BANK OF SOUTH CAROLINA CORP
Form 10-K
March 08, 2010

U.S. SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

x ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2009

¨ TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from __________ to __________

Commission file number: U0-27702U

BANK OF SOUTH CAROLINA CORPORATION
(Exact name of registrant as specified in its charter)

South Carolina (State or other jurisdiction of incorporation or organization)	57-1021355 (IRS Employer Identification Number)
256 Meeting Street, Charleston, SC (Address of principal executive offices)	29401 (Zip Code)

Issuer's telephone number: (843) 724-1500

Securities registered under Section 12(b) of the Exchange Act:
Common Stock
(Title of Class)

Securities registered under Section 12(g) of the Exchange Act: NONE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. ¨ Yes x No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. ¨ Yes x No

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant’s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10K or any amendment to this Form 10-K. o

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

Large accelerated filer ¨ Accelerated Filer ¨ Non-accelerated filer ¨ Smaller reporting Company x

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

Aggregate market value of the voting stock held by non-affiliates, computed by reference to the closing price of such stock on June 30, 2009 was: $29,542,427

As of February 26, 2010, the Registrant has out standing 4,002,910 shares of common stock.

BANK OF SOUTH CAROLINA CORPORATION
AND SUBSIDIARY

Table of Contents

		Page
	PART I	
Item 1.	Business	3
Item 1A.	Risk Factors	5
Item 1B.	Unresolved Staff Comments	5
Item 2.	Description of Properties	5
Item 3.	Legal Proceedings	5
	PART II	
Item 4.	Market for Common Equity, Related Stockholder Matters and Issuers Purchases of Equity Securities	6
Item 5.	Selected Financial Data	8
Item 6.	Management's Discussion and Analysis of Financial Condition and Results of Operations	9
Item 6A	Quantitative and Qualitative Disclosures About Market Risk	15
Item 7.	Financial Statements and Supplementary Data	29
Item 8.	Changes In and Disagreements with Accountants on Accounting and Financial Disclosure	58
Item 8A(T).	Controls and Procedures	58
Item 8B.	Other Information	59
	PART III	
Item 9.	Directors, Executive Officers, and Corporate Governance of the Registrant	59
Item 10.	Executive Compensation	60
Item 11.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	60
Item 12.	Certain Relationships and Related Transactions and Director Independence	60
Item 13.	Principal Accountant Fees and Services	61
	Part IV	
Item 14.	Exhibits, Financial Statement Schedules	61

PART I

Item 1. Business

The Bank of South Carolina (the "Bank") was organized on October 22, 1986 and opened for business as a state-chartered financial institution on February 26, 1987, in Charleston, South Carolina. The Bank was reorganized into a wholly-owned subsidiary of Bank of South Carolina Corporation (the "Company"), effective April 17, 1995. At the time of the reorganization, each outstanding share of the Bank was exchanged for two shares of Bank of South Carolina Corporation Stock.

The Company, a bank holding company within the meaning of the Bank Holding Company Act of 1956, (the "BHCA"), as amended, is subject to regulation and supervision by the Board of Governors of the Federal Reserve System (the "Federal Reserve"). In addition the Company is registered under the laws of the South Carolina Bank Holding Company Act, and therefore is also subject to regulation by the South Carolina State Board of Financial Institutions. The Company is required to file annual reports and other information with the Federal Reserve and the South Carolina State Board of Financial Institutions regarding its financial condition, results of operations, management and intercompany relationships and transactions between the Company and its subsidiaries. Compliance with federal, state and local provisions regulating the discharge of materials into the environment had no material effect on the capital expenditures, earnings and competitive position of the Bank in fiscal year ended December 31, 2009.

The Company's subsidiary bank, The Bank of South Carolina, is an FDIC insured state chartered financial institution, and as such, is subject to various statutory requirements, supervision and regulation, of which regular bank examinations are a part, promulgated and enforced primarily by the Federal Deposit Insurance Corporation (FDIC), through which the Bank is insured, and the South Carolina State Board of Financial Institutions. Since the primary asset of the Company is its wholly-owned subsidiary, the majority of the following discussion relates to the Bank.

The Bank serves Berkeley, Charleston and Dorchester counties (the "Tri-County Area") as an independent, community-oriented commercial bank concentrating on individuals and small and medium-sized businesses desiring a high level of personalized services. The four banking house locations of the Bank include: 256 Meeting Street, Charleston, SC, 100 North Main Street, Summerville, SC, 1337 Chuck Dawley Boulevard, Mt. Pleasant, SC and 2027 Sam Rittenberg Boulevard, Charleston, SC. The business of the Bank is not considered to be seasonal nor is the Bank's business dependent on any one industry.

The Bank offers a full range of deposit services. Checking account services include regular non-interest bearing checking accounts as well as interest bearing negotiable order of withdrawal ("NOW") accounts. Savings and certificate of deposit accounts include accounts ranging from a daily maturity (regular savings and also money market accounts) to longer term certificates as authorized by regulation. The Bank offers tiered interest to its customers on both money market and NOW accounts. In addition, Individual Retirement Accounts are available. During 2006, the bank added health savings accounts to its deposit services. All deposit accounts are insured by the FDIC to the full amount permitted by law. Deposit accounts are solicited from individuals, businesses, professional organizations and governmental authorities.

Lending services include a full range of commercial, personal and mortgage loans. The Bank's primary focus is on business lending. The types of commercial loans that are available include both secured and unsecured loans for working capital (including inventory and receivables), business expansion (including acquisition of real estate and improvements) and purchase of machinery and equipment. From time to time the Bank may make real estate loans for land acquisition, land development or construction loans. The types of personal loans that are available include secured and unsecured loans for such purposes as financing automobiles, home improvements, education, lot

acquisition, construction, home equity loans and personal investments. The Bank offers a personal checking account related line of credit. This line of credit is available for both protection against unexpected overdrafts and also for the convenience of having a pre-arranged loan that can be activated simply by a check drawn on a personal checking account. The residential mortgage lending department provides mortgage loans through correspondent relationships. The Bank originates, processes and closes the loan and sells (each individually) to investors on a list preapproved by the Board. The Bank's lending activities are subject to a variety of lending limits imposed by Federal law. While differing limits apply in certain circumstances based on the type of loan or the nature of the borrower, in general the direct, indirect and related credit to a single borrowing entity is limited to 10% of the Bank's unimpaired capital and surplus and up to 15% if approved in advance by the Board of Directors. All loans made to any director or executive officer (limited to overdraft protection) of the Bank must be approved by the Board of Directors and made on terms not more favorable than would be available to a person not affiliated with the bank.

The Bank offers credit cards (through correspondent banking services) including MasterCard (TM) and Visa (TM). The Bank does not have a proprietary automated teller machine but participates in a national ATM network through the Visa Debit Card Program. This service is called "Check Card" by the Bank and also offers purchases by the cardholder where Visa debit cards are accepted worldwide using a direct charge to their checking account. Other services offered, but not limited to, include safe deposit boxes, letters of credit, travelers checks, direct deposit of payroll, social security and dividend payments and automatic payment of insurance premiums and mortgage loans. The Bank offers a courier service and ACH origination service as part of its deposit services for commercial customers. Internet Banking called "ESafe" by the Bank, offers twenty-four hour information, up-to-the minute account activity, automatic transfers or one-time transfers between accounts, actual images of customer checks, and statement viewing. The Bank began offering internet “Bill Pay” services in 2008 on personal accounts and added this feature for business accounts in 2009 through a new product “eCorp”.

The Company (“BKSC”) is publicly traded on the National Association of Securities Dealers Automated Quotations (NASDAQ), and is under the reporting authority of the Securities and Exchange Commission (“SEC”). All of the Company’s electronic filings with the SEC, including its Annual Report on Form 10-K, Quarterly Reports on Form 10Q, Current Reports on Form 8-K and other documents filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, are accessible at no cost on the Bank’s website, www.banksc.com. through the “Investor Relations” link. The Company’s filings are also available through the SEC’s web site at www.sec.gov or by calling 1-800-SEC-0330.

The Company is not an accelerated filer as defined in Rule 12b-2 of the Exchange Act. As a result, the Company qualifies for the extended compliance period with respect to the accountants report on management’s assessment of internal control over financial reporting as required by the PCAOB Auditing Standards No. 5.

The Company’s accounting policies are discussed in Item 7, Note 1 to the Consolidated Financial Statements. Of these significant accounting policies, the Company considers its policies regarding the allowance for loan losses to be its most critical accounting policy due to the significant degree of management judgment. For additional discussion concerning the Company’s allowance for loan losses and related matters, see Item 6, “Allowance for Loan Losses”.

Since January 1, 1986, South Carolina law has permitted regional interstate banking. Pursuant to such law, several of the banks in the Tri-County Area have been acquired by banks with headquarters outside the State of South Carolina. In addition, South Carolina laws permit statewide branching by banks and savings and loan associations. As a result, the Bank encounters strong competition from local and national financial institutions as well as consumer and commercial finance companies, insurance companies, brokerage firms, some of which are not subject to the same degree of regulation and restrictions as the Bank. Many of these competitors have substantially greater resources and lending limits than the Bank has and offer certain services, such as trust and international banking services, which the Bank is not providing. The Bank does, however, provide a means for clearing international checks and drafts through a correspondent bank.

