset and Liability Management Committee monitors the Bank's interest rate sensitivity with the goal of neutralizing the impact on net interest income due to changes in interest rates.

For the three months ended September 30, 2009, net interest income decreased \$377,000 (24.5%) to \$1,162,000 versus \$1,539,000 for the quarter ended September 30, 2008. Though the average interest-earning asset categories increased \$28.7 million (14.9%) to \$220.4 million for the three months ended September 30, 2009 from \$191.7 million for the three months ended September 30, 2008, the net interest spread (the yield on interest-earning assets less the cost of interest-bearing liabilities) decreased to 1.78% from 2.58%. The major component of the total average interest-earning asset growth was the Bank's average loan portfolio which increased by \$28.6 million (19.9%) from \$143.6 million (74.9% of average interest-earning assets) for the three months ended September 30, 2008 to \$172.2 million (78.1% of average interest-earning assets) for the three months ended September 30, 2009. The reduction in net interest spread reflects the changes in interest earning asset and liability volumes; the negative impact of the increased level of non-accrual loans; and the impact on the net interest spread resulting from the reduction in the prevailing level of interest rates. During the three months ended September 30, 2009, the yield on investments was favorably impacted as a result of the interest being recognized on the investment securities which were written down due to the other-than-temporary credit loss amount reflected in earnings. The interest accrued on these investments is being collected. This favorable impact is more than offset by the decreasing interest rate environment resulting in lower yields on newly purchased investments. Interest income derived from the growth in average interest earning assets is partially offset by the negative impact on interest income caused primarily by the \$36.7 million increase in non-accrual loans, which reached \$40.6 million at September 30, 2009 as compared to \$3.9 million at September 30, 2008. The reduction in interest income reflects both the reversal of interest due on loans when placed on non-accrual status and the lack of interest income being generated while these loans remain on non-accrual status. Had non-accrual loans continued accruing during the three months ended September 30, 2009, an additional \$747,000 of interest income would have been recorded during this period.

For the nine months ended September 30, 2009, net interest income decreased \$684,000 (15.8%) to \$3,639,000 versus \$4,323,000 for the nine months ended September 30, 2008. Though average interest-earning assets increased \$31.2 million (16.6%) to \$219.3 million for the nine months ended September 30, 2009 from \$188.1 million for the nine months ended September 30, 2008, the net interest spread decreased to 1.84% from 2.32%. The major

component of this overall average interest-earning asset growth was the Bank's average loan portfolio which increased by \$32.3 million (24.4%) from \$132.2 million (70.3% of average interest-earning assets) for the nine months ended September 30, 2008 to \$164.5 million (75.0% of average interest-earning assets) for the nine months ended September 30, 2009. The reduction in net interest spread reflects the changes in interest earning asset and liability volumes; the negative impact of the increased level of non-accrual loans; and the impact on the net interest spread resulting from the reduction in the prevailing level of interest rates. During the nine months ended September 30, 2009 the yield on investments was favorably impacted as a result of the interest being recognized on the investment securities which were written down due to the other-than-temporary credit loss amount reflected in earnings. The interest accrued on these investments is being collected. This favorable impact is more than offset by the decreasing interest rate environment resulting in lower yields on newly purchased investments. Interest income derived from the growth in average interest earning assets is partially offset by the negative impact on interest income caused by the \$36.7 million increase in non-accrual loans, which reached \$40.6 million at September 30, 2009 as compared to \$3.9 million at September 30, 2008. The reduction in interest income reflects both the reversal of interest due on loans when placed on non-accrual status and the lack of interest income being generated while these loans remain on non-accrual status. Had non-accrual loans continued accruing during the nine months ended September 30, 2009, an additional \$1.6 million of interest income would have been recorded during this period.

For the three months ended September 30, 2009 the yield on earning assets was 5.24% compared to 6.88% for the three months ended September 30, 2008. This decrease in the overall yield on earning assets reflects both the negative impact on the loan yield due to the increased level of non-accrual loans and the negative impact on each category of interest-earning assets due to the declining interest rate environment. For example, the Bank's average loan portfolio increased \$28.6 million (19.9%) to \$172.2 million, which yielded 5.55% for the three months ended September 30, 2009, as compared to an average balance of \$143.6 million which yielded 7.52% for the three months ended September 30, 2008.

The decrease in the Bank's cost of interest-bearing liabilities for the three months ended September 30, 2009, as compared to the three months ended September 30, 2008, resulted from the reduction in the prevailing interest rates. This can be seen in the reduction in the Bank's cost of interest-bearing liabilities from 4.30% for the three months ended September 30, 2008 to 3.46% for three months ended September 30, 2009. Similarly, the cost of time deposits decreased from 4.51% for the three months ended September 30, 2008 to 3.64% for the three months ended September 30, 2009. The reduction in the cost of interest-bearing liabilities due to changes in interest rates was offset primarily by the \$29.0 million (25.9%) increase in the average balance of time deposits for the three months ended September 30, 2009, which reached \$141.1 million (70.7% of total average interest-bearing liabilities) from \$112.0 million (68.5% of total average interest-bearing liabilities) for the three months ended September 30, 2008.

