FIRST BANCORP /NC/
Form 10-Q
November 09, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2012

Commission File Number 0-15572

FIRST BANCORP

(Exact Name of Registrant as Specified in its Charter)

North Carolina (State or Other Jurisdiction of Incorporation or Organization)	56-1421916 (I.R.S. Employer Identification Number)

341 North Main Street, Troy, North Carolina	27371-0508
(Address of Principal Executive Offices)	(Zip Code)
(Registrant's telephone number, including area code)	(910) 576-6171

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 twelve 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. ý YES o NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ý YES o 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)

o Large Accelerated Filer	ýAccelerated Filer	o Non-Accelerated Filer (Do not check if a smaller reporting company)	o Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). o YES ý NO

The number of shares of the registrant's Common Stock outstanding on October 31, 2012 was 17,013,008.

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FIRST BANCORP AND SUBSIDIARIES

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FORWARD-LOOKING STATEMENTS

Part I of this report contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934 and the Private Securities Litigation Reform Act of 1995, which statements are inherently subject to risks and uncertainties. Forward-looking statements are statements that include projections, predictions, expectations or beliefs about future events or results or otherwise are not statements of historical fact. Such statements are often characterized by the use of qualifying words (and their derivatives) such as “expect,” “believe,” “estimate,” “plan,” “project,” or other statements concerning our opinions or judgment about future events. Our actual results may differ materially from those anticipated in any forward-looking statements, as they will depend on many factors about which we are unsure, including many factors which are beyond our control. Factors that could influence the accuracy of such forward-looking statements include, but are not limited to, the financial success or changing strategies of our customers, our level of success in integrating acquisitions, actions of government regulators, the level of market interest rates, and general economic conditions. For additional information about factors that could affect the matters discussed in this paragraph, see the “Risk Factors” section of our 2011 Annual Report on Form 10-K.

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Part I. Financial Information

Item 1 - Financial Statements

First Bancorp and Subsidiaries

Consolidated Balance Sheets

($ in thousands-unaudited)	September 30, 2012	December 31, 2011 (audited)	September 30, 2011
ASSETS			
Cash and due from banks, noninterest-bearing	$ 79,991	80,341	75,772
Due from banks, interest-bearing	202,693	135,218	167,053
Federal funds sold	519	608	659
Total cash and cash equivalents	283,203	216,167	243,484
Securities available for sale	161,407	182,626	159,870
Securities held to maturity (fair values of $61,877, $62,754, and $61,512)	56,123	57,988	57,533
Presold mortgages in process of settlement	4,380	6,090	3,823
Loans – non-covered	2,137,074	2,069,152	2,058,724
Loans – covered by FDIC loss share agreement	303,997	361,234	373,824
Total loans	2,441,071	2,430,386	2,432,548
Allowance for loan losses – non-covered	(45,154)	(35,610)	(34,397)
Allowance for loan losses – covered	(4,394)	(5,808)	(3,257)
Total allowance for loan losses	(49,548)	(41,418)	(37,654)
Net loans	2,391,523	2,388,968	2,394,894
Premises and equipment	74,044	69,975	69,862
Accrued interest receivable	10,720	11,779	11,568
FDIC indemnification asset	107,615	121,677	120,950
Goodwill	65,835	65,835	65,835
Other intangible assets	3,335	3,897	4,123
Foreclosed real estate – non-covered	38,065	37,023	32,673
Foreclosed real estate – covered	58,367	85,272	104,785
Bank-owned life insurance	27,587	2,207	2,170
Other assets	40,473	40,970	31,128
Total assets	$ 3,322,677	3,290,474	3,302,698
LIABILITIES			
Deposits: Noninterest bearing checking accounts	$ 398,527	335,833	334,109
Interest bearing checking accounts	482,583	423,452	376,999
Money market accounts	539,504	513,832	506,013

Savings accounts	159,189	146,481	146,977
Time deposits of $100,000 or more	717,457	753,233	751,994
Other time deposits	537,204	582,206	613,312
Total deposits	2,834,464	2,755,037	2,729,404
Securities sold under agreements to repurchase	—	17,105	60,498
Borrowings	111,394	133,925	135,759
Accrued interest payable	1,421	1,872	1,938
Other liabilities	32,608	37,385	23,286
Total liabilities	2,979,887	2,945,324	2,950,885
Commitments and contingencies			
SHAREHOLDERS' EQUITY			
Preferred stock, no par value per share. Authorized: 5,000,000 shares			
Issued and outstanding: 63,500, 63,500, and 63,500 shares	63,500	63,500	63,500
Common stock, no par value per share. Authorized: 40,000,000 shares			
Issued and outstanding: 17,013,008, 16,909,820 and 16,884,617 shares	105,454	104,841	105,518
Retained earnings	181,672	185,491	186,654
Accumulated other comprehensive income (loss)	(7,836)	(8,682)	(3,859)
Total shareholders' equity	342,790	345,150	351,813
Total liabilities and shareholders' equity	$ 3,322,677	3,290,474	3,302,698

See notes to consolidated financial statements.