At year- end 2009, the Bank employed 72 people, 1 individual is considered a part time employee, none of whom are subject to a collective bargaining agreement. The Bank provides a variety of benefit programs including an Employee Stock Ownership Plan and Trust, health, life, disability and other insurance. Management believes its relationship with its employees is excellent.

Item 1A. Risk Factors

Not applicable

Item 1B. Unresolved Staff Comments

Not applicable

Item 2. Description of Properties

The Bank's headquarters and main office facility is located at 256 Meeting Street in downtown Charleston, South Carolina. The Bank currently leases this facility. On June 30, 1995 the Bank renegotiated its lease for one hundred forty (140) months with two additional ten-year terms. Base rent was $26,432 monthly payable in advance for the first twenty (20) months and the remaining one hundred twenty (120) months of the term (which began March 1, 1997) and for the two (2) extensions of the original term is $24,801 per month in advance and is adjustable by 4% of the base rent every two years. The rent is payable in equal monthly installments of $31,382. In addition, the Bank leases adjacent parking facilities at $3,042 per month.

In October of 1993, the Bank opened an office at 100 N. Main Street, Summerville, SC. The lease on this facility began on August 9, 1993, with an original termination date of June 30, 1999, with two 5-year options to renew. In June of 2004, the bank was successful in renegotiating its lease which began July 1, 2004. Rent increased from a fixed rate of $2,262 monthly to $30,725 annually with an increase of $3,582 each year thereafter until July 1, 2009. The renegotiated lease allows the bank to remain in its current location with an option to expand. At the end of the five year term (June 30, 2009) The Bank of South Carolina exercised the first of three (3) ten (10) year options for renewal. Rent increased to $3,773 on July 1, 2009, and will be adjusted annually using the current Consumer Price Index (CPI), capped at 3%.

On November 1, 1995, the Bank entered into an agreement with an individual to lease property for construction of a new banking facility at 1337 Chuck Dawley Boulevard, Mt. Pleasant, SC. The original term of the lease is for fifteen (15) years with six (6) additional terms of five (5) years each. The base rent for the first ten (10) years was $2,250 per month paid in advance. Rent for years 11 through 15 and each six (6) option periods shall be adjusted to reflect an annualized return determined by multiplying the average yield on five (5) year U.S. Treasury Notes plus 150 basis points times an assumed raw land value of $325,000. The monthly rent, however, shall never be less than the original rent of $2,250 per month. As of February 26, 2010, the rent has not increased based on the above formula.

In the first quarter of 1997, the Bank purchased one acre of land for approximately $838,000 in order to construct a full service banking office and operations center in the West Ashley community of Charleston. In March, 1998, the two-story, 12,000 square foot facility was completed at a cost of approximately $1,334,000 representing construction costs and furnishings.

All leased properties are in good order and condition.

Item 3. Legal Proceedings

In the opinion of management, there are no legal proceedings pending other than routine litigation incidental to its business involving amounts which are not material to the financial condition of the Company and the Bank. To the knowledge of management, no proceedings have been instituted or are contemplated by or against any governmental authority against or by the Company or the Bank.

5

PART II

Item 4. Market for the Company's Common Equity, Related Stockholder Matters and Issuers Purchases of Equity Securities

There were issued and outstanding 4,002,910 shares of the 12,000,000 authorized shares of common stock of the Company at the close of the Company's fiscal year ended December 31, 2009. These outstanding shares were held by approximately 1,200 shareholders in nominee names and of record on December 31, 2009. The common stock of the Company is traded on The NASDAQ Capital Market under the trading symbol “BKSC”.

The following table sets forth the high and low sales price information as reported by NASDAQ in 2009, 2008 and 2007.

	2009		2008		2007	
	High	Low	High	Low	High	Low
First Quarter	12.88	10.00	15.00	13.50	17.00	15.54
Second Quarter	13.45	10.25	15.01	12.90	16.37	15.10
Third Quarter	14.70	11.14	14.64	11.31	16.48	15.10
Fourth Quarter	12.85	9.50	13.49	9.10	16.30	13.82

The Board of Directors of Bank of South Carolina Corporation declared a quarterly dividend of $.16 per share to shareholders of record March 31, 2009, payable April 30, 2009; $.16 per share to shareholders of record July 10, 2009, payable July 31, 2009.

The Board of Directors of Bank of South Carolina Corporation declared a quarterly dividend of $.16 per share to shareholders of record March 31, 2008, payable April 30, 2008; $.16 per share to shareholders of record July 1, 2008, payable July 31, 2008; $.16 per share to shareholders of record October 1, 2008, payable October 31, 2008; $.16 per share to shareholders of record December 31, 2008, payable January 30, 2009.

The Board of Directors of Bank of South Carolina Corporation declared a quarterly dividend of $.14 per share to shareholders of record March 30, 2007, payable April 30, 2007; $.16 per share to shareholders of record July 2, 2007, payable July 31, 2007; $.16 per share to shareholders of record October 1, 2007, payable October 31, 2007; $.16 per share to shareholders of record December 31, 2007, payable January 31, 2008.

As of January 1, 2010, there were approximately 1,200 shareholders of record with shares held by individuals and in nominee names, and on February 26, 2010, the market price for the common stock of the Company was $9.53.

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

At its December 1995 Board Meeting, the Board of Directors authorized the repurchase of up to 116,462 shares of its common stock on the open market. At its October, 1999 Board meeting, the Board of Directors authorized the repurchase up to 37,812 shares of its common stock on the open market and again at its September, 2001 Board meeting, the Board of Directors authorized the repurchase of up to 45,375 shares of its common stock on the open market. As of the date of this report, 199,501 shares have been repurchased by the Company with 148 shares remaining that are authorized to be repurchased. At the Annual Meeting April 2007, the shareholders’ voted to

increase the number of authorized shares from 6,000,000 to 12,000,000. As of February 26, 2010, there are 4,202,411 shares of common stock issued and 4,002,910 shares of common stock outstanding.

THE BANK OF SOUTH CAROLINA EMPLOYEE STOCK OWNERSHIP PLAN AND TRUST

During 1989, the Board of Directors of the Bank adopted an Employee Stock Ownership Plan and Trust Agreement to provide retirement benefits to eligible employees of the Bank for long and faithful service. The Board of Directors of the Bank approved the cash contribution of $120,000 to The Bank of South Carolina Employee Stock Ownership Plan for the fiscal year ended December 31, 2009. The contribution was made during 2009. An amendment and restatement was made to the Employee Stock ownership plan effective January 1, 2007, approved by the Board of Directors January 18, 2007. An employee of the Bank is eligible to become a participant in the ESOP upon reaching 21 years of age and credited with one year of service (1,000 hours of service). The employee may enter the plan on the January 1st that occurs nearest the date on which the employee first satisfies the age and service requirements described above. No contributions by employees are permitted. The amount and time of contributions are at the sole discretion of the Board of Directors of the Bank. The contribution for all participants is based solely on each participant's respective regular or base salary and wages paid by the Bank including commissions, bonuses and overtime, if any.

A participant becomes vested in the ESOP based upon the employees credited years of service. The vesting schedule is as follows;

- 1 year of service 0% Vested
- 2 Years of Service 25% Vested
- 3 Years of Service 50% Vested
- 4 Years of Service 75% Vested
- 5 Years of Service 100% Vested

The Bank is the Plan Administrator. Thomas C. Stevenson, III, Sheryl G. Sharry and Hugh C. Lane, Jr., currently serve as the Plan Administrative Committee and as Trustees for the Plan. The Plan currently owns 219,185 shares of common stock of Bank of South Carolina Corporation.