For the nine months ended September 30, 2009, the yield on earning assets was 5.60% as compared to 6.91% for the nine months ended September 30, 2008. This decrease in the overall yield on earning assets reflects both the negative impact on the loan yield due to the increased level of non-accrual loans and the negative impact on each interest-earning asset category due to the declining interest rate environment. For example, the Bank's average loan portfolio

increased \$32.3 million (24.4%) to \$164.5 million, which yielded 6.19% for the nine months ended September 30, 2009, as compared to an average balance of \$132.2 million which yielded 7.60% for the nine months ended September 30, 2008.

The decrease in the Bank's cost of interest-bearing liabilities for the nine months ended September 30, 2009, as compared to the nine months ended September 30, 2008, resulted from the reduction in the prevailing interest rates. This can be seen in the reduction in the Bank's cost of interest-bearing liabilities from 4.59% for the nine months ended September 30, 2008 to 3.77% for the nine months ended September 30, 2009. Similarly, the cost of time deposits decreased from 4.82% during the nine months ended September 30, 2008 to 3.92% for the nine months ended September 30, 2009. The reduction in the cost of interest-bearing liabilities due to changes in interest rates was offset primarily by the \$33.9 million (30.1%) increase in the average balance of time deposits for the nine months ended September 30, 2009, which reached \$146.5 million (74.2% of total average interest-bearing liabilities) at September 30, 2009 from \$112.6 million (71.4% of total average interest-bearing liabilities) at September 30, 2008.

Average Balances, Yields and Rates

The following table presents average balance sheets (daily averages), interest income, interest expense, and the corresponding annualized rates on earning assets and rates paid on interest-bearing liabilities for the three months ended September 30, 2009 and 2008.

Distribution of Assets, Liabilities and Shareholders' Equity: Interest Rates and Interest Differential

	Three months ended September 30, 2009			Three months ended September 30, 2008			Fluctuations in Interest Income/ Expense Total
	Average Balance	Interest Income/ Expense	Average Rate	Average Balance	Interest Income/ Expense	Average Rate	
Interest-earning assets:							
Loans (1)	\$172,160,871	\$ 2,387,084	5.55%	\$143,584,552	\$ 2,700,140	7.52%	\$ (313,056)
Investments	39,232,535	494,456	5.04%	36,176,483	495,431	5.48%	(975)
Interest-bearing deposits	-	-	-	8,710	108	4.96%	(108)
Federal funds sold and overnight investments	8,569,687	3,232	0.15%	7,670,010	40,685	2.12%	(37,453)
Loans held for sale	406,506	4,070	4.00%	4,287,637	62,077	5.79%	(58,007)
Total interest-earning assets	<u>220,369,599</u>	<u>2,888,842</u>	5.24%	<u>191,727,392</u>	<u>3,298,441</u>	6.88%	<u>(409,599)</u>
Cash and due from banks	2,503,754			1,171,847			
Leasehold improvements and equipment, net	648,723			757,894			
Allowance for loan losses	(3,542,774)			(1,713,689)			
Other	3,124,923			3,331,614			
Total Assets	<u>\$223,104,225</u>			<u>\$195,275,058</u>			
Interest-bearing liabilities							
Saving deposits	\$ 12,218,633	\$ 56,892	1.86%	\$ 13,191,770	\$ 113,731	3.45%	\$ (56,839)
Money market, NOW and interest-bearing checking	23,142,185	121,378	2.10%	15,371,455	117,689	3.06%	3,689
Time deposits	141,055,824	1,282,389	3.64%	112,041,442	1,262,688	4.51%	19,701
Repurchase agreements	23,000,000	266,125	4.63%	23,000,000	265,650	4.62%	475
Total interest-bearing liabilities	<u>199,416,642</u>	<u>1,726,784</u>	3.46%	<u>163,604,667</u>	<u>1,759,758</u>	4.30%	<u>(32,974)</u>
Noninterest-bearing deposits	8,168,473			10,082,725			
Accrued expenses and other liabilities	1,249,723			1,171,093			
Shareholders' equity	14,269,387			20,416,573			
Total Liabilities and Equity	<u>\$223,104,225</u>			<u>\$195,275,058</u>			
Net interest income		<u>\$ 1,162,058</u>			<u>\$ 1,538,683</u>		<u>\$ (376,625)</u>
Interest spread			<u>1.78%</u>			<u>2.58%</u>	
Interest margin			<u>2.11%</u>			<u>3.21%</u>	

(1) Includes \$40,616,792 in non-accruing loans at September 30, 2009, as compared to \$3,914,726 at September 30, 2008.