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First Bancorp and Subsidiaries

Consolidated Statements of Income

	Three Months Ended September 30,		Nine Months Ended September 30,	
($ in thousands, except share data-unaudited)	2012	2011	2012	2011
INTEREST INCOME				
Interest and fees on loans	$37,037	37,200	107,715	112,471
Interest on investment securities:				
Taxable interest income	1,001	1,421	3,408	4,316
Tax-exempt interest income	487	500	1,471	1,499
Other, principally overnight investments	164	107	481	300
Total interest income	38,689	39,228	113,075	118,586
INTEREST EXPENSE				
Savings, checking and money market	650	1,020	2,258	3,353
Time deposits of $100,000 or more	2,022	2,479	6,282	7,744
Other time deposits	1,097	1,651	3,535	5,587
Securities sold under agreements to repurchase	—	46	4	144
Borrowings	447	543	1,481	1,475
Total interest expense	4,216	5,739	13,560	18,303
Net interest income	34,473	33,489	99,515	100,283
Provision for loan losses – non-covered	5,970	6,441	29,721	21,618
Provision for loan losses – covered	1,103	2,705	5,374	9,805
Total provision for loan losses	7,073	9,146	35,095	31,423
Net interest income after provision for loan losses	27,400	24,343	64,420	68,860
NONINTEREST INCOME				
Service charges on deposit accounts	3,053	3,046	8,867	8,985
Other service charges, commissions and fees	2,275	2,040	6,634	6,025
Fees from presold mortgage loans	785	468	1,685	1,109
Commissions from sales of insurance and financial products	510	383	1,325	1,147
Bank-owned life insurance income	207	9	380	33
Gain from acquisition	—	—	—	10,196
Foreclosed property losses and write-downs – non-covered	(1,020)	(919)	(3,026)	(2,543)
Foreclosed property losses and write-downs – covered	(1,641)	(5,176)	(12,742)	(12,693)
FDIC indemnification asset income (expense), net	(1,569)	3,589	6,094	10,455
Securities gains	189	—	638	74
Other gains	14	46	67	5
Total noninterest income	2,803	3,486	9,922	22,793
NONINTEREST EXPENSES				
Salaries	10,370	9,980	30,717	29,385
Employee benefits	2,539	3,086	9,230	9,242
Total personnel expense	12,909	13,066	39,947	38,627
Net occupancy expense	1,670	1,674	4,966	4,944
Equipment related expenses	1,318	1,089	3,652	3,261

Intangibles amortization	224	226	670	676
Acquisition expenses	—	12	—	606
Other operating expenses	7,536	7,891	22,245	23,800
Total noninterest expenses	23,657	23,958	71,480	71,914
Income before income taxes	6,546	3,871	2,862	19,739
Income taxes	2,123	1,314	331	7,081
Net income	4,423	2,557	2,531	12,658
Preferred stock dividends	(688)	(815)	(2,277)	(2,440)
Accretion of preferred stock discount	—	(2,474)	—	(2,932)
Net income (loss) available to common shareholders	$3,735	(732)	254	7,286
Earnings (loss) per common share - Basic	$0.22	(0.04)	0.01	0.43
Earnings (loss) per common share – Diluted	0.22	(0.04)	0.01	0.43
Dividends declared per common share	$0.08	0.08	0.24	0.24
Weighted average common shares outstanding: Basic	16,988,150	16,875,918	16,955,130	16,843,716
Weighted average common shares outstanding: Diluted	16,988,150	16,903,031	16,955,130	16,871,010

See notes to consolidated financial statements.

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First Bancorp and Subsidiaries

Consolidated Statements of Comprehensive Income

($ in thousands-unaudited)	Three Months Ended September 30, 2012	2011	Nine Months Ended September 30, 2012	2011
Net income	$ 4,423	2,557	2,531	12,658
Other comprehensive income (loss):				
Unrealized gains on securities available for sale:				
Unrealized holding gains arising during the period, pretax	635	259	1,536	1,646
Tax expense	(249)	(101)	(599)	(642)
Reclassification to realized (gains)	(189)	—	(638)	(74)
Tax expense	74	—	249	29
Postretirement Plans:				
Amortization of unrecognized net actuarial loss	82	140	465	420
Tax expense	(32)	(56)	(181)	(168)
Amortization of prior service cost and transition obligation	7	9	24	27
Tax expense	(3)	(4)	(10)	(12)
Other comprehensive income	325	247	846	1,226
Comprehensive income	$ 4,748	2,804	3,377	13,884

See notes to consolidated financial statements.

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First Bancorp and Subsidiaries

Consolidated Statements of Shareholders' Equity

(In thousands, except per share - unaudited)	Preferred Stock	Preferred Stock Discount	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders Equity
Balances, January 1, 2011	$65,000	(2,932)	16,801	$104,207	183,413	(5,085)	344,60
Net income					12,658		12,658
Preferred stock redeemed	(65,000)						(65,00
Preferred stock issued	63,500						63,500
Common stock issued under stock option plans			2	30			30
Common stock issued into dividend reinvestment plan			53	638			638
Cash dividends declared ($0.24 per common share)					(4,045)		(4,045
Preferred dividends					(2,440)		(2,440
Accretion of preferred stock discount		2,932			(2,932)		—
Stock-based compensation			29	643			643
Other comprehensive income						1,226	1,226
Balances, September 30, 2011	$63,500	—	16,885	$105,518	186,654	(3,859)	351,81
Balances, January 1, 2012	$63,500	—	16,910	$104,841	185,491	(8,682)	345,15
Net income					2,531		2,531
Common stock issued into dividend reinvestment plan			31	335			335
Repurchases of common stock			—	(2)			(2
Cash dividends declared ($0.24 per common share)					(4,073)		(4,073
Preferred dividends					(2,277)		(2,277
Stock-based compensation			72	280			280
Other comprehensive income						846	846
Balances, September 30, 2012	$63,500	—	17,013	$105,454	181,672	(7,836)	342,79

See notes to consolidated financial statements.