Item 5. Selected Financial Data

Consolidated Financial Highlights

U	2009	2008	2007	2006	2005
For December 31:					
Net Income	$ 1,869,854	$ 2,939,297	$ 3,831,244	$ 3,928,263	$ 3,185,006
Selected Year End Balances:					
Total Assets	265,914,758	243,665,930	225,157,090	243,472,740	222,517,526
Total Loans (1)	217,315,936	183,538,172	158,329,035	162,557,288	159,338,650
Investment Securities Available for Sale	36,862,345	37,896,250	35,840,019	40,897,855	39,833,240
Federal Funds Sold	3,779,693	13,352,303	18,357,674	26,857,657	10,600,904
Interest Bearing Deposits in Other Banks	8,269	8,212	8,109	7,990	7,872
Earning Assets	257,966,243	234,794,937	212,534,837	230,320,790	209,780,666
Deposits	229,837,680	214,786,515	197,346,458	215,316,901	197,847,314
Shareholders' Equity	27,567,197	26,808,064	25,692,570	23,640,431	21,505,794
Weighted Average Shares Outstanding-Diluted	3,991,668	3,977,714	3,971,349	3,945,928	3,913,119
For the Year:					
Selected Average Balances:					
Total Assets	257,195,300	228,987,689	236,019,185	232,257,502	225,939,657
Total Loans (1)	202,885,118	165,905,847	162,006,962	159,659,211	147,844,856
Investment Securities Available for Sale	37,325,137	37,210,126	38,810,306	39,330,090	38,596,553
Federal Funds Sold and Resale Agreements	7,095,852	14,475,859	22,548,768	19,893,084	26,109,498
Interest Bearing Deposits in Other Banks	8,241	510,894	8,049	7,931	7,824
Earning Assets	247,314,348	218,102,726	223,374,085	218,890,316	212,558,731
Deposits	223,770,359	200,955,703	209,104,665	207,459,557	203,645,606
Shareholders' Equity	27,546,030	26,470,992	24,841,050	22,841,402	20,867,968
Performance Ratios:					
Return on Average Equity	6.79%	11.10%	15.42%	17.20%	15.26%
Return on Average Assets	.73%	1.28%	1.62%	1.69%	1.41%
Average Equity to Average Assets	10.71%	11.56%	10.53%	9.83%	9.24%
Net Interest Margin	4.18%	4.71%	5.13%	5.24%	4.58%
Net (Recoveries) Charge-offs to Average Loans	.38%	.06%	(0.01)%	(0.02)%	0.03%
Allowance for Loan Losses as a Percentage of Total Loans (excluding mortgage loans held for sale)	1.42%	.79%	.85%	.82%	.65%
Per Share:					
Basic Earnings	$ 0.47	$ 0.74	$ 0.97	$ 1.01	$ 0.83

Diluted Earnings	0.47	0.74	0.96	1.00	0.81
Year End Book Value	6.89	6.74	6.50	6.02	5.56
Cash Dividends Declared	0.32	0.64	0.62	0.67	0.51
Dividend Payout Ratio	68.28%	86.44%	63.88%	63.76%	48.39%
Full Time Employee Equivalents	72	67	68	67	64

(1) Including mortgage loans held for sale

All share and per share data have been restated to reflect a 10% stock distribution declared on April 12, 2005 and a 25% stock dividend declared on April 11, 2006.

The following tables, as well as the previously presented consolidated financial highlights, set forth certain selected financial information concerning the Company and its wholly owned subsidiary. The information was derived from audited consolidated financial statements. The information should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations, which follows, and the audited consolidated financial statements and notes which are presented elsewhere in this report.

	For Years Ended December 31,				
	2009	2008	2007	2006	2005
Operating Data:					
Interest and fee income	$ 11,671,949	$ 12,146,820	$ 16,482,178	$ 16,169,958	$ 12,383,548
Interest expense	1,336,329	1,878,778	5,023,086	4,696,492	2,646,198
Net interest income	10,335,620	10,268,042	11,459,092	11,473,466	9,737,350
Provision for loan losses	2,369,000	192,000	40,000	240,000	12,000
Net interest income after provision for loan losses	7,966,620	10,076,042	11,419,092	11,233,466	9,725,350
Other income	2,264,056	1,472,854	1,543,869	1,467,393	1,788,472
Other expense	7,589,461	7,181,641	7,085,401	6,703,716	6,529,267
Income before income taxes	2,641,215	4,367,255	5,877,560	5,997,143	4,984,555
Income tax expense	771,361	1,427,958	2,046,316	2,068,880	1,799,549
Net income	$ 1,869,854	$ 2,939,297	$ 3,831,244	$ 3,928,263	$ 3,185,006
Basic income per share	$ .47	$ .74	$ .97	$ 1.01	$ 0.83
Diluted income per share	$ .47	$ .74	$ .96	$ 1.00	$ 0.81
Weighted average common shares-basic	3,991,668	3,966,193	3,943,067	3,900,707	3,859,351
Weighted average common shares – diluted	3,991,668	3,977,714	3,971,349	3,945,928	3,913,119
Dividends per common share	$ 0.32	$ 0.64	$ 0.62	$ 0.67	$ 0.51

	As of December 31,				
	2009	2008	2007	2006	2005
Balance Sheet Data:					
Investment securities available for sale	$ 36,862,345	$ 37,896,250	$ 35,840,019	$ 40,897,855	$ 39,833,240
Total loans (1)	217,315,936	183,538,172	158,329,035	162,557,288	159,338,650
Allowance for loan losses	3,026,997	1,429,835	1,355,099	1,294,994	1,017,175
Total assets	265,914,758	243,665,930	225,170,090	243,472,740	222,157,526
Total deposits	229,837,680	214,786,515	197,346,458	215,316,901	197,847,314
Shareholders' equity	27,567,197	26,808,064	25,692,570	23,640,431	21,505,794

(1) Including Mortgage loans to be sold

All share and per share data have been restated to reflect a 10% stock distribution declared on April 12, 2005, and a 25% stock dividend declared on April 11, 2006.

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

Management's discussion and analysis is included to assist the shareholders in understanding the Company's financial condition, results of operations, and cash flow. This discussion should be read in conjunction with the audited consolidated financial statements and accompanying notes presented in Item 7 of this report and the supplemental financial data appearing throughout this report. Since the primary asset of the Company is its wholly-owned subsidiary, most of the discussion and analysis relates to the Bank.

DISCUSSION OF FORWARD-LOOKING STATEMENTS

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

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

Such forward looking statements speak only as of the date on which such statements are made and shall be deemed to be updated by any future filings made by the Company with the SEC. The Company will undertake no obligation to update any forward looking statement to reflect events or circumstances after the date on which such statement is made to reflect the occurrence of unanticipated events. In addition, certain statements in future filings by the Company with the SEC, in press releases, and in oral and written statements made by or with the approval of the Company, which are not statements of historical fact, constitute forward looking statements.

OVERVIEW

Bank of South Carolina Corporation (the "Company") is a financial institution holding company headquartered in Charleston, South Carolina, with $265.9 million in assets as of December 31, 2009 and net income of $270,970 and $1,869,854, respectively, for the three and twelve months ended December 31, 2009. The Company offers a broad range of financial services through its wholly-owned subsidiary, The Bank of South Carolina (the "Bank"). The Bank is a state-chartered commercial bank which operates principally in the Charleston, Dorchester and Berkeley counties of South Carolina. The Bank's original and current business plan is to be a full service financial institution specializing in personal service, responsiveness, attention to detail, and long standing relationships.

The following is a discussion of the Company's financial condition and the results of operations as of December 31, 2009 as compared to December 31, 2008 and December 31, 2008 as compared to December 31, 2007. The Company derives most of its income from interest on loans and investments (interest bearing assets). The primary source of funding for making these loans and investments is the Company's deposits (interest bearing liabilities), on which the Company pays interest. Consequently, one of the key measures of the Company's success is the amount of net interest income, or the difference between the income on its interest earning assets, such as loans and investments, and the expense on its interest bearing liabilities such as deposits. Another key measure is the spread between the yield the Company earns on these interest bearing assets and the rate the Company pays on its interest bearing liabilities.

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

In addition to earning interest on loans and investments, the Company also earns income through fees and other expenses it charges to the customer. The following discussion includes various components of this noninterest income as well as our non interest expenses. The discussion and analysis also identifies significant factors that have affected the Company's financial position and operating results and should be read in conjunction with the financial statements and the related notes included in this report. In addition, a number of tables have been included to assist in the discussion.

CRITICAL ACCOUNTING POLICIES

The Company has adopted various accounting policies that govern the application principles generally accepted in the United States and with general practices within the banking industry in the preparation of its financial statements. The Company's significant accounting policies are set forth in the notes to the Company's consolidated financial statements in this report.

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

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

COMPARISON OF THE YEAR ENDED DECEMBER 31, 2009 TO DECEMBER 31, 2008

Net income of $1,869,854, for the year ended December 31, 2009 was a decrease of $1,069,443 or 36.38% from $2,939,297 for the year ended December 31, 2008. Basic and diluted earnings per share decreased from $.74 for the year ended December 31, 2008 to $.47 for the year ended December 31, 2009. The decrease in net income is

primarily due to the decision by the Company to strengthen its reserves for loan losses by more than $2,000,000 in the second half of 2009.

Net interest income is a primary source of revenue. Net interest income is the difference between income earned on assets and interest paid on deposits and borrowings used to support such assets. Net interest income is determined by the rates earned on interest earning assets and the rates paid on interest bearing liabilities, the relative amounts of interest earning assets and interest bearing liabilities, and the degree of mismatch and maturity and repricing characteristics of its interest earning assets and interest bearing liabilities.