Changes in Assets and Liabilities and Fluctuations in Interest Rates

The following table summarizes the variance between interest income and interest expense for the three months ended September 30, 2009 versus September 30, 2008, resulting from changes in the volume of average assets and liabilities and fluctuations in interest rates earned and paid. The changes in interest attributable to both rate and volume have been allocated to both rate and volume based on the relative absolute values of the change in volume and the change in rate.

	Three months ended September 30, 2009 versus 2008		
	Increase (Decrease)	Due to Change in Average	
		Volume	Rate
Interest-earning assets			
Loans	\$ (313,056)	\$ 476,536	\$ (789,592)
Investments	(975)	40,136	(41,111)
Interest-bearing deposits	(108)	(108)	-
Federal funds sold and overnight investments	(37,453)	4,275	(41,728)
Loans held for sale	(58,007)	(43,262)	(14,745)
Total interest-earning assets	<u>(409,599)</u>	<u>477,577</u>	<u>(887,176)</u>
Interest-bearing liabilities			
Savings deposits	(56,839)	(7,856)	(48,983)
Money market, NOW and interest-bearing checking	3,689	47,950	(44,261)
Time deposits	19,701	290,796	(271,095)
Repurchase agreements	475	-	475
Total interest-bearing liabilities	<u>(32,974)</u>	<u>330,890</u>	<u>(363,864)</u>
Net interest income	<u>\$ (376,625)</u>	<u>\$ 146,687</u>	<u>\$ (523,312)</u>

Average Balances, Yields and Rates

The following table presents average balance sheets (daily averages), interest income, interest expense, and the corresponding annualized rates on earning assets and rates paid on interest-bearing liabilities for the nine months ended September 30, 2009 and 2008.

Distribution of Assets, Liabilities and Shareholders' Equity: Interest Rates and Interest Differential

	Nine months ended September 30, 2009			Nine months ended September 30, 2008			Fluctuations in Interest Income/ Expense Total
	Average Balance	Interest Income/ Expense	Average Rate	Average Balance	Interest Income/ Expense	Average Rate	
Interest-earning assets							
Loans (1)	\$164,543,791	\$ 7,635,539	6.19%	\$132,216,954	\$ 7,538,544	7.60%	\$ 96,995
Investments	42,269,002	1,556,797	4.91%	37,957,717	1,623,936	5.70%	(67,139)
Interest-bearing deposits	-	-	-	3,128,493	114,415	4.88%	(114,415)
Federal funds sold and overnight investments	12,157,838	13,953	0.15%	9,238,364	178,647	2.58%	(164,694)
Loans held for sale	336,686	11,961	4.74%	5,562,064	298,751	7.16%	(286,790)
Total interest-earning assets	<u>219,307,317</u>	<u>9,218,250</u>	5.60%	<u>188,103,592</u>	<u>9,754,293</u>	6.91%	<u>(536,043)</u>
Cash and due from banks	2,444,412			1,537,867			
Leasehold improvements and equipment, net	662,571			791,847			
Allowance for loan losses	(2,695,919)			(1,645,869)			
Other	<u>1,889,823</u>			<u>1,949,191</u>			
Total Assets	<u>\$221,608,204</u>			<u>\$190,736,628</u>			
Interest-bearing liabilities							
Saving deposits	\$ 11,355,177	\$ 194,551	2.28%	\$ 12,048,060	\$ 335,018	3.71%	\$ (140,467)
Money market, NOW and interest-bearing checking	16,504,710	282,957	2.29%	10,169,451	232,945	3.05%	50,012
Time deposits	146,547,408	4,312,944	3.92%	112,618,338	4,071,872	4.82%	241,072
Repurchase agreements	23,000,000	788,763	4.57%	23,000,000	791,396	4.59%	(2,633)
Line of Credit	-	-	-	3,285	68	2.76%	(68)
Total interest-bearing liabilities	<u>197,407,295</u>	<u>5,579,215</u>	3.77%	<u>157,839,134</u>	<u>5,431,299</u>	4.59%	<u>147,916</u>
Noninterest-bearing deposits	7,466,508			10,378,887			
Accrued expenses and other liabilities	1,186,929			1,213,629			
Shareholders' equity	<u>15,547,472</u>			<u>21,304,978</u>			
Total Liabilities and Equity	<u>\$221,608,204</u>			<u>\$190,736,628</u>			
Net interest income		<u>\$ 3,639,035</u>			<u>\$ 4,322,994</u>		<u>\$ (683,959)</u>
Interest spread			<u>1.84%</u>			<u>2.32%</u>	
Interest margin			<u>2.21%</u>			<u>3.06%</u>	

(1) Includes \$40,616,792 in non-accruing loans at September 30, 2009, as compared to \$3,914,726 at September 30, 2008.