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First Bancorp and Subsidiaries

Consolidated Statements of Cash Flows

($ in thousands-unaudited)	Nine Months Ended September 30, 2012	2011
Cash Flows From Operating Activities		
Net income	$2,531	12,658
Reconciliation of net income to net cash provided by operating activities:		
Provision for loan losses	35,095	31,423
Net security premium amortization	1,397	1,013
Purchase accounting accretion and amortization, net	(10,209)	(9,921)
Gain from acquisition	—	(10,196)
Foreclosed property losses and write-downs	15,768	15,236
Gain on securities available for sale	(638)	(74)
Other gains	(67)	(5)
Increase in net deferred loan costs	(198)	(322)
Depreciation of premises and equipment	3,427	3,302
Stock-based compensation expense	280	643
Amortization of intangible assets	670	676
Origination of presold mortgages in process of settlement	(70,507)	(53,094)
Proceeds from sales of presold mortgages in process of settlement	72,217	53,233
Decrease in accrued interest receivable	1,059	2,011
Increase in other assets	(11,412)	(12,842)
Decrease in accrued interest payable	(455)	(144)
Decrease in other liabilities	(4,225)	(6,087)
Net cash provided by operating activities	34,733	27,510
Cash Flows From Investing Activities		
Purchases of securities available for sale	(64,269)	(43,146)
Purchases of securities held to maturity	—	(3,816)
Proceeds from sales of securities available for sale	9,641	2,518
Proceeds from maturities/issuer calls of securities available for sale	76,161	66,281
Proceeds from maturities/issuer calls of securities held to maturity	1,690	1,053
Purchase of bank-owned life insurance	(25,000)	—
Net decrease (increase) in loans	(63,868)	30,476
Proceeds from FDIC loss share agreements	25,116	59,411
Proceeds from sales of foreclosed real estate	46,618	24,650
Purchases of premises and equipment	(7,496)	(5,407)
Net cash received in acquisition	9,312	54,037
Net cash provided by investing activities	7,905	186,057
Cash Flows From Financing Activities		
Net increase (decrease) in deposits and repurchase agreements	52,979	(109,551)
Repayments of borrowings, net	(22,500)	(65,081)
Cash dividends paid – common stock	(4,065)	(4,039)

Cash dividends paid – preferred stock	(2,349)	(2,582)
Proceeds from issuance of common stock	335	668
Repurchase of common stock	(2)	—
Proceeds from issuance of preferred stock	—	63,500
Redemption of preferred stock	—	(65,000)
Net cash provided (used) by financing activities	24,398	(182,085)
Increase in cash and cash equivalents	67,036	31,482
Cash and cash equivalents, beginning of period	216,167	212,002
Cash and cash equivalents, end of period	$283,203	243,484
Supplemental Disclosures of Cash Flow Information:		
Cash paid during the period for:		
Interest	$14,011	18,447
Income taxes	12,025	13,943
Non-cash transactions:		
Unrealized gain on securities available for sale, net of taxes	548	959
Foreclosed loans transferred to foreclosed real estate	36,523	60,030

See notes to consolidated financial statements.

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First Bancorp and Subsidiaries

Notes to Consolidated Financial Statements

(*unaudited)* For the Periods Ended September 30, 2012 and 2011

Note 1 - Basis of Presentation

In the opinion of the Company, the accompanying unaudited consolidated financial statements contain all adjustments necessary to present fairly the consolidated financial position of the Company as of September 30, 2012 and 2011 and the consolidated results of operations and consolidated cash flows for the periods ended September 30, 2012 and 2011. All such adjustments were of a normal, recurring nature. Reference is made to the 2011 Annual Report on Form 10-K filed with the SEC for a discussion of accounting policies and other relevant information with respect to the financial statements. The results of operations for the periods ended September 30, 2012 and 2011 are not necessarily indicative of the results to be expected for the full year. The Company has evaluated all subsequent events through the date the financial statements were issued.

Note 2 – Accounting Policies

Note 1 to the 2011 Annual Report on Form 10-K filed with the SEC contains a description of the accounting policies followed by the Company and a discussion of recent accounting pronouncements. The following paragraphs update that information as necessary.

In July 2012, rules related to intangible assets were amended to permit an entity to consider qualitative factors to determine whether it is more likely than not that indefinite-lived intangible assets are impaired. If it is determined to be more likely than not that indefinite-lived intangible assets are impaired, then the entity is required to determine the fair value of the indefinite-lived intangible asset and perform the quantitative impairment testing by comparing the fair value with carrying amount. The amendments are effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted. The amendments are not expected to have a material effect on the Company’s financial statements.

In October 2012, rules related to business combinations were amended to address the subsequent accounting for an indemnification asset resulting from a government-assisted acquisition of a financial institution. The guidance indicates that when a reporting entity records an indemnification asset as a result of a government-assisted acquisition of a financial institution involving an indemnification agreement, the indemnification asset should be subsequently measured on the same basis as the asset subject to indemnification. Any amortization of changes in value should be limited to any contractual limitations on the amount and the term of the indemnification agreement. The amendments should be applied prospectively to any new indemnification assets acquired and to changes expected in cash flows of existing indemnification assets occurring on or after the date of adoption. Prior periods would not be adjusted. These changes are effective for fiscal years, and interim periods within those years, beginning on or after December 15, 2012. Early adoption is permitted. The amendments are not expected to have a material effect on the Company's financial statements.

Note 3 – Reclassifications

Certain amounts reported in the period ended September 30, 2011 have been reclassified to conform to the presentation for September 30, 2012. These reclassifications had no effect on net income or shareholders' equity for the periods presented, nor did they materially impact trends in financial information.

Note 4 – Acquisitions

On August 24, 2012, the Company completed the purchase of a branch of Gateway Bank & Trust Co. located in Wilmington, North Carolina. The Company assumed the branch's $9 million in deposits. No loans were acquired in this transaction. The Company also did not purchase the branch building, but instead transferred the acquired accounts to one of the Company's nearby existing branches. The primary reason for this acquisition was to increase the Company's presence in Wilmington, North Carolina, where the Company already has five branches. The Company paid a deposit premium for the branch of approximately $107,000, which is the amount of the identifiable intangible asset associated with the fair value of the core deposit base. The intangible asset is being amortized as expense on straight-line basis over a seven year period. This branch's operations are included in the accompanying Consolidated Statements of Income beginning on the acquisition date of August 24, 2012. Historical pro forma information is not presented due to the immateriality of the transaction.