Net interest income increased $67,578 to $10,335,620 for the year ended December 31, 2009 from $10,268,042 for the year ended December 31, 2008. Net interest income represented approximately 72.10% of net revenues in 2009 as compared to 75.39% in 2008. Total interest and fee income decreased $474,871 to $11,671,949 for the year ended December 31, 2009, from $12,146,820 for the year ended December 31, 2008. This decrease was mainly due to a decrease in interest on federal funds sold of $305,117. Total interest and fees on loans decreased $64,588 or .63% to $10,154,464 for the year ended December 31, 2009, from $10,219,052 for the year ended December 31, 2008. At the same time interest paid on interest bearing liabilities, interest expense, decreased $542,449 to $1,336,329 for the year ended December 31, 2009. Average interest earning assets increased $29,211,622 to $247,314,348 for the year ended December 31, 2009 from $218,102,726 for 2008. The yield on these average earning assets decreased 85 basis points to 4.72% at December 31, 2009 from 5.57% at December 31, 2008. This increase was primarily due to an increase in the average loan balance of $36,979,271. The average balance of federal funds decreased $7,380,007. As of December 31, 2009, the federal funds target rate was .25%.

Average interest bearing liabilities increased $31,327,516 to $179,114,568 for the year ended December 31, 2009, from $147,787,052 for the year ended December 31, 2008. This increase was primarily due to an increase in both transaction accounts and Certificate of Deposits of $9,845,398 and $16,578,091, respectively. The yield on average interest bearing liabilities decreased 52 basis points from 1.27% in 2008 to .75% in 2009. The increase in average interest bearing liabilities over the increase in average interest bearing assets resulted in a decrease in net average assets thereby contributing to the decline in the net interest margin from 4.71% in 2008 to 4.18% in 2009.

Total interest expense decreased $542,449 to $1,336,329 for the year ended December 31, 2009 from $1,878,778 for the year ended December 31, 2008. This decrease in interest expense is primarily due to the decrease in average cost of deposits. Average interest bearing liabilities increased $31,327,516 for the year ended December 31, 2009. Interest expense on deposit accounts decreased $547,636 or 29.29% to $1,322,019 for the year ended December 31, 2009, from $1,869,655 for the year ended December 31, 2008.

The provision for loan losses is a charge to earnings in a given period to maintain the allowance for loan losses at an adequate level. The provision for loan losses was $2,369,000 for the year ended December 31, 2009 as compared to $192,000 for the year ended December 31, 2008, increasing the allowance for loan losses to $3,026, 997 at December 31, 2009 from $1,429,835 at December 31, 2008. Approximately $1,000,000 of this contribution made in the third quarter was the result of significant growth of the loan portfolio. An additional $1,000,000 was added in the fourth quarter to fully account for and allocate to the total exposure of a specific credit. The allowance for loan losses represents an amount which we believe will be adequate to absorb probable losses on existing loans that may become uncollectible. Management's judgment as to the adequacy of the allowance for loan losses is based on a number of assumptions about future events, which management believes to be reasonable, but which may or may not prove to be accurate. Management's determination of the allowance of loan losses is based on evaluations of the collectability of loans, including consideration of factors such as the balance of impaired loans, the quality, mix and size of the Company's overall loan portfolio, economic conditions that may affect the borrower's ability to repay, the amount and quality of collateral securing the loans, the Company's historical loan loss experience, and a review of specific problem loans. Recognized losses are charged to the allowance with subsequent recoveries added back.

The allowance consists of an allocated and unallocated allowance. The allocated portion is determined by types and ratings of loans within the portfolio. The unallocated portion of the allowance is established for losses that exist in the remainder of the portfolio and compensates for uncertainty in estimating the loan losses. The Company had $842,158 in unallocated reserves at December 31, 2009 as compared to $16,387 at December 31, 2008. This increase is the result of the ongoing economic downturn experienced throughout the market and the nation. Management anticipates funding the provision for loan losses at levels higher than the Company has historically experienced. There can be no assurance that charge-offs of loans in future periods will not exceed the allowance for loan losses as estimated at any point in time or that provisions for loan losses will not be significant to a particular accounting period. In addition the

allowance is subject to examination and testing for adequacy by regulatory agencies. Such regulatory agencies could require management to adjust the allowance based on information available to them at the time of their examination.

During 2009, the Company recorded net charge-offs of $771,838 as compared to net charge-offs of $97,264 in 2008. Impaired loans at December 31, 2009 totaled $2,502,002 an increase of 38.82% over total impaired loans of $1,802,291 at December 31, 2008. Impaired loans include non accrual loans of $627,373 at December 31, 2009 and $75,486 at December 31, 2008. There were no loans at December 31, 2009 or 2008, over 90 days past due that were still accruing interest.

Non-interest income increased $791,202 or 53.72%, to $2,264,056 for the year ended December 31, 2009, from $1,472,854 for the year ended December 31, 2008. Service charge, fees and commissions increased $64,756 as a result of an increase of $128,586 or 61.62% in service charges on business accounts offset by a decrease of $55,249 or 15.84% in overdraft fees. Mortgage banking income increased $548,047 to $1,020,373 for the year ended December 31, 2009, from $472,326 for the year ended December 31, 2008. This increase included an increase for the period of $966,763 in service release premiums, $291,864 in loan origination fees and $130,016 in discount fees earned. With these increases come increases in mortgage expenses. Discount fees paid on mortgage loans increased $431,061 and commissions increased $432,210 in 2009. Interest rates on mortgage loans decreased during 2009 allowing homeowners to refinance at lower rates. In addition this growth was also attributed to first-time homebuyers enticed by low interest rates, falling prices and an $8,000 federal tax credit. In addition the Company recognized a gain of $177,881 on the sale of $10,175,000 available for sale securities and a gain of $2,190 on $660,000 Municipal Security called during the year ended December 31, 2009. The Company recognized a loss of $238 on a $520,000 Municipal Security called during the year ended December 31, 2008.

Bank overhead increased $407,820 to $7,589,461 for the year ended December 31, 2009 from $7,181,641 at December 31, 2008. Other operating expenses increased $401,913 for the period or 24.16%. This increase is primarily due to an increase of $358,400 for the period or 405.30% in fees paid to the FDIC. Back in 2007, as the banking crisis began, the FDIC reinstated a deposit insurance assessment for the purpose of increasing the reserve ratios of the Deposit Insurance Fund. In addition to the regular assessment, the Company also paid a 5% special assessment to the FDIC of $115,808. Salaries and Employee benefits increased $74,642 for the period or 1.79%. This increase was due to the hiring of two new loan officers and annual merit increases. This increase was offset by a decrease of $168,000 in contributions made to the ESOP.

Income tax expense decreased 45.98% to $771,361 at December 31, 2009 from $1,427,958 at December 31, 2008, due to a decrease in income before taxes. This included an increase in bank qualified securities in the investment portfolio. The Company's effective tax rate was approximately 29.20% for the year ended December 31, 2009 compared to 32.70% for the year ended December 31, 2008.

COMPARISON OF THE YEAR ENDED DECEMBER 31, 2008 TO DECEMBER 31, 2007

Net income decreased $891,947 from $3,831,244 for the year ended December 31, 2007, to $2,939,297 for the year ended December 31, 2008, a decrease of 23.28%. Basic and diluted earnings per share decreased from $.97 and $.96, respectively in 2007 to $.74 and $.74, respectively for the year ended December 31, 2008. The decrease in net income is primarily due to a decrease in interest and fees on loans and a decrease in interest on federal funds sold.

Net interest income, the major component of the Company's net income, decreased 10.39% to $10,268,042 for the year ended December 31, 2008, from $11,459,092 for the year ended December 31, 2007. Total interest and fee income decreased 26.30% or $4,335,358, to $12,146,820 for the year ended December 31, 2008, from $16,482,178 for the year ended December 31, 2007. This decrease is due to a decrease in interest and fees on loans and a decrease in interest on federal funds sold. Decreases in the Federal Reserve short-term rates and the resulting decrease in the yields generated on earning assets (from variable rate loan repricing and new loans at lower rates) contributed to this decrease. Total interest and fees on loans decreased $3,350,564 or 24.69% to $10,219,052 for the year ended December 31, 2008, from $13,569,616 for the year ended December 31, 2007. Interest on federal funds sold decreased

$800,790 or 71.53% to $318,695 for the year ended December 31, 2008. As of December 31, 2008, the federal funds target rate, the rate at which banks lend balances at the Federal Reserve to other depository institutions (federal funds sold), was .25%. The federal funds target rate at December 31, 2007 was 4.25%. Net interest income depends upon the volume of and rates associated with interest earning assets and interest bearing liabilities, which result in net interest spread. The average net interest spread increased from 4.12% at December 31, 2007 to 4.30% for the year ended December 31, 2008.