Changes in Assets and Liabilities and Fluctuations in Interest Rates

The following table summarizes the variance between interest income and interest expense for the nine months ended September 30, 2009 versus September 30, 2008, resulting from changes in the volume of average assets and liabilities and fluctuations in interest rates earned and paid. The changes in interest attributable to both rate and volume have been allocated to both rate and volume based on the relative absolute values of the change in volume and the change in rate.

	Nine months ended September 30, 2009 versus 2008		
	Increase (Decrease)	Due to Change in Average	
		Volume	Rate
Interest-earning assets			
Loans	\$ 96,995	\$ 1,648,381	\$ (1,551,386)
Investments	(67,139)	172,915	(240,054)
Interest-bearing deposits	(114,415)	(114,415)	-
Federal funds sold and overnight investments	(164,694)	43,101	(207,795)
Loans held for sale	(286,790)	(210,809)	(75,981)
Total interest-earning assets	<u>(536,043)</u>	<u>1,539,173</u>	<u>(2,075,216)</u>
Interest-bearing liabilities			
Savings deposits	(140,467)	(18,303)	(122,164)
Money market, NOW and interest-bearing checking	50,012	119,113	(69,101)
Time deposits	241,072	1,085,663	(844,591)
Repurchase agreements	(2,633)	-	(2,633)
Line of Credit	(68)	(68)	-
Total interest-bearing liabilities	<u>147,916</u>	<u>1,186,405</u>	<u>(1,038,489)</u>
Net interest income	<u>\$ (683,959)</u>	<u>\$ 352,768</u>	<u>\$ (1,036,727)</u>

Provision for Loan Losses

The provision for loan losses for the three months ended September 30, 2009 and 2008, was \$3,714,000 and \$185,000, respectively. The provision for loan losses for the nine months ended September 30, 2009 and 2008 was \$5,063,000 and \$724,000, respectively. The provision for loan losses for the three- and nine-month periods ended September 30, 2009 reflects the loan growth experienced for those periods, and the negative impact on certain borrowers due to the weakened economy, which resulted in a \$2,917,000 specific reserve being established for sixteen impaired loans as of September 30, 2009, as compared to a specific reserve of \$139,000 for one loan as of September 30, 2008. The amount of the provision for loan losses represents the amount considered necessary by management to maintain an adequate allowance for loan losses based on management's analysis of risks inherent in the loan portfolio.

The allowance for loan losses totaled \$7,154,000 or 4.16% of total gross loans as of September 30, 2009, and \$1,862,000 or 1.24% of total gross loans as of September 30, 2008. The increase in the percentage of allowance for loan losses to total gross loans at September 30, 2009 primarily reflects the negative impact on certain borrowers due to the weakened economy.

Noninterest income (loss)

Non-interest income increased \$194,000 from \$127,000 for the three months ended September 30, 2008 to \$321,000 for the three months ended September 30, 2009. This increase primarily reflects the \$574,000 increase in gains recognized on the sale of investments from \$86,000 during the third quarter of 2008 compared to \$660,000 during the third quarter of 2009. These gains were partially offset by an additional \$438,000 other-than-temporary impairment charge recognized during the third quarter of 2009 related to credit quality of the Bank's private label collateralized mortgage obligations, compared to no such charges against income in the third quarter of 2008.

For the nine months ended September 30, 2009, as compared to the nine months ended September 30, 2008, non-interest income decreased \$2.2 million (345.4%) from income of \$638,000 to a loss of \$(1.6) million, respectively. The change in non-interest income (loss) reflects the \$2,476,000 of other-than-temporarily impaired charges during the nine months ended September 30, 2009 related to the credit quality of the Bank's private label collateralized mortgage obligations, as compared to no such charges experienced during the nine months ended September 30, 2008. These charges were partially offset by the \$259,000 (64.5%) increase in gains on the sales of securities from \$401,000 during the nine months ended September 30, 2008 to \$660,000 during the nine months ended September 30, 2009.

Noninterest expense

Total non-interest expense for the three months ended September 30, 2009 increased \$242,000 (15.1%) from \$1,599,000 for the three months ended September 30, 2008 to \$1,841,000 for the three months ended September 30, 2009. This increase primarily reflects the \$141,000 of expenses related to foreclosures of properties securing loans placed on non-accrual status during the three months ended September 30, 2009, as compared to no such expenses during the three months ended September 30, 2008. The increase in non-interest expenses also reflects increases in salaries and benefits expense, professional fees and FDIC insurance, which were partially offset by planned reductions in occupancy expense, commissions expense and legal expense.