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Note 5 – Equity-Based Compensation Plans

At September 30, 2012, the Company had the following equity-based compensation plans: the First Bancorp 2007 Equity Plan, the First Bancorp 2004 Stock Option Plan, and the First Bancorp 1994 Stock Option Plan. The Company's shareholders approved all equity-based compensation plans. The First Bancorp 2007 Equity Plan became effective upon the approval of shareholders on May 2, 2007. As of September 30, 2012, the First Bancorp 2007 Equity Plan was the only plan that had shares available for future grants.

The First Bancorp 2007 Equity Plan is intended to serve as a means to attract, retain and motivate key employees and directors and to associate the interests of the plans' participants with those of the Company and its shareholders. The First Bancorp 2007 Equity Plan allows for both grants of stock options and other types of equity-based compensation, including stock appreciation rights, restricted stock, restricted performance stock, unrestricted stock, and performance units.

Recent equity grants to employees have either had performance vesting conditions, service vesting conditions, or both. Compensation expense for these grants is recorded over the various service periods based on the estimated number of equity grants that are probable to vest. No compensation cost is recognized for grants that do not vest and any previously recognized compensation cost will be reversed. As it relates to director equity grants, the Company grants common shares, valued at approximately $16,000 to each non-employee director (currently 14 in total) in June of each year. Compensation expense associated with these director grants is recognized on the date of grant since there are no vesting conditions.

Pursuant to an employment agreement, the Company granted the chief executive officer 75,000 non-qualified stock options and 40,000 shares of restricted stock during the third quarter of 2012. The option award and the restricted stock award will vest in full on December 31, 2014 and December 31, 2015, respectively, if the Company achieves certain earnings targets for those years, and will be forfeited if the applicable targets are not achieved. Compensation expense for this grant will be recorded over the various periods based on the estimated number of options and restricted stock that are probable to vest. If the awards do not vest, no compensation cost will be recognized and any previously recognized compensation cost will be reversed. Based on current conditions, the Company has concluded that it is not probable that these awards will vest, and thus no compensation expense has been recorded.

The Company granted long-term restricted shares of common stock to certain senior executives on February 24, 2011 and February 23, 2012 with a two year minimum vesting period. The total compensation expense associated with the February 24, 2011 grant was $105,500 and the grant will fully vest on February 24, 2013. The Company recorded $29,600 in stock option expense in the first nine months of 2012 in connection with this grant and expects to record $11,800 of expense each quarter thereafter until the awards vest. The total compensation expense associated with the February 23, 2012 grant was $89,700 and the grant will fully vest on February 23, 2014. The Company recorded

$24,400 in expense in the first nine months of 2012 in connection with this grant and expects to record $13,000 of expense each quarter thereafter until the awards vest.

Under the terms of the predecessor plans and the First Bancorp 2007 Equity Plan, options can have a term of no longer than ten years, and all options granted thus far under these plans have had a term of ten years. The Company's options provide for immediate vesting if there is a change in control (as defined in the plans).

At September 30, 2012, there were 521,613 options outstanding related to the three First Bancorp plans, with exercise prices ranging from $9.76 to $22.12. At September 30, 2012, there were 758,731 shares remaining available for grant under the First Bancorp 2007 Equity Plan. The Company also has a stock option plan as a result of a corporate acquisition.

The Company issues new shares of common stock when options are exercised.

The Company measures the fair value of each option award on the date of grant using the Black-Scholes option-pricing model. The Company determines the assumptions used in the Black-Scholes option pricing model as follows: the risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of the grant; the dividend yield is based on the Company's dividend yield at the time of the grant (subject to adjustment if the dividend yield on the grant date is not expected to approximate the dividend yield over the expected life of the option); the volatility factor is based on the historical volatility of the Company's stock (subject to adjustment if future volatility is reasonably expected to differ from the past); and the weighted-average expected life is based on the historical behavior of employees related to exercises, forfeitures and cancellations.

The Company's equity grants for the nine months ended September 30, 2012 were the issuance of 1) 9,559 shares of long-term restricted stock to certain senior executives on February 23, 2012, at a fair market value of $10.96 per share, which was the closing price of the Company's common stock on that date, 2) 25,452 shares of common stock to non-employee directors on June 1, 2012 (1,818 shares per director), at a fair market value of $8.86 per share, which was the closing price of the Company's common stock on that date, 3) 40,000 shares of restricted stock to the chief executive officer on August 28, 2012, at a fair market value of $9.76 per share, which was the closing price of the Company's common stock on that date, and 4) 75,000 stock options to the chief executive officer on August 28, 2012, at a fair value of $3.65 per share on the date of the grant using the Black-Scholes option pricing model with the following assumptions:

	2012
Expected dividend yield	3.28%
Risk-free interest rate	1.64%
Expected life	10 years
Expected volatility	41.82%

The Company's equity grants for the nine months ended September 30, 2011 were the issuance of 1) 7,259 shares of long-term restricted stock to certain senior executives on February 24, 2011, at a fair market value of $14.54 per share, which was the closing price of the Company's common stock on that date, and 2) 21,210 shares of common stock to non-employee directors on June 1, 2011 (1,414 shares per director), at a fair market value of $11.39 per share, which was the closing price of the Company's common stock on that date.

The Company recorded total stock-based compensation expense of $280,000 and $643,000 for the nine month periods ended September 30, 2012 and 2011, respectively. Stock-based compensation expense related to employee grants is recorded as “salaries expense” in the Consolidated Statements of Income and as an adjustment to cash flows from operating activities on the Company’s Consolidated Statement of Cash Flows. The Company recognized $109,000 and $251,000 of income tax benefits related to stock based compensation expense in the income statement for the nine months ended September 30, 2012 and 2011, respectively.