Average interest earning assets decreased $5,271,359, from $223,374,085 for the year ended December 31, 2007 to $218,102,726 for the year ended December 31, 2008. This decrease was primarily due to a decrease in the average balances of federal funds sold of $8,072,909 and investment securities available for sale of $1,600,180. Average loans including mortgage loans held for sale increased $3,898,885, offsetting the decrease in average federal funds sold. The yield on interest earning assets decreased 181 basis points between periods to 5.57% for the year ended December 31, 2008, from 7.38% for the year ended December 31, 2007. This decrease is primarily due to the decrease in the yield on average loans of 222 basis points and the decrease of 291 basis points on federal funds sold to 6.16% and 2.05%, respectively. Average interest bearing liabilities decreased $6,185,251 to $147,787,052 for the year ended December 31, 2008, from $153,972,303 for the year ended December 31, 2007. This decrease is primarily due to a decrease in average transaction accounts and average savings accounts. Average interest-bearing transaction accounts decreased $2,866,890 and average savings accounts decreased $2,130,883 for the year ended December 31, 2008. The yield on average transaction accounts and average savings accounts at December 31, 2008 was .57% and .61%, respectively, compared to 2.82% and 2.59%, respectively, for the year ended December 31, 2007. The yield on average interest bearing liabilities of 1.27% at December 31, 2008 is a decrease of 199 basis points from 3.26% at December 31, 2007.

Total interest expense decreased $3,144,308 or 62.60% to $1,878,778 for the year ended December 31, 2008 from $5,023,086 for the year ended December 31, 2007. The decrease in interest expense is primarily due to the decrease in the average cost of deposits. As noted above average interest bearing liabilities decreased $6,185,251 for the year ended December 31, 2008. Interest expense on deposit accounts decreased $3,113,269 or 62.48% to $1,869,655 for the year ended December 31, 2008, from $4,982,924 for the year ended December 31, 2007.

Total provision for loan losses for the year ended December 31, 2008 was $192,000 compared to $40,000 for the year ended December 31, 2007. Management believes the allowance for loan losses at December 31, 2008, is adequate to cover estimated losses in the loan portfolio; however, assessing the adequacy of the allowance is a process that requires considerable judgment. Management's judgments are based on numerous assumptions about current events which it believes to be reasonable, but which may or may not be valid. Thus there can be no assurance that loan losses in future periods will not exceed the current allowance amount or that future increases in the allowance will not be required. No assurance can be given that management's ongoing evaluation of the loan portfolio in light of changing economic conditions and other relevant circumstances will not require significant future additions to the allowance, thus adversely affecting the operating results of the Company.

The Allowance is also subject to examination testing by regulatory agencies, which may consider such factors as the methodology used to determine adequacy and the size of the Allowance relative to that of peer institutions, and other adequacy tests. In addition, such regulatory agencies could require the Company to adjust its Allowance based on information available to them at the time of their examination. For further discussion, see “Non Accrual and Past Due Loans” and “Allowance for Loan Losses”.

The methodology used to determine the reserve for unfunded lending commitments, which is included in other liabilities, is inherently similar to that used to determine the allowance for loan losses described above adjusted for factors specific to binding commitments, including the probability of funding and historical loss ratio. During the third quarter of the year ended December 31, 2007, Management determined that $20,796 of the allowance for loan loss represented the reserve for unfunded lending commitments and as such this amount was moved from the allowance for loan loss to the allowance for unfunded loans and commitments. In addition $1,507 was added to the provision of unfunded loans and commitments, for the year ending December 31, 2007, based on the methodology referred to above. During the year ended December 31, 2008, the provision for unfunded commitments was decreased by $1,478 bringing the balance to $20,825 at December 31, 2008.

14

Total non interest income decreased $71,015 or 4.60% to $1,472,854 for the year ended December 31, 2008 from $1,543,869 for the year ended December 31, 2007. This decrease was primarily due to a decrease of $82,628 or 14.89% in mortgage banking income. The decrease in mortgage banking income is the result of the slowdown in the real estate market locally and nationally. Mortgage loan origination fees and discount fees earned decreased from $534,395 for the year ended December 31, 2007 to $311,130 for the year ended December 31, 2008, a decrease of 41.78%. During the year ended December 31, 2007, a security was sold at a gain of $69,792, whereas during the year ended December 31, 2008 a municipal bond was sold at a loss of $238, resulting in a decrease of $70,030 or 100.34% in other income. Service charges, fees and commissions increased $95,145 or 10.85% from $877,155 for the year ended December 31, 2007 to $972,300. This increase resulted primarily from an increase in service charges on business accounts of $65,821 and an increase of $25,133 in overdraft fees. The increase in service charges on business accounts is due to a decrease in the earnings credit and the decrease in average balances maintained.

Banking overhead increased $96,240 or 1.36% to $7,181,641 for the year ended December 31, 2008 from $7,085,401 for the year ended December 31, 2007. Other operating expenses increased $103,679 or 6.65% to $1,663,891 for the year ended December 31, 2008 from $1,560,212 for the year ended December 31, 2007. This increase is primarily due to the increase in professional fees and insurance paid to the FDIC which increased $58,727 and $63,304, respectively, for the year ended December 31, 2008. Professional audit and legal fees increased $36,603 due to compliance with Sarbanes Oxley. The increase in insurance paid to the FDIC is due to the FDIC Insurance Reform Legislation. This Legislation allows the FDIC to price deposit insurance according to risk for all insured institutions regardless of the level of the reserve ratio. In 2007 the Company had a credit with the FDIC that was used toward payment of this assessment. These increases were offset by a decrease in salaries and employee benefits of $13,441 due to non replacement of employees who terminated with the Bank during 2008.

Income tax expense decreased $618,358 or 30.22% to $1,427,958 for the year ended December 31, 2008 from $2,046,316 for the year ended December 31, 2007. The company's effective tax rate was approximately 32.70% for the year ended December 31, 2008 compared to 34.82% for the year ended December 31, 2007.

Item 6A. Quantitative and Qualitative Disclosures About Market Risk

ASSET AND LIABILITY MANAGEMENT

The assets and liabilities of the Company are managed to provide a consistent level of liquidity to accommodate normal fluctuations in loans and deposits. At year end 2009, total assets were $265,914,758 an increase of 9.13% from year end 2008, total deposits were $229,837,680, an increase of 7.01% from the end of the previous year, while short-term borrowings, consisting of Demand Notes Issued to U.S. Treasury and funds borrowed from the Federal Reserve Bank's Term Auction Facility (TAF), increased $7,006,753 or 700.68% to $8,006,753 at December 31, 2009 from $1,000,000 at December 31, 2008. (See "Short Term Borrowings" for further discussion)

At December 31, 2009, approximately 97.01% of the Company's assets were earning assets composed of U.S. Treasury, Government Sponsored Enterprises and Municipal Securities in the amount of $36,862,345, Federal Funds Sold and interest bearing deposits in other banks in the amount of $3,787,962 and total loans including mortgage loans held for sale in the amount of $217,315,936.

The yield on a majority of the Company's earning assets adjusts simultaneously with changes in the general level of interest rates. Some of the Company's liabilities are issued with fixed terms and can be repriced only at maturity. In 2006, net interest margin increased 66 basis points to 5.24% for the year ended December 31, 2006, from 4.58% at December 31, 2005, as a result of an increase in loan growth. The Bank's net interest margin decreased 11 basis points from 5.24% at December 31, 2006 to 5.13% at December 31, 2007 due to a decrease in interest rates and a decrease in loan growth. During the year ended December 31, 2008 the net interest margin decreased from 5.13% at December

31, 2007 to 4.71%. The net interest margin at December 31, 2009 was 4.18%.

MARKET RISK

Market risk is the risk of loss from adverse changes in market prices and rates. For the Company, this risk is constituted primarily of interest rate risk in its lending and investing activities as they relate to their funding by deposit and borrowing activities.

The Bank's policy is to minimize interest rate risk between interest bearing assets and liabilities at various maturities and to attempt to maintain an asset positive position over a 6 month period. In adhering to this policy, unless there is a sudden extraordinary drop in interest rates, generally it is anticipated that the Bank's net interest margins will not be materially affected by changes in interest rates. The average net interest rate spread for 2009 decreased to 3.97% from 4.30% for 2008 and the average net interest margin for 2009 decreased to 4.18% from 4.71% for 2008. Management will continue to monitor its asset sensitive position.

Since the rates on most of the Bank's interest bearing liabilities can vary on a daily basis, management continues to maintain a loan portfolio priced predominately on a variable rate basis; however, in an effort to protect future earnings in a declining rate environment, the Bank offers certain fixed rates and terms primarily associated with real estate transactions. The Bank seeks stable, long-term deposit relationships to fund its loan portfolio.

At December 31, 2009, the average maturity of the investment portfolio was 4 years 9.28 months with an average yield of 4.14% compared to 2 year 7.4 months with an average yield of 4.38% at December 31, 2008. Although there is greater market risk with maturity extension, management feels that the core deposit base minimizes the need to sell securities, and the extension of the investment portfolio improves the yield on the portfolio.

The Company does not take foreign exchange or commodity risks. In addition the Company does not own mortgage-backed securities, nor does it have any exposure to the sub-prime market or any other distressed debt instruments.