Increases in non-interest expense for the three months ended September 30, 2009 compared to the three months ended September 30, 2008 are due to the following reasons: The \$102,000 (17.2%) increase in salaries and benefits from \$591,000 during the three months ended September 30, 2008 compared to \$693,000 for the three months ended September 30, 2009 primarily reflects the hiring in the fourth quarter of 2008 of two former consultants. One of the consultants, a former member of the FDIC, was hired as the Bank's Compliance Officer and the other was hired to assist in the loan documentation area. The \$62,000 (29.6%) increase in professional fees from \$208,000 during the three months ended September 30, 2008 to \$270,000 for the three months ended September 30, 2009 primarily reflects the cost for the services of two experienced loan work-out specialists retained in June 2009, as compared to no such consulting costs incurred in the same period of the prior year. The \$55,000 (61.7%) increase in FDIC insurance from \$89,000 for the three months ended September 30, 2008 to \$144,000 for the three months ended September 30, 2009 reflects increased deposit levels as well as increased premiums related to FDIC insurance being provided on deposits up to \$250,000 in 2009, as compared to up to \$100,000 in 2008.

The causes of the planned reductions in non-interest expense which partially offset the increases noted for the three months ended September 30, 2009, as compared to the three months ended September 30, 2008, were as follows: the reduction in occupancy expense of \$77,000 (40.4%) from \$192,000 for the three months ended September 30, 2008 compared to \$115,000 during the three months ended September 30, 2009 primarily reflects the Bank's buy-out of its former lease at 800 Westchester Avenue in Rye Brook, NY, which occurred in November 2008, along with the relocation of staff in January and February 2009 from the Bank's former administrative office facility at 800 Westchester Avenue, Rye Brook, NY, to its branch at 601 North Main Street in Port Chester, NY, and to another existing leased facility in Greenwich, CT. Commissions paid on loan closings decreased \$58,000 (97.3%) from \$60,000 for the three months ended September 30, 2008 to \$2,000 for the three months ended September 30, 2009, due to the Bank's focus on traditional commercial banking. The \$30,000 (26.7%) reduction in legal expense from \$111,000 for the three months ended September 30, 2008 to \$81,000 for the three months ended September 30, 2009 primarily reflects a reduction in legal services relating to regulatory issues that were incurred during the three months ended September 30, 2008 with no such similar expenses incurred during the three months ended September 30, 2009.

Total non-interest expense for the nine months ended September 30, 2009 increased \$383,000 (7.0%) from \$5,484,000 for the nine months ended September 30, 2008 to \$5,867,000 for the nine months ended September 30, 2009, which primarily reflects the write-down in the value of other real estate owned ("OREO"), expenses related to foreclosures of properties securing loans placed on non-accrual status as well as increases in salaries and employee benefits and FDIC insurance. These increases were partially offset by planned reductions in occupancy expenses, commissions, legal expenses and professional fees.

Increases in non-interest expense for the nine months ended September 30, 2009 compared to the nine months ended September 30, 2008 are due to the following reasons: the \$375,000 write-down in the value of OREO was due to the decline in the property's appraised value, based on the receipt of an updated appraisal in June 2009, as compared to no such write-down during the nine months ended September 30, 2008. Expenses relating to foreclosures of properties securing loans placed on non-accrual status totaled \$289,000 during the nine months ended September 30, 2009, as compared to \$79,000 during the nine months ended September 30, 2008. The \$83,000 (4.1%) increase in salaries and benefits from \$2,036,000 during the nine months ended September 30, 2009 compared to \$2,119,000 for the nine months ended September 30, 2008 primarily reflects the hiring in the fourth quarter of 2008 of two former consultants. The increase in FDIC insurance of \$251,000 (76.5%) from \$327,000 for the nine months ended September 30, 2008 to \$578,000 for the nine months ended September 30, 2009 reflects increased deposit levels as well as increased premiums related to FDIC insurance being provided on deposits up to \$250,000 in 2009, as compared to up to \$100,000 in 2008. The increase also includes the \$105,000 special FDIC insurance assessment incurred in June 2009, with no such special assessment incurred in 2008.

The causes of the planned reductions in non-interest expense which partially offset the increases noted for the nine months ended September 30, 2009 as compared to the nine months ended September 30, 2008 were as follows: the \$238,000 (39.5%) reduction in occupancy expense from \$604,000 for the nine months ended September 30, 2008 to \$365,000 for the nine months ended September 30, 2009, primarily reflects the reduction in rent expense as a result of