As noted above, certain of the Company’s stock option grants contain terms that provide for a graded vesting schedule whereby portions of the award vest in increments over the requisite service period. The Company has elected to recognize compensation expense for awards with graded vesting schedules on a straight-line basis over the requisite service period for the entire award. Compensation expense is based on the estimated number of stock options and awards that will ultimately vest. Over the past five years, there have only been minimal amounts of forfeitures, and therefore the Company assumes that all options granted without performance conditions will become vested.

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The following table presents information regarding the activity for the first nine months of 2012 related to all of the Company's stock options outstanding:

	Options Outstanding			
	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Contractual Term (years)	Aggregate Intrinsic Value
Balance at December 31, 2011	493,850	$ 18.92		
Granted	75,000	9.76		
Exercised	—	—		
Forfeited	—	—		
Expired	(47,237)	16.70		
Outstanding at September 30, 2012	521,613	$ 17.80	4.2	$ 133,000
Exercisable at September 30, 2012	445,613	$ 19.15	3.2	$ —

The Company did not have any stock option exercises during the nine months ended September 30, 2012 and received $30,000 as a result of stock option exercises during the nine months ended September 30, 2011. The Company recorded no tax benefits from the exercise of nonqualified stock options during the nine months ended September 30, 2012 or 2011.

The following table presents information regarding the activity during 2012 related to the Company's outstanding restricted stock:

	Long-Term Restricted Stock	
	Number of Units	Weighted-Average Grant-Date Fair Value
Nonvested at December 31, 2011	7,259	$ 14.54
Granted during the period	49,559	$ 9.99
Vested during the period	—	—

Forfeited or expired during the period	(2,474)	12.55
Nonvested at September 30, 2012	54,344	$ 10.48

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Note 6 – Earnings Per Common Share

Basic earnings per common share were computed by dividing net income (loss) available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per common share is computed by assuming the issuance of common shares for all potentially dilutive common shares outstanding during the reporting period. Currently, the Company's potentially dilutive common stock issuances relate to grants under the Company's equity-based compensation plans, including stock options and restricted stock. The following is a reconciliation of the numerators and denominators used in computing basic and diluted earnings per common share:

	For the Three Months Ended September 30,					
	2012			2011		
($ in thousands except per share amounts)	Income (Numerator)	Shares (Denominator)	Per Share Amount	Income (Numerator)	Shares (Denominator)	Per Share Amount
Basic EPS						
Net income (loss) available to common shareholders	$3,735	16,988,150	$ 0.22	$(732)	16,875,918	$ (0.04)
Effect of Dilutive Securities	—	—		—	27,113	
Diluted EPS per common share	$3,735	16,988,150	$ 0.22	$(732)	16,903,031	$ (0.04)

	For the Nine Months Ended September 30,					
	2012			2011		
($ in thousands except per share amounts)	Income (Numerator)	Shares (Denominator)	Per Share Amount	Income (Numerator)	Shares (Denominator)	Per Share Amount
Basic EPS						
Net income available to common shareholders	$254	16,955,130	$ 0.01	$7,286	16,843,716	$ 0.43
Effect of Dilutive Securities	—	—		—	27,294	
Diluted EPS per common share	$254	16,955,130	$ 0.01	$7,286	16,871,010	$ 0.43

For both the three and nine months ended September 30, 2012, there were 446,613 options, respectively, that were antidilutive because the exercise price exceeded the average market price for the period. For the three and nine month periods ended September 30, 2011, there were 545,347 and 542,916 options, respectively, that were antidilutive because the exercise price exceeded the average market price for the period. Antidilutive options have been omitted from the calculation of diluted earnings per share for the respective periods.

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Note 7 – Securities

The book values and approximate fair values of investment securities at September 30, 2012 and December 31, 2011 are summarized as follows:

($ in thousands)	September 30, 2012 Amortized Cost	Fair Value	Unrealized Gains	(Losses)	December 31, 2011 Amortized Cost	Fair Value	Unrealized Gains	(Losses)
Securities available for sale:								
Government-sponsored enterprise securities	$20,500	20,614	114	—	34,511	34,665	170	(16)
Mortgage-backed securities	124,164	128,533	4,369	—	120,032	124,105	4,164	(91)
Corporate bonds	3,997	3,857	100	(240)	13,189	12,488	279	(980)
Equity securities	7,952	8,403	473	(22)	10,998	11,368	409	(39)
Total available for sale	$156,613	161,407	5,056	(262)	178,730	182,626	5,022	(1,126)
Securities held to maturity:								
State and local governments	$56,123	61,877	5,754	—	57,988	62,754	4,766	—
Total held to maturity	$56,123	61,877	5,754	—	57,988	62,754	4,766	—

Included in mortgage-backed securities at September 30, 2012 were collateralized mortgage obligations with an amortized cost of $515,000 and a fair value of $532,000. Included in mortgage-backed securities at December 31, 2011 were collateralized mortgage obligations with an amortized cost of $1,462,000 and a fair value of $1,515,000. All of the Company's mortgage-backed securities, including collateralized mortgage obligations, were issued by government-sponsored corporations.

The Company owned Federal Home Loan Bank (FHLB) stock with a cost and fair value of $7,859,000 at September 30, 2012 and $10,904,000 at December 31, 2011, which is included in equity securities above and serves as part of the collateral for the Company's line of credit with the FHLB. The investment in this stock is a requirement for membership in the FHLB system.