The following table summarizes the Bank's interest sensitivity position as of December 31, 2009:

Earning Assets (in 000's)	1 Day	Less Than 3 Months	3 Months to Less Than 6 Months	6 Months to Less Than 1 Year	1 Year to Less Than 5 Years	5 years or More	Total	Estimated Fair Value
Loans (1)	$ 152,329	$ 9,923	$ 9,152	$ 8,240	$ 37,645	$ 27	$ 217,316	$ 222,969
Investment securities (2)	-	-	421	5,983	11,598	17,622	35,624	36,862
Short term investments	8	-	-	-	-	-	8	8
Federal funds sold	3,780	-	-	-	-	-	3,780	3,780
Total	$ 156,117	$ 9,923	$ 9,573	$ 14,223	$ 49,243	$ 17,649	$ 256,728	$ 263,619
Interest Bearing Liabilities (in 000's)								
CD's and other time deposits 100,000 and over	$ -	$ 16,506	$ 17,299	$ 6,598	$ 1,527	$ -	$ 41,930	$ 42,034

CD's and other time deposits under 100,000	112	6,346	4,444	4,488	1,553	-	16,943	17,082
Money market and interest bearing demand accounts	113,224	-	-	-	-	-	113,224	113,224
Savings	9,347	-	-	-	-	-	9,347	9,347
Short term borrowings	507	7,500	-	-	-	-	8,007	8,007
	$ 123,190	$ 30,352	$ 21,743	$ 11,086	$ 3,080	$ -	$ 189,451	$ 189,694
Net	$ 32,927	$ (20,429)	$ (12,170)	$ 3,137	$ 46,163	$ 17,649	$ 67,277	$ 76,931
Cumulative		$ 12,498	$ 328	$ 3,465	$ 49,628	$ 67,277		

(1) Including mortgage loans held for sale.

(2) At amortized cost

16

LIQUIDITY

Historically, the Company has maintained its liquidity at levels believed by management to be adequate to meet requirements of normal operations, potential deposit outflows and strong loan demand and still allow for optimal investment of funds and return on assets. The following table summarizes future contractual obligations as of December 31, 2009:

	Total	Payment Due by Period Less than 1 Year	1-5 Years	After 5 Years
Contractual Obligations (in 000's)				
Time deposits	$ 58,873	$ 55,793	$ 3,080	$ -
Short-term borrowings	8,007	8,007	-	-
Operating leases	3,763	487	2,038	1,238
Total contractual cash obligations	$ 70,643	$ 64,287	$ 5,118	$ 1,238

The Bank manages its assets and liabilities to ensure that there is sufficient liquidity to enable management to fund deposit withdrawals, loan demand, capital expenditures, reserve requirements, operating expenses, dividends and to manage daily operations on an ongoing basis. Funds are primarily provided by the Bank through customer's deposits, principal and interest payments on loans, mortgage loan sales, the sale or maturity of securities, temporary investments and earnings.

Proper liquidity management is crucial to ensure that the Company is able to take advantage of new business opportunities as well as meet the credit needs of its existing customers. Investment securities are an important tool in the Company's liquidity management. Securities classified as available for sale, which are not pledged, may be sold in response to changes in interest rates and liquidity needs. All of the securities presently owned by the Bank are classified as Available for Sale. Net cash provided by operations and deposits from customers have been the primary sources of liquidity for the Company. At December 31, 2009, the Bank had unused short-term lines of credit totaling approximately $22,000,000 (which are withdrawable at the lender's option). Additional sources of funds available to the Company for additional liquidity needs include borrowing on a short-term basis from the Federal Reserve System, increasing deposits by raising interest rates paid and selling mortgage loans held for sale. In order to establish a secondary source of liquidity, the Company has established a Borrower-In-Custody arrangement with the Federal Reserve. This arrangement permits the Company to retain possession of assets pledged as collateral to secure advances from the Federal Reserve Discount Window up to $58,036,846 at December 31, 2009. The Company has also pledged Municipal Securities with a market value of $1,050,822 to the Federal Reserve Discount Window. In addition the Company borrowed $7,500,000 from the Federal Reserve Bank’s Term Auction Facility (TAF) at a rate of .25% for a term of forty-two days. The Board of Governor’s of the Federal Reserve System established this program to allow depository institutions to place a bid for an advance from its local Federal Reserve Bank at a fixed interest rate determined via centralized single-price auction. The collateral pledged to secure advances from the Federal Reserve Discount Window, serves as collateral.

Composition of Average Assets

	2009	2008	2007	2006	2005
Loans (1)	$ 202,885,118	$ 165,905,847	$ 162,006,962	$ 159,659,211	$ 147,844,856
	37,325,137	37,210,126	38,810,306	39,330,090	38,596,553

Investment securities available for sale					
Federal funds sold and other investments	7,104,093	14,986,753	22,556,817	19,901,015	26,117,322
Non-earning assets	9,880,952	10,884,963	12,645,100	13,367,186	13,380,926
Total average assets	$ 257,195,300	$ 228,987,689	$ 236,019,185	$ 232,257,502	$ 225,939,657

(1) Including mortgage loans held for sale

17

Average earning assets increased by $28,206,351 from 2008 to 2009. Average earning assets increased primarily as a result of an increase in average loans. Average loans increased $36,979,271 or 22.29% from $165,905,847 for the year ended December 31, 2008 to $202,885,118 for the year ended December 31, 2009.

ANALYSIS OF CHANGES IN NET INTEREST INCOME

The following table shows changes in interest income and expense based upon changes in volume and changes in rates:

	2009 vs. 2008			2008 vs. 2007			2007 vs. 2006		
	Volume	Rate	Net Dollar Change (1)	Volume	Rate	Net Dollar Change (1)	Volume	Rate	Net Dollar Change (1)
Loans (2)	$ 2,045,844	$ (2,110,432)	$ (64,588)	$ 319,364	$ (3,669,928)	$ (3,350,564)	$ 196,646	$ 3,026	$ 199,672
Investment securities available for sale	4,959	(110,125)	(105,166)	(72,076)	(111,928)	(184,004)	(24,006)	4,241	(19,765)
Federal funds sold and and other investments	(113,836)	(191,281)	(305,117)	(289,842)	(510,948)	(800,790)	131,835	478	132,313
Interest Income	$ 1,936,967	$ (2,411,838)	$ (474,871)	$ (42,554)	$ (4,292,804)	$ (4,335,358)	$ 304,475	$ 7,745	$ 312,220
Interest-bearing transaction accounts	$ 51,505	$ (387,556)	$ (336,051)	$ (78,764)	$ (2,224,793)	$ (2,303,557)	$ 35,140	$ (9,146)	$ 25,994
Savings	2,484	(34,835)	(32,351)	(46,710)	(184,617)	(231,327)	(62,831)	(21,002)	(83,833)
Time deposits	416,787	(596,021)	(179,234)	(41,587)	(536,798)	(578,385)	213,789	164,691	378,480
Federal funds purchased	4,200	(74)	4,126	64	0	64	0	0	0
Demand notes issued to U.S. Treasury	(1,801)	(7,258)	(9,059)	(9,429)	(21,674)	(31,103)	6,029	(76)	5,953
Term auction facility	10,120	-	10,120	-	-	-	-	-	-
Interest expense	$ 483,295	$ (1,025,744)	$ (542,449)	$ (176,426)	$ (2,967,882)	$ (3,144,308)	$ 192,127	$ 134,467	$ 326,594
Increase (decrease) in net interest income			$ 67,758			$ (1,191,050)			$ (14,374)

(1) Volume/Rate changes have been allocated to each category based on the percentage of each to the total change.

(2) Including mortgage loans held for sale

YIELDS ON AVERAGE EARNING ASSETS AND RATES ON AVERAGE INTEREST-BEARING LIABILITIES

	2009			2008			2007		
	Average Balance	Interest Paid/ Earned	Average Yield/ Rate (1)	Average Balance	Interest Paid/ Earned	Average Yield/ Rate (1)	Average Balance	Interest Paid/ Earned	Average Yield/ Rate (1)
nterest-Earning ssets									
oans (2)	$ 202,885,118	$ 10,154,464	5.01%	$ 165,905,847	$ 10,219,052	6.16%	$ 162,006,962	$ 13,569,616	8.38%
nvestment ecurities available or sale	37,325,137	1,503,907	4.03%	37,210,126	1,609,073	4.32%	38,810,306	1,793,077	4.62%
ederal funds sold	7,095,852	13,520	0.19%	14,475,859	296,145	2.05%	22,548,768	1,119,366	4.96%
ther investments	8,241	58	0.70%	510,894	22,550	4.41%	8,049	119	1.49%
otal earning assets	$ 247,314,348	$ 11,671,949	4.72%	$ 218,102,726	$ 12,146,820	5.57%	$ 223,374,085	$ 16,482,178	7.38%
nterest-Bearing iabilities:									
nterest earing transaction ccounts	$ 108,542,471	$ 228,938	0.21%	$ 98,697,073	$ 564,989	0..57%	$ 101,563,963	$ 2,868,546	2.82%
avings	9,289,183	21,350	0.23%	8,860,083	53,701	0.61%	10,990,966	285,028	2.59%
ime deposits	56,216,166	1,071,731	1.91%	39,638,075	1,250,965	3.16%	40,580,931	1,829,350	4.51%
ederal funds urchased	575,890	4,190	0.73%	2,732	64	2.34%	-	-	-
emand notes sued to .S. Treasury	442,913	-	0.00%	589,089	9,059	1.54%	836,443	40,162	4.80%
erm auction cility	4,047,945	10,120	0.25%	-	-	0.00%	-	-	0.00%
otal interest earing liabilities	$ 179,114,568	$ 1,336,329	0.75%	$ 147,787,052	$ 1,878,778	1.27%	$ 153,972,303	$ 5,023,086	3.26%
et interest spread			3.97%			4.30%			4.12%
et interest margin			4.18%			4.71%			5.13%
et interest income		$ 10,335,620			$ 10,268,042			$ 11,459,092	

(1) The effect of forgone interest income as a result of non-accrual loans was not considered in the above analysis.
(2) Average loan balances include non-accrual loans and mortgage loans held for sale.