the Bank's buy-out of its former lease at 800 Westchester Avenue in Rye Brook, NY, which occurred in November 2008, along with the relocation of staff in January and February 2009 from the Bank's former administrative office facility at 800 Westchester Avenue, Rye Brook, NY, to its branch at 601 North Main Street in Port Chester, NY, and to another existing leased facility in Greenwich, CT. Commissions paid on loan closings decreased \$244,000 (96.3%) from \$253,000 for the nine months ended September 30, 2008 to \$9,000 for the nine months ended September 30, 2009, due to the Bank's focus on traditional commercial banking. Legal expenses decreased \$204,000 (40.3%) from \$507,000 for the nine months ended September 30, 2008 to \$303,000 for the nine months ended September 30, 2009, which primarily reflects reduction in legal services relating to regulatory issues that were incurred during the nine months ended September 30, 2008, as compared to no such similar expenses incurred during the nine months ended September 30, 2009. The \$45,000 (6.9%) reduction in professional fees from \$652,000 for the nine months ended September 30, 2008 to \$607,000 for the nine months ended September 30, 2009 reflects a reduction in fees related to two individuals, whose expenses had been recorded in professional fees during 2008, but who were hired as Bank employees for compliance and lending purposes during the fourth quarter of 2008, and therefore such expenses were not recorded in professional fees during 2009. This reduction was partially offset by the consultants hired in June 2009 for loan collection and loan work-outs as a result of the increases in impaired loans during 2009.

Net interest margin

Net interest margin for the three months and nine months ended September 30, 2009 was 2.11% and 2.21%, as compared to 3.21% and 3.06% for the three months and nine months ended September 30, 2008. The decrease in net interest margin for the three months ended September 30, 2009 compared to the three months ended September 30, 2008 reflects the negative impact on interest income resulting from the increase in non-accrual loans and the decrease in prevailing interest rates. The yield on loans decreased 1.33% and 0.72%, respectively, from 7.52% and 7.60%, respectively, for the three months and nine months ended September 30, 2008 to 5.55% and 6.19%, respectively, for the three months and nine months ended September 30, 2009. Non-accrual loans increased \$36.7 million from \$3.9 million at September 30, 2008 to \$40.6 million at September 30, 2009. Non-accrual construction loans accounted for \$27.6 million (68.1%) of the total increase in non-accrual loans compared to no such loans being on non-accrual status at September 30, 2008. The majority of the non-accrual construction loans at September 30, 2009 totaling \$20.8 million are for speculative one-to-four family housing.

The decline in the prevailing interest rates unfavorably impacted the yield on other interest-earning assets, while favorably impacting the cost of interest-bearing liabilities. The increased earning asset volume is primarily due to increased loan volume, before adjusting for the increase in non-accrual loans. Average loan volume increased \$28.6 million (19.9%) from \$143.6 million for the three months ended September 30, 2008 to \$172.2 million for the three months ended September 30, 2009, and increased by \$32.3 million (24.4%) from \$132.2 million for the nine months ended September 30, 2008 to \$164.5 million for the nine months ended September 30, 2009. The increased loan volume partially offset the negative influences noted above. The Bank continues to manage its interest rate sensitivity, with the goal that the interest rate changes will have a minimal impact on net interest income.

Loss on Average Equity and Average Assets

The loss on average equity for the three months and nine months ended September 30, 2009, was (114.15)% and (75.95)%, respectively, compared to the loss on average equity of (2.32)% and (7.81%) for the three months and nine months ended September 30, 2008, respectively. The loss on average assets for the three months and nine months ended September 30, 2009, was (7.30)% and (5.33)%, compared to the loss on average assets of (0.24)% and (0.87)% for the three months and nine months ended September 30, 2008.

Liquidity

The liquidity ratio is defined as the percentage of liquid assets to total assets. The following categories of assets in the accompanying balance sheet are considered liquid assets: cash and due from banks; federal funds sold and overnight investments; available for sale investments (which have not been pledged to secure the Bank's collateralized lines of credit, municipal deposits or repurchase agreements); and loans held for sale. Liquidity is a measure of the Bank's ability to generate adequate cash to meet financial obligations. The principal cash requirements of a financial institution are to cover downward fluctuations in deposits and increases in its loan portfolio. Additional liquidity is also provided by the Bank's lines of credit. The Bank has in place a \$5.0 million overnight secured line of credit with a correspondent bank, and a \$1.0 million secured line of credit with the Federal Reserve Bank of New York to meet daily needs. No borrowings were made against either of these lines during the three months and nine months ended September 30, 2009.

Management believes that the Bank's short-term assets provide excess liquidity with liquid assets of approximately \$35.9 million (16.1% of total assets) at September 30, 2009, and \$23.5 million (11.2% of total assets) at December 31, 2008. The existing excess liquidity at September 30, 2009, will be used to fund new loans for both portfolio and sale, as well as to meet potential fluctuations in deposits. As the Bank begins to fund loans at higher rates than liquid assets, the liquidity ratio will be reduced to a targeted level of approximately 10% of total assets.