The following table presents information regarding securities with unrealized losses at September 30, 2012:

($ in thousands)	Securities in an Unrealized Loss Position for Less than 12 Months		Securities in an Unrealized Loss Position for More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses

Government-sponsored enterprise securities	$	—	—	—	—	—	—
Mortgage-backed securities		—	—	—	—	—	—
Corporate bonds		—	—	760	240	760	240
Equity securities		—	—	30	22	30	22
State and local governments		—	—	—	—	—	—
Total temporarily impaired securities	$	—	—	790	262	790	262

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The following table presents information regarding securities with unrealized losses at December 31, 2011:

($ in thousands)	Securities in an Unrealized Loss Position for Less than 12 Months		Securities in an Unrealized Loss Position for More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Government-sponsored enterprise securities	$ 8,984	16	—	—	8,984	16
Mortgage-backed securities	14,902	61	9,302	30	24,204	91
Corporate bonds	4,588	458	2,773	522	7,361	980
Equity securities	4	2	22	37	26	39
State and local governments	—	—	—	—	—	—
Total temporarily impaired securities	$ 28,478	537	12,097	589	40,575	1,126

In the above tables, all of the non-equity securities that were in an unrealized loss position at September 30, 2012 and December 31, 2011 are bonds that the Company has determined are in a loss position due to interest rate factors, the overall economic downturn in the financial sector, and the broader economy in general. The Company has evaluated the collectability of each of these bonds and has concluded that there is no other-than-temporary impairment. The Company does not intend to sell these securities, and it is more likely than not that the Company will not be required to sell these securities before recovery of the amortized cost. The Company has also concluded that each of the equity securities in an unrealized loss position at September 30, 2012 and December 31, 2011 was in such a position due to temporary fluctuations in the market prices of the securities. The Company's policy is to record an impairment charge for any of these equity securities that remains in an unrealized loss position for twelve consecutive months unless the amount is insignificant.

The aggregate carrying amount of cost-method investments was $7,859,000 at September 30, 2012 and $10,904,000 at December 31, 2011, respectively, which was the FHLB stock discussed above. The Company determined that none of its cost-method investments were impaired at either period end.

The book values and approximate fair values of investment securities at September 30, 2012, by contractual maturity, are summarized in the table below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

($ in thousands)	Securities Available for Sale		Securities Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Debt securities				
Due within one year	$ 3,000	3,007	350	355
Due after one year but within five years	20,497	20,704	3,208	3,484

Due after five years but within ten years	—	—	29,677	32,653
Due after ten years	1,000	760	22,888	25,385
Mortgage-backed securities	124,164	128,533	—	—
Total debt securities	148,661	153,004	56,123	61,877
Equity securities	7,952	8,403	—	—
Total securities	$ 156,613	161,407	56,123	61,877

At September 30, 2012 investment securities with a book value of $83,557,000 were pledged as collateral for public deposits. At December 31, 2011, investment securities with a book value of $47,418,000 were pledged as collateral for public and private deposits and securities sold under agreements to repurchase.

There were $9,641,000 in sales of securities during the nine months ended September 30, 2012, which resulted in a net gain of $439,000. There were $2,518,000 in sales during the nine months ended September 30, 2011, which resulted in a net gain of $8,000. During the nine months ended September 30, 2012 and 2011, the Company recorded a net gain of $200,000 and $71,000, respectively, related to the call of several municipal and corporate bond securities. Also, during the nine months ended September 30, 2012 and 2011, the Company recorded net losses of $1,000 and $5,000, respectively, related to write-downs of the Company's equity portfolio.

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Note 8 – Loans and Asset Quality Information

The loans and foreclosed real estate that were acquired in FDIC-assisted transactions are covered by loss share agreements between the FDIC and the Company's banking subsidiary, First Bank, which afford First Bank significant loss protection. (See the Company's 2011 Annual Report on Form 10-K for more information regarding these transactions.) Because of the loss protection provided by the FDIC, the risk of the Cooperative Bank and The Bank of Asheville loans and foreclosed real estate are significantly different from those assets not covered under the loss share agreements. Accordingly, the Company presents separately loans subject to the loss share agreements as "covered loans" in the information below and loans that are not subject to the loss share agreements as "non-covered loans."

The following is a summary of the major categories of total loans outstanding:

($ in thousands)	September 30, 2012		December 31, 2011		September 30, 2011	
	Amount	Percentage	Amount	Percentage	Amount	Percen
All loans (non-covered and covered):						
Commercial, financial, and agricultural	$161,846	7 %	162,099	7 %	161,300	7 %
Real estate – construction, land development & other land loans	329,375	13 %	363,079	15 %	370,735	15 %
Real estate – mortgage – residential (1-4 family) first mortgages	823,069	34 %	805,542	33 %	803,688	33 %
Real estate – mortgage – home equity loans / lines of credit	243,556	10 %	256,509	11 %	258,653	11 %
Real estate – mortgage – commercial and other	807,914	33 %	762,895	31 %	756,568	31 %
Installment loans to individuals	73,833	3 %	78,982	3 %	80,309	3 %
Subtotal	2,439,593	100%	2,429,106	100%	2,431,253	100%
Unamortized net deferred loan costs	1,478		1,280		1,295	
Total loans	$2,441,071		2,430,386		2,432,548	

As of September 30, 2012, December 31, 2011 and September 30, 2011, net loans include unamortized premiums of $601,000, $949,000, and $1,065,000, respectively, related to acquired loans.