INVESTMENT PORTFOLIO

The following is a schedule of the Bank's investment portfolio as of December 31, 2009, as compared to December 31, 2008, and December 31, 2008 to December 31, 2007:

DECEMBER 31, 2009	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	ESTIMATED FAIR VALUE
U.S. Treasury Notes	$ 2,981,338	$ 137,256	$ -	$ 3,118,594
Government-Sponsored Enterprises	12,026,844	514,975	-	12,541,819
Municipal Securities	20,615,647	675,572	89,287	21,201,932
Total	$ 35,623,829	$ 1,327,803	$ 89,287	$ 36,862,345

DECEMBER 31, 2008	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	ESTIMATED FAIR VALUE
U.S. Treasury Bills	$ 2,964,269	$ 262,137	$ -	$ 3,226,406
Government-Sponsored Enterprises	21,018,810	998,158	-	22,016,968
Municipal Securities	12,489,652	183,123	19,899	12,652,876
Total	$ 36,472,731	$ 1,443,418	$ 19,899	$ 37,896,250

DECEMBER 31, 2007	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	ESTIMATED FAIR VALUE
U.S. Treasury Bills	$ 2,948,002	$ 148,091	$ -	$ 3,096,093
Government-Sponsored Enterprises	21,873,129	466,859	-	22,339,988
Municipal Securities	10,336,322	89,464	21,848	10,403,938
Total	$ 35,157,453	$ 704,414	$ 21,848	$ 35,840,019

The Bank's investment portfolio had a weighted average yield of 4.14%, 4.38% and 4.51% for the years ended December 31, 2009, 2008 and 2007, respectively.

At December 31, 2009, there were four Municipal Securities with an unrealized loss of $89,287 as compared to five Municipal Securities with an unrealized loss of $19,899, at December 31, 2008. These investments are not considered other-than-temporarily impaired. The Company has the ability and the intent to hold these investments until a market price recovery or maturity. The unrealized losses on these investments were caused by interest rate increases. The contractual terms of these investments do not permit the issuer to settle the securities at a price less than the amortized cost of the investment.

LOAN PORTFOLIO COMPOSITION

The following is a schedule of the Bank's loan portfolio, excluding mortgage loans held for sale, as of December 31, 2009, as compared to December 31, 2008, 2007, 2006 and 2005:

	Book Value (in 000's)				
Type	2009	2008	2007	2006	2005
Commercial and industrial loans	$ 48,719	$ 46,840	$ 51,443	$ 53,609	$ 52,373
Real estate loans	158,961	127,405	98,738	99,932	98,619
Loans to individuals for household, family and other personal expenditures	6,036	5,667	5,507	4,872	4,941
All other loans (including overdrafts)	179	226	709	259	170
Total Loans (excluding unearned income)	$ 213,895	$ 180,138	$ 156,397	$ 158,672	$ 156,103

As a Bank with a mission to serve its community, there is a geographic concentration of loans in Charleston, Dorchester and Berkeley Counties.

The Bank had no foreign loans or loans to fund leveraged buyouts (LBO's) during 2009, 2008, 2007, 2006 or 2005.

SELECTED LOAN MATURITY (IN 000'S)

	One year or less	Over one but less than five years	Over five Years	Total
Type				
Commercial and industrial loans	$ 30,735	$ 14,630	$ 3,354	$ 48,719
Real estate loans	43,343	67,789	47,829	158,961
Loans to individuals for household, family and other personal expenditures	3,020	2,684	332	6,036
All other loans (including overdrafts)	115	64	-	179
Total Loans (excluding unearned income)	$ 77,213	$ 85,167	$ 51,515	$ 213,895

IMPAIRED AND RESTRUCTURED LOANS

The Bank had impaired loans totaling $2,502,002 as of December 31, 2009 compared to$1,802,291, $882,269, $10,864, and $80,852 as of December 31, 2008, 2007, 2006 and 2005, respectively. The impaired loans include non-accrual loans with balances at December 31, 2009, 2008, 2007, 2006, and 2005 of $627,373, $75,486, $761,748, $10,864 and $80,852, respectively. The Bank had no restructured loans at December 31, 2009 or 2008, one restructured loan at December 31, 2007, in the amount of $10,567, no restructured loans at December 31, 2006, and one restructured loan included in non accrual loans at December 31, 2005 in the amount of $3,394. Management does not know of any loans, which will not meet their contractual obligations that are not otherwise discussed herein.

20

As of December 31, 2009 and 2008, loans individually evaluated and considered impaired:

	December 31, 2009	December 31, 2008
Total loans considered impaired at period end	$ 2,502,002	$ 1,802,291
Loans considered impaired for which there is a related allowance for loan loss:		
Outstanding loan balance	1,943,599	1,717,813
Related allowance established	1,403,962	930,650
Loans considered impaired for which no related allowance for loan loss was established	558,403	84,478
Average annual investment in impaired loans	2,501,910	1,748,039
Interest income recognized on impaired loans during the period of impairment	$ 87,237	$ 92,149

NON-ACCRUAL AND PAST DUE LOANS

The Bank had $627,373 in non-accrual loans as of December 31, 2009, compared to $75,486, $761,748, $10,864 and $80,852 as of December 31, 2008, 2007, 2006 and 2005, respectively. There were no loans at December 31, 2009 or at December 31, 2008 that were over 90 days past due still accruing interest.

The accrual of interest is generally discontinued on loans, which become 90 days past due as to principal or interest. The accrual of interest on some loans, however, may continue even though they are 90 days past due if the loans are well secured, in the process of collection, and management deems it appropriate. If non-accrual loans decrease their past due status to 30 days for a period of six months, they are reviewed individually by management to determine if they should be returned to accrual status.

ALLOWANCE FOR LOAN LOSSES

The allowance for loan losses represents management's estimate of probable losses inherent in the loan portfolio. The adequacy of the allowance for loan losses (the "Allowance") is reviewed monthly by the Loan Committee and on a quarterly basis by the Board of Directors. For purposes of this analysis, adequacy is defined as a level sufficient to absorb estimated losses in the loan portfolio as of the balance sheet date presented. The methodology employed for this analysis was modified in 2007, 2008 and 2009 to better reflect the economic environment and regulatory guidance. The revised methodology is based on a Reserve Model that is comprised of the three components listed below.

1) Specific Reserve analysis for impaired loans based on FASB ASC 310-10-35.
2) General reserve analysis applying historical loss rates based on FASB ASC 450-20.
3) Qualitative or environmental factors.

Loans are reviewed for impairment which is measured in accordance with FASB ASC 310-10-35. Impaired loans can either be secured or unsecured, not including large groups of smaller balance loans that are collectively evaluated. Impairment is measured by the difference between the loan amount and the present value of the future cash flow discounted at the loan's effective interest rate, or, alternatively the fair value of the collateral if the loan is collateral dependent. An impaired loan may not represent an expected loss.

A general reserve analysis is performed on individually reviewed loans, but not impaired loans, and excluded individually reviewed impaired loans, based on FASB ASC 450-20. Historical losses are segregated into risk-similar groups and a loss ratio is determined for each group over a three year period. The three year average loss ratio by type is then used to calculate the estimated loss based on the current balance of each group. The Company shortened its historical loss percentage for this component from five years to three years. The change resulted in an increase in the historical loss percentage from .087 to .156%. This increase was reasonable given the Company's historical lack of losses and, more importantly, represents the current economic environment.

Qualitative and environmental factors include external risk factors that Management believes are representative of the overall lending environment of the Bank. Management believes that the following factors create a more comprehensive system of controls in which the Bank can monitor the quality of the loan portfolio.