Capital

In a letter dated August 19, 2009, the FDIC notified the Bank that as of June 30, 2009, it fell within the adequately capitalized category under the regulatory framework for prompt corrective action. To be categorized as "well capitalized," the Bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios. As of September 30, 2009, the Bank meets the "well capitalized" standard for the Tier 1 risk-based capital ratio and the "adequately capitalized" standard for the Tier 1 leverage ratio. For the total risk-based capital ratio, the Bank is considered "undercapitalized."

The following table illustrates the Bank's regulatory capital ratios as of the dates indicated:

	<u>September 30, 2009</u>		<u>December 31, 2008</u>	
	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>
	(Dollars in thousands)			
Total Capital to Risk-Weighted Assets	\$ 12,962	7.48%	\$21,635	12.71%
Tier 1 Capital to Risk-Weighted Assets	\$ 10,735	6.20%	\$19,591	11.51%
Tier 1 (Leverage) Capital to Average Assets	\$ 10,735	4.81%	\$19,591	9.65%

Capital adequacy is one of the most important factors used to determine the safety and soundness of individual banks. Under capital adequacy guidelines, an institution is required to maintain total risk-based capital ratio, Tier 1 risk-based capital ratio and Tier 1 leverage ratio of at least 8%, 4% and 4%, respectively. Based on the above ratios, the Bank does not meet the minimum total risk-based capital ratio of 8%.

On September 1, 2009, the Bank contracted the services of Laidlaw & Company (UK), Ltd., an investment banking firm, to develop a capital plan in order to raise an additional \$15 to \$20 million of capital, pending regulatory and shareholder approval.

Market Risk

Market risk is defined as the sensitivity of income to fluctuations in interest rates, foreign exchange rates, equity prices, commodity prices and other market-driven rates or prices. Based on the nature of the Bank's business, market risk is primarily limited to interest rate risk, defined as the impact of changing interest rates on current and future earnings.

The Bank's goal is to maximize long-term profitability, while minimizing its exposure to interest rate fluctuations. The first priority is to structure and price the Bank's assets and liabilities to maintain an acceptable interest rate spread, while reducing the net effect of changes in interest rates. In order to reach an acceptable interest rate spread, the Bank must generate loans and seek acceptable long-term investments to replace lower yielding balances in Federal funds sold. The focus also must be on maintaining a proper balance between the timing and volume of assets and liabilities re-pricing within the balance sheet. One method of achieving this balance is to originate variable rate loans for the portfolio to offset the short-term re-pricing of the liabilities. In fact, a number of interest-bearing deposit products have no contractual maturity. Customers may withdraw funds from their accounts at any time; deposit balances may therefore run off unexpectedly due to changing market conditions.

The exposure to interest rate risk is monitored by the Bank's Senior Management and is reported to the Bank's Asset and Liability Management Committee on a quarterly basis. Management reviews the interrelationships within the balance sheet to maximize net interest income within acceptable levels of risk.

Impact of Inflation and Changing Prices

The Bank's consolidated financial statements have been prepared in terms of historical dollars, without considering changes in the relative purchasing power of money over time due to

inflation. Unlike most industrial companies, virtually all of the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates have a more significant impact on a financial institution's performance than the effect of general levels of inflation. Interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services. Notwithstanding this fact, inflation can directly affect the value of loan collateral, in particular, real estate. Inflation, or disinflation, could significantly affect the Bank's earnings in future periods.

“Safe Harbor” Statement under Private Securities Litigation Reform Act of 1995

Some of the statements under “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and elsewhere in this Report on Form 10-Q may include forward-looking statements which reflect our current views with respect to future events and financial performance. Statements which include the words “expect,” “intend,” “plan,” “believe,” “project,” “anticipate” and similar statements of future or forward-looking nature identify forward-looking statements for purposes of the federal securities laws or otherwise. All forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause actual results to differ materially from those indicated in these statements or that could adversely affect the holders of our common stock. These factors include, but are not limited to, (1) changes in prevailing interest rates that would affect the interest earned on the Bank’s interest-earning assets and interest paid on its interest-bearing liabilities, (2) the timing of re-pricing of the Bank’s interest-earning assets and interest-bearing liabilities, (3) the effect of changes in governmental monetary policy, (4) the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard setters, (5) changes in competition among financial service companies, including possible further encroachment of non-banks on services traditionally provided by banks and the impact of recently enacted federal legislation, (6) the ability of competitors which are larger than the Bank to provide products and services that are impractical for the Bank to provide, (7) the volatility of quarterly earnings, due in part to the variation in number, dollar volume, and profit realized from the brokering and sale of loans held for sale in different quarters, (8) the effect of the loss of any executive officer, key personnel, or director, (9) the effect of the Bank’s opening branches and the receipt of regulatory approval to complete such actions, (10) the concentration of the Bank’s business in its market area, (11) the concentration of the Bank’s loan portfolio in construction loans and commercial loans to small- and medium-sized businesses, which may be affected more severely than larger businesses during periods of economic weaknesses, (12) the lack of seasoning in the Bank’s loan portfolio, which may increase risk for future credit defaults, (13) volatility and disruption in national and international financial markets, (14) changes in the level of non-performing assets and charge-offs, (15) the costs and effects of legal and regulatory developments including the resolution of legal proceedings or regulatory or governmental inquiries and the results of regulatory examinations or review, and (16) the Bank’s success at managing the risks involved in the foregoing items. Other such factors may be described in other filings made by the Bank with the FDIC.