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The following is a summary of the major categories of non-covered loans outstanding:

($ in thousands)	September 30, 2012		December 31, 2011		September 30, 2011	
	Amount	Percentage	Amount	Percentage	Amount	Percen
Non-covered loans:						
Commercial, financial, and agricultural	$154,956	7 %	152,627	8 %	150,252	7 %
Real estate – construction, land development & other land loans	273,985	13 %	290,983	14 %	298,650	14 %
Real estate – mortgage – residential (1-4 family) first mortgages	681,168	32 %	646,616	31 %	637,129	31 %
Real estate – mortgage – home equity loans / lines of credit	223,154	10 %	233,171	11 %	236,578	12 %
Real estate – mortgage – commercial and other	729,310	34 %	666,882	32 %	656,035	32 %
Installment loans to individuals	73,023	4 %	77,593	4 %	78,785	4 %
Subtotal	2,135,596	100%	2,067,872	100%	2,057,429	100%
Unamortized net deferred loan costs	1,478		1,280		1,295	
Total non-covered loans	$2,137,074		2,069,152		2,058,724	

The carrying amount of the covered loans at September 30, 2012 consisted of impaired and nonimpaired purchased loans, as follows:

($ in thousands)	Impaired Purchased Loans – Carrying Value	Impaired Purchased Loans – Unpaid Principal Balance	Nonimpaired Purchased Loans – Carrying Value	Nonimpaired Purchased Loans – Unpaid Principal Balance	Total Covered Loans – Carrying Value	Total Covered Loans – Unpaid Principal Balance
Covered loans:						
Commercial, financial, and agricultural	$71	148	6,819	8,671	6,890	8,819
Real estate – construction, land development & other land loans	1,577	2,601	53,813	94,481	55,390	97,082
Real estate – mortgage – residential (1-4 family) first mortgages	815	1,908	141,086	168,840	141,901	170,748
Real estate – mortgage – home equity loans / lines of credit	15	308	20,387	25,999	20,402	26,307
Real estate – mortgage – commercial and other	2,265	4,128	76,339	103,399	78,604	107,527
Installment loans to individuals	2	3	808	881	810	884
Total	$4,745	9,096	299,252	402,271	303,997	411,367

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The carrying amount of the covered loans at December 31, 2011 consisted of impaired and nonimpaired purchased loans, as follows:

($ in thousands)	Impaired Purchased Loans – Carrying Value	Impaired Purchased Loans – Unpaid Principal Balance	Nonimpaired Purchased Loans – Carrying Value	Nonimpaired Purchased Loans – Unpaid Principal Balance	Total Covered Loans – Carrying Value	Total Covered Loans – Unpaid Principal Balance
Covered loans:						
Commercial, financial, and agricultural	$69	319	9,403	11,736	9,472	12,055
Real estate – construction, land development & other land loans	3,865	8,505	68,231	115,489	72,096	123,994
Real estate – mortgage – residential (1-4 family) first mortgages	1,214	2,639	157,712	189,436	158,926	192,075
Real estate – mortgage – home equity loans / lines of credit	127	577	23,211	29,249	23,338	29,826
Real estate – mortgage – commercial and other	2,585	4,986	93,428	125,450	96,013	130,436
Installment loans to individuals	4	6	1,385	1,583	1,389	1,589
Total	$7,864	17,032	353,370	472,943	361,234	489,975

The following table presents information regarding covered purchased nonimpaired loans since December 31, 2010. The amounts include principal only and do not reflect accrued interest as of the date of the acquisition or beyond.

($ in thousands)	
Carrying amount of nonimpaired covered loans at December 31, 2010	$366,521
Additions due to acquisition of The Bank of Asheville (at fair value)	84,623
Principal repayments	(40,576)
Transfers to foreclosed real estate	(53,999)
Loan charge-offs	(14,797)
Accretion of loan discount	11,598
Carrying amount of nonimpaired covered loans at December 31, 2011	$353,370
Principal repayments	(42,651)
Transfers to foreclosed real estate	(15,106)
Loan charge-offs	(6,816)
Accretion of loan discount	10,455
Carrying amount of nonimpaired covered loans at September 30, 2012	$299,252

As reflected in the table above, the Company accreted $10,455,000 of the loan discount on purchased nonimpaired loans into interest income during the first nine months of 2012. As of September 30, 2012, there was remaining loan discount of $62,805,000 related to purchased performing loans. If these loans continue to be repaid by the borrowers, the Company will accrete the remaining loan discount into interest income over the lives of the respective loans. In such circumstances, a corresponding entry to reduce the indemnification asset will be recorded amounting to 80% of the loan discount accretion, which reduces noninterest income. At September 30, 2012, the Company also had $23,070,000 of loan discount related to purchased nonperforming loans. It is not expected that this amount will be accreted. An additional $21,495,000 in partial charge-offs have been recorded on purchased loans outstanding at September 30, 2012.

The following table presents information regarding all purchased impaired loans since December 31, 2010, substantially all of which are covered loans. The Company has applied the cost recovery method to all purchased impaired loans at their respective acquisition dates due to the uncertainty as to the timing of expected cash flows, as reflected in the following table.

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($ in thousands)	Contractual Principal Receivable	Fair Market Value Adjustment – Write Down (Nonaccretable Difference)	Carrying Amount
Purchased Impaired Loans			
Balance at December 31, 2010	$ 8,080	2,329	5,751
Additions due to acquisition of The Bank of Asheville	38,452	20,807	17,645
Change due to payments received	(1,620)	(327)	(1,293)
Transfer to foreclosed real estate	(19,881)	(9,308)	(10,573)
Change due to loan charge-off	(7,522)	(4,193)	(3,329)
Other	807	224	583
Balance at December 31, 2011	$ 18,316	9,532	8,784
Change due to payments received	(330)	(23)	(307)
Transfer to foreclosed real estate	(7,636)	(3,487)	(4,149)
Change due to loan charge-off	(109)	(109)	—
Other	(1,145)	(1,562)	417
Balance at September 30, 2012	$ 9,096	4,351	4,745

Each of the purchased impaired loans is on nonaccrual status and considered to be impaired. Because of the uncertainty of the expected cash flows, the Company is accounting for each purchased impaired loan under the cost recovery method, in which all cash payments are applied to principal. Thus, there is no accretable yield associated with the above loans. For the nine months ended September 30, 2012 and 2011, the Company received $0 and $717,000 in payments that exceeded the initial carrying amount of the purchased impaired loans, which is included in the loan discount accretion amount discussed previously.