1) Portfolio risk
2) National and local economic trends and conditions
3) Effects of changes in risk selection and underwriting practices
4) Experience, ability and depth of lending management staff
5) Industry conditions
6) Effects of changes in credit concentrations
7) Loan and credit administration risk

Portfolio risk includes the levels and trends in delinquencies, impaired loans and changes in the loan rating matrix, trends in volume and terms of loans and overmargined real estate lending. Management is satisfied with the stability of the past due and non-performing loans and believes there has been no decline in the quality of the loan portfolio due to any trend in delinquent or adversely classified loans. Although the aggregate total of classified loans has increased, Management is confident in the adequacy of the sources of repayment. Sizable unsecured principal balances on a non-amortizing basis are monitored. Within the portfolio risk factor the Company elected to increase the risk percentage for "trends in volume and terms of loan" as a result of the increased volume in its loan portfolio. Loans have increased 18.78% or approximately $33,809,526 from December 31, 2008 to December 31, 2009. In addition the Company elected to increase the risk percentage for "over margined real estate lending risk". Although the vast majority of the Company's real estate loans are underwritten on a cash flow basis, the secondary source of repayment is typically tied to the Company's ability to realize on the collateral. Given the contraction in real estate values, the Company closely monitors its loan to value. The Company recently amended its Loan Policy to allow for a maximum of 80% collateral advance percentage on all real estate transactions.

Occasional extensions of credit occur beyond the policy thresholds of the Company's normal collateral advance margins for real estate lending. These loans are monitored and the balances reported to the Board every quarter. An excessive level of this practice could result in additional examiner scrutiny, competitive disadvantages and potential losses if forced to convert the collateral. The consideration of overmargined real estate loans directly relates to the capacity of the borrower. Management often requests additional collateral to bring the loan to value ratio within the policy guidelines and also require a strong secondary source of repayment in addition to the primary source of repayment.

Although significantly under the threshold of 100% of capital (currently approximately $28 million), the Company's list and number of over margined real estate loans currently totals approximately $15,884,926 or approximately 7.3% of it loan portfolio.

Management revised the credit rating matrix in order to rate all extensions of credit providing a more specified picture of the risk each loan poses to the quality of the loan portfolio. There are eight possible ratings based on ten different qualifying characteristics. The ten characteristics are: cash flow, collateral quality, guarantor strength, financial

condition, management quality, operating performance, the relevancy of the financial statements, historical loan performance, debt service coverage and the borrower's leverage. A weighted average method is used to determine the loan grade with cash flow and financial statements being weighted double. The matrix is designed to meet management's standards and expectations of loan quality. In addition to the rating matrix, the Company rates its credit exposure on the basis of each loan and the quality of each borrower.

National and local economic trends and conditions are constantly changing and results in both positive and negative impact on borrowers. Most macroeconomic conditions are not controllable by the Company and are incorporated into the qualitative risk factors. Natural disasters, wars and the recent fallout of the subprime lending market as well as problems in the traditional mortgage market are a few of the trends and conditions that are currently affecting our national and local economy. Changes in the national and local economy have impacted borrower's ability, in many cases, to repay loans in a timely manner. On occasion a loan's primary source of repayment (i.e., personal income, cash flow, or lease income) may be eroded as a result of unemployment, lack of revenues, or the inability of a tenant to make rent payments.

The quality of the Bank's loan portfolio is contingent upon its risk selection and underwriting practices. Every credit with over $100,000 in exposure is summarized by the Bank's Credit Department and reviewed by the Loan Committee on a monthly basis. The Board of Directors review credits over $500,000 monthly with an annual credit analysis conducted on credits in excess of $350,000 upon the receipt of updated financial information. Prior to any extension of credit, every significant commercial loan goes through sound credit underwriting. The Credit Department conducts detailed cash flow analysis on each proposal using the most current financial information. Relevant trends and ratios are evaluated.

The Bank has over 300 years of lending management experience among eleven members of lending staff. In addition to the lending staff the Bank has an Advisory Board for each branch comprised of business and community leaders from the specific branch's market area. Management meets with these boards quarterly to discuss the trends and conditions in each respective market. Management is aware of the many challenges currently facing the banking industry. Specifically, assessing banks to replenish the insurance fund and its corresponding impact on bank profits, increased regulatory scrutiny in and or on lending practices, pending changes in deposit and or funding source type and mix, to name a few, continue to impact the Company's environment. As other banks look to increase earnings in the short term, the Company will continue to emphasize the need to maintain its sound lending practices and core deposit growth. Accordingly, the Company has elected to increase the risk percentage for this factor.

There has been an influx of new banks within the Company's geographic area. This increase has decreased the local industry's overall margins as a result of pricing competition. Management believes that the borrowing base of the Bank is well established and therefore unsound price competition is not necessary.

The risk associated with the effects of changes in credit concentration includes loan concentration, geographic concentration and regulatory concentration.

As of December 31, 2009, there were only four Standard Industrial Code groups that comprised more than three percent of the Bank's total outstanding loans. The four groups are non-residential building operations, offices and clinics of doctors, real-estate agents and managers and legal services.

The Company is located along the coast and on an earthquake fault, increasing the chances that a natural disaster may impact the Bank and its borrowers. The Company has a Disaster Recovery Plan in place; however, the amount of time it would take for our customers to return to normal operations is unknown.

Loan and credit administration risk includes collateral documentation, insurance risk and maintaining financial information risk.

The majority of the Bank's loan portfolio is collateralized with a variety of its borrower's assets. The execution and monitoring of the documentation to properly secure the loan is the responsibility of the Bank's lenders and Loan Department. The Bank requires insurance coverage naming the Bank as the mortgagee or loss payee. Although insurance risk is also considered collateral documentation risk, the actual coverage, amounts of coverage and

increased deductibles are important to management.

Risk includes a function of time and the borrower's financial condition may change; therefore, keeping financial information up to date is important to the Bank. The policy of the Bank is that all new loans, regardless of the customer's history with the Bank, should have updated financial information, as long as exposure is greater than $10,000.

The aforementioned changes to the Company's Allowance for Loan Loss methodology were not made as a result of dramatic or patterned history of loan losses, increase in past due loans, or non-performing assets, but rather because of specific changes in the Company's lending environment. These changes have precipitated the need for additional reserves in a period of time when the Company's loan portfolio has grown significantly. Based on the evaluation described above, the Company recorded a provision for loan loss of $2,369,000 for the year ended December 31, 2009 compared to $192,000 for the year ended December 31, 2008. At December 31, 2009 the three year average loss ratios were: .509% Commercial, .268% Consumer, .011% 1-4 Residential, .000% Real Estate Construction and .040% Real Estate Mortgage. At December 31, 2008 the five year average loss ratios were: .051% Commercial, ..0352% Consumer, .000% 1-4 Residential, .000% Real Estate Construction and .032% Real Estate Mortgage.

During the year ended December 31, 2009 charge-offs of $777,166 and recoveries of $5,328 were recorded to the allowance for loan losses, resulting in an allowance for loan losses of $3,026,997 or 1.42% of total loans at December 31, 2009, compared to charge-offs of $114,313 and recoveries of $17,049 resulting in an allowance for loan losses of $1,429,835 or .79% of total loans at December 31, 2008.

Net charge-offs for the year ended December 31, 2009, were $771,838 as compared to net charge-offs of $97,264 for the year ended December 31, 2008. Uncertainty in the economic outlook still exists, making charge-off levels in future periods less predictable; however, loss exposure in the portfolio is identified, reserved and closely monitored to ensure that changes are promptly addressed in the analysis of reserve adequacy.

The Company had $842,158 in unallocated reserves at December 31, 2009 related to other inherent risk in the portfolio compared to unallocated reserves of $16,387 at December 31, 2008. Management believes the allowance for loan losses at December 31, 2009, is adequate to cover estimated losses in the loan portfolio; however, assessing the adequacy of the allowance is a process that requires considerable judgment. Management's judgments are based on numerous assumptions about current events which it believes to be reasonable, but which may or may not be valid. Thus there can be no assurance that loan losses in future periods will not exceed the current allowance amount or that future increases in the allowance will not be required. No assurance can be given that management's ongoing evaluation of the loan portfolio in light of changing economic conditions and other relevant circumstances will not require significant future additions to the allowance, thus adversely affecting the operating results of the Company.

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

The methodology used to determine the reserve for unfunded lending commitments, which is included in other liabilities, is inherently similar to that used to determine the allowance for loan losses described above adjusted for factors specific to binding commitments, including the probability of funding and historical loss ratio. During the third quarter of the year ended December 31, 2007, Management determined that $20,796 of the allowance for loan loss represented the reserves for unfunded lending commitments. This amount was moved from the allowance for loan loss to the allowance for unfunded loans and commitments. In addition $1,507 was added to the provision of unfunded loans and commitments, for the year ending December 31, 2007, based on the methodology referred to above with $1,478 recovered in 2008, leaving a balance of $20,825 at December 31, 2008. No provision was recorded during 2009 resulting in no change to the balance of $20,825.

SUMMARY OF LOAN LOSS EXPERIENCE

	Year Ended December 31,				
	2009	2008	2007	2006	2005
Allowance for loan losses, beginning of year	$ 1,429,835	$ 1,335,099	$ 1,294,994	$ 1,017,175	$ 1,043,901
Charge-offs:					
Commercial	676,660	34,878	14,535	9,164	-
Consumer	66,219	3,470	4,336	15,692	45,982
Real estate	34,287	75,965	-	-	