Although the Bank believes that it offers both the loan and deposit products and has the resources needed for success, future revenues and interest spreads and yields cannot be reliably predicted. These trends may cause the Bank to adjust its operations in the future. Because of the

foregoing and other factors, recent results should not be considered reliable indicators of future financial results.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Bank is a “smaller reporting company” and, accordingly, is not required to provide the information required by this Item.

Item 4. Controls and Procedures

Not applicable.

Item 4T. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

Based on an evaluation of the Bank’s disclosure controls and procedures performed by its Chief Executive Officer and its Chief Financial Officer as of the end of the period covered by this report, the Bank’s Chief Executive Officer and its Chief Financial Officer concluded that the Bank’s disclosure controls and procedures have been effective during the period covered by this report.

As used herein, “disclosure controls and procedures” means controls and other procedures of the Bank that are designed to ensure that information, required to be disclosed by the Bank in the reports it files or submits under the Securities Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the applicable rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by the Bank in the reports it files or submits under the Securities Exchange Act is accumulated and communicated to the Bank’s management, including its principal executive officer or officers and its principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

(b) Changes in Internal Control over Financial Reporting

There have not been any material changes in the Bank’s internal controls or in other factors that occurred during the quarter ended September 30, 2009, that have materially affected or are reasonably likely to materially affect the Bank’s internal control over financial reporting.

**PART II
OTHER INFORMATION**

Item 1. Legal Proceedings

The information contained in Note 16 to the financial statements under “Legal Proceedings” included herein is hereby incorporated in response to this Item 1.

Item 1A. Risk Factors

Not applicable.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

During the quarter ended September 30, 2009, the Bank had no unregistered sales of securities nor did it repurchase any of its Common Stock.

Item 3. Defaults upon Senior Securities

Not applicable.

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

Not applicable.

Item 5. Other Information

Not applicable.

Item 6. Exhibits

Exhibit No.	Description
31.1	Certification by Chief Executive Officer Pursuant to Rule 13a-14.
31.2	Certification by Chief Financial Officer Pursuant to Rule 13a-14.
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes–Oxley Act of 2002.
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes–Oxley Act of 2002.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

USA Bank

Date: November 18, 2009

/s/ Ronald J. Gentile

Name: Ronald J. Gentile
President and Chief Executive Officer

Date: November 18, 2009

/s/ Paul V. Erwin

Name: Paul V. Erwin
Senior Vice President and Chief Financial
Officer and Secretary

**CERTIFICATION
BY PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO RULE 13a-14**

I, Ronald J. Gentile, certify that:

1. I have reviewed this quarterly report on Form 10-Q of USA Bank;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Ronald J. Gentile

Name: Ronald J. Gentile
President and Chief Executive Officer
(Principal executive officer)

Date: November 18, 2009

**CERTIFICATION
BY PRINCIPAL FINANCIAL OFFICER
PURSUANT TO RULE 13a-14**

I, Paul V. Erwin, certify that:

1. I have reviewed this quarterly report on Form 10-Q of USA Bank;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Paul V. Erwin

Name: Paul V. Erwin
Senior Vice President, Chief Financial Officer,
and Secretary
(Principal financial officer)

Date: November 18, 2009

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES–OXLEY ACT OF 2002

In connection with the Quarterly Report of USA BANK (the “*Bank*”) on Form 10-Q for the period ended September 30, 2009, as transmitted for filing with the Federal Deposit Insurance Corporation on the date hereof (the “*Report*”), I, Ronald J. Gentile, the Chief Executive Officer of the Bank, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes–Oxley Act of 2002, that:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank.

Date: November 18, 2009

/s/ Ronald J. Gentile

Name: Ronald J. Gentile

President and Chief Executive Officer

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES–OXLEY ACT OF 2002

In connection with the Quarterly Report of USA BANK (the “*Bank*”) on Form 10-Q for the period ended September 30, 2009, as transmitted for filing with the Federal Deposit Insurance Corporation on the date hereof (the “*Report*”), I, Paul V. Erwin, the Chief Financial Officer of the Bank, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes–Oxley Act of 2002, that:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank.

Date: November 18, 2009

/s/ Paul V. Erwin

Name: Paul V. Erwin
Senior Vice President, Chief Financial Officer
and Secretary