Nonperforming assets are defined as nonaccrual loans, restructured loans, loans past due 90 or more days and still accruing interest, and foreclosed real estate. Nonperforming assets are summarized as follows:

ASSET QUALITY DATA *($ in thousands)*	September 30, 2012	December 31, 2011	September 30, 2011
Non-covered nonperforming assets			
Nonaccrual loans	$ 69,413	73,566	75,013
Restructured loans - accruing	38,522	11,720	11,257
Accruing loans > 90 days past due	—	—	—

Total non-covered nonperforming loans	107,935	85,286	86,270
Foreclosed real estate	38,065	37,023	32,673
Total non-covered nonperforming assets	$ 146,000	122,309	118,943
Covered nonperforming assets			
Nonaccrual loans (1)	$ 37,619	41,472	36,536
Restructured loans - accruing	17,945	14,218	16,912
Accruing loans > 90 days past due	—	—	—
Total covered nonperforming loans	55,564	55,690	53,448
Foreclosed real estate	58,367	85,272	104,785
Total covered nonperforming assets	$ 113,931	140,962	158,233
Total nonperforming assets	$ 259,931	263,271	277,176

(1) At September 30, 2012, December 31, 2011, and September 30, 2011, the contractual balance of the nonaccrual loans covered by FDIC loss share agreements was $67.9 million, $69.0 million, and $65.0 million, respectively.

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The following table presents information related to the Company's impaired loans.

($ in thousands)	As of /for the nine months ended September 30, 2012	As of /for the year ended December 31, 2011	As of /for the nine months ended September 30, 2011
Impaired loans at period end			
Non-covered	$ 107,935	85,286	86,270
Covered	55,564	55,690	53,448
Total impaired loans at period end	$ 163,499	140,976	139,718
Average amount of impaired loans for period			
Non-covered	$ 92,027	89,023	89,957
Covered	56,228	63,289	65,189
Average amount of impaired loans for period – total	$ 148,255	152,312	155,146
Allowance for loan losses related to impaired loans at period end			
Non-covered	$ 9,410	5,804	5,429
Covered	4,074	5,106	2,287
Allowance for loan losses related to impaired loans - total	$ 13,484	10,910	7,716
Amount of impaired loans with no related allowance at period end			
Non-covered	$ 34,150	35,721	35,897
Covered	40,595	43,702	43,918
Total impaired loans with no related allowance at period end	$ 74,745	79,423	79,815

All of the impaired loans noted in the table above were on nonaccrual status at each respective period end except for those classified as restructured loans (see table on previous page for balances).

The remaining tables in this note present information derived from the Company's allowance for loan loss model. Relevant accounting guidance requires certain disclosures to be disaggregated based on how the Company develops its allowance for loan losses and manages its credit exposure. This model combines loan types in a different manner than the tables previously presented.

The following table presents the Company's nonaccrual loans as of September 30, 2012.

($ in thousands)	Non-covered	Covered	Total
Commercial, financial, and agricultural:			
Commercial – unsecured	$ 104	189	293
Commercial – secured	3,386	3	3,389
Secured by inventory and accounts receivable	701	31	732

Real estate – construction, land development & other land loans	16,858	18,032	34,890
Real estate – residential, farmland and multi-family	21,980	9,013	30,993
Real estate – home equity lines of credit	3,211	726	3,937
Real estate – commercial	20,354	9,556	29,910
Consumer	2,819	69	2,888
Total	$ 69,413	37,619	107,032

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The following table presents the Company's nonaccrual loans as of December 31, 2011.

($ in thousands)	Non-covered	Covered	Total
Commercial, financial, and agricultural:			
Commercial - unsecured	$ 452	—	452
Commercial - secured	2,190	358	2,548
Secured by inventory and accounts receivable	588	102	690
Real estate – construction, land development & other land loans	22,772	21,204	43,976
Real estate – residential, farmland and multi-family	25,430	11,050	36,480
Real estate – home equity lines of credit	3,161	1,068	4,229
Real estate - commercial	16,203	7,459	23,662
Consumer	2,770	231	3,001
Total	$ 73,566	41,472	115,038

The following table presents an analysis of the payment status of the Company's loans as of September 30, 2012.

($ in thousands)	30-59 Days Past Due	60-89 Days Past Due	Nonaccrual Loans	Current	Total Loans Receivable
Non-covered loans					
Commercial, financial, and agricultural:					
Commercial - unsecured	$289	61	104	36,379	36,833
Commercial - secured	930	336	3,386	108,956	113,608
Secured by inventory and accounts receivable	32	—	701	20,542	21,275
Real estate – construction, land development & other land loans	2,021	1,690	16,858	216,391	236,960
Real estate – residential, farmland, and multi-family	8,532	2,997	21,980	793,444	826,953
Real estate – home equity lines of credit	1,337	315	3,211	198,291	203,154
Real estate - commercial	3,925	756	20,354	615,543	640,578
Consumer	538	238	2,819	52,640	56,235
Total non-covered	$17,604	6,393	69,413	2,042,186	2,135,596
Unamortized net deferred loan costs					1,478
Total non-covered loans					$2,137,074

Covered loans	$5,118	2,583	37,619	258,677	303,997
Total loans	$22,722	8,976	107,032	2,300,863	2,441,071

The Company had no non-covered or covered loans that were past due greater than 90 days and accruing interest at September 30, 2012.

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The following table presents an analysis of the payment status of the Company's loans as of December 31, 2011.

($ in thousands)	30-59 Days Past Due	60-89 Days Past Due	Nonaccrual Loans	Current	Total Loans Receivable
Non-covered loans					
Commercial, financial, and agricultural:					
Commercial - unsecured	$ 67	591	452	37,668	38,778
Commercial - secured	672	207	2,190	108,682	111,751
Secured by					