FARMERS CAPITAL BANK CORP
Form 10-Q
November 08, 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

Farmers Capital Bank Corporation
(Exact name of registrant as specified in its charter)

Kentucky	000-14412	61-1017851
(State or other jurisdiction of incorporation)	(Commission File Number)	(IRS Employer Identification No.)

P.O. Box 309 Frankfort, KY	40602
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code – (502) 227-1668

Not Applicable
(Former name or former address, if changed since last report.)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes x No ¨

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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes x 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” in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨ Accelerated filer ¨

Non-accelerated filer x (Do not check if a smaller reporting company) Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common stock, par value $0.125 per share
7,465,754 shares outstanding at November 5, 2012

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PART I – FINANCIAL INFORMATION
Item 1. Financial Statements
Unaudited Consolidated Balance Sheets

(Dollars in thousands, except share data)	September 30, 2012	December 31, 2011
Assets		
Cash and cash equivalents:		
Cash and due from banks	$28,045	$28,842
Interest bearing deposits in other banks	78,956	62,226
Federal funds sold and securities purchased under agreements to resell	3,217	3,241
Total cash and cash equivalents	110,218	94,309
Investment securities:		
Available for sale, amortized cost of $582,159 (2012) and $583,951 (2011)	600,556	597,819
Held to maturity, fair value of $1,008 (2012) and $974 (2011)	875	875
Total investment securities	601,431	598,694
Loans, net of unearned income	1,018,311	1,072,108
Allowance for loan losses	(25,144)	(28,264)
Loans, net	993,167	1,043,844
Premises and equipment, net	36,846	38,770
Company-owned life insurance	27,745	27,461
Intangible assets, net	1,648	2,409
Other real estate owned	47,480	38,157
Other assets	36,447	39,946
Total assets	$1,854,982	$1,883,590
Liabilities		
Deposits:		
Noninterest bearing	$248,822	$224,259
Interest bearing	1,155,169	1,210,806
Total deposits	1,403,991	1,435,065
Federal funds purchased and other short-term borrowings	25,740	27,022
Securities sold under agreements to repurchase and other long-term borrowings	180,380	190,694
Subordinated notes payable to unconsolidated trusts	48,970	48,970
Dividends payable	188	188
Other liabilities	27,035	24,594
Total liabilities	1,686,304	1,726,533
Shareholders' Equity		
Preferred stock, no par value 1,000,000 shares authorized; 30,000 Series A shares issued and outstanding at September 30, 2012 and December 31, 2011; Liquidation preference of $30,000	29,429	29,115
Common stock, par value $.125 per share 14,608,000 shares authorized; 7,465,754 and 7,446,445 shares issued and outstanding at September 30, 2012 and December 31, 2011, respectively	933	931
Capital surplus	50,894	50,848
Retained earnings	77,628	69,520
Accumulated other comprehensive income	9,794	6,643
Total shareholders' equity	168,678	157,057
Total liabilities and shareholders' equity	$1,854,982	$1,883,590

See accompanying notes to unaudited consolidated financial statements.

Unaudited Consolidated Statements of Income

(In thousands, except per share data)	Three Months Ended September 30, 2012	2011	Nine Months Ended September 30, 2012	2011
Interest Income				
Interest and fees on loans	$13,883	$15,245	$42,268	$47,126
Interest on investment securities:				
Taxable	3,084	3,746	10,044	11,022
Nontaxable	573	461	1,661	1,455
Interest on deposits in other banks	37	41	99	188
Interest on federal funds sold and securities purchased under agreements to resell	1	-	3	3
Total interest income	17,578	19,493	54,075	59,794
Interest Expense				
Interest on deposits	2,141	3,553	7,320	11,272
Interest on federal funds purchased and other short-term borrowings	24	43	74	154
Interest on securities sold under agreements to repurchase and other long-term borrowings	1,828	1,996	5,481	5,978
Interest on subordinated notes payable to unconsolidated trusts	518	504	1,559	1,515
Total interest expense	4,511	6,096	14,434	18,919
Net interest income	13,067	13,397	39,641	40,875
Provision for loan losses	(256)	3,232	2,062	10,201
Net interest income after provision for loan losses	13,323	10,165	37,579	30,674
Noninterest Income				
Service charges and fees on deposits	2,062	2,251	6,080	6,481
Allotment processing fees	1,304	1,342	3,932	4,027
Other service charges, commissions, and fees	1,104	1,055	3,332	3,146
Data processing income	47	156	215	691
Trust income	469	507	1,404	1,593
Investment securities gains, net	276	386	964	1,209
Gains on sale of mortgage loans, net	603	328	1,364	620
Income from company-owned life insurance	301	230	1,289	706
Other	-	5	26	20
Total noninterest income	6,166	6,260	18,606	18,493
Noninterest Expense				
Salaries and employee benefits	7,019	6,646	20,999	20,281
Occupancy expenses, net	1,235	1,254	3,606	3,696
Equipment expenses	576	659	1,757	1,836
Data processing and communication expenses	1,059	1,147	3,211	3,574
Bank franchise tax	605	637	1,793	1,930
Amortization of intangibles	254	286	761	858
Deposit insurance expense	667	643	2,039	2,254
Other real estate expenses, net	1,531	3,569	3,197	6,184
Legal expenses	251	164	989	581
Other	2,150	1,954	5,989	6,554
Total noninterest expense	15,347	16,959	44,341	47,748

Income (loss) before income taxes	4,142	(534)	11,844	1,419
Income tax expense (benefit)	1,051	(806)	2,297	(67)
Net income	3,091	272	9,547	1,486
Less preferred stock dividends and discount accretion	481	474	1,439	1,419
Net income (loss) available to common shareholders	$2,610	$(202)	$8,108	$67
Per Common Share				
Net income (loss), basic and diluted	$.35	$(.03)	$1.09	$.01
Cash dividends declared	N/A	N/A	N/A	N/A
Weighted Average Common Shares Outstanding				
Basic and diluted	7,461	7,427	7,454	7,420

See accompanying notes to unaudited consolidated financial statements.

Unaudited Consolidated Statements of Comprehensive Income

(In thousands)	Three Months Ended September 30, 2012	2011	Nine Months Ended September 30, 2012	2011
Net Income	$3,091	$272	$9,547	$1,486
Other comprehensive income:				
Net unrealized holding gain on available for sale securities arising during the period on securities held at end of period, net of tax of $1,270, $1,767, $1,861 and $3,289, respectively	2,359	3,281	3,456	6,109
Reclassification adjustment for prior period unrealized gain previously reported in other comprehensive income recognized during current period, net of tax of $97, $25, $275 and $181, respectively	(181)	(46)	(511)	(337)
Change in unfunded portion of postretirement benefit obligation, net of tax of $44, $32, $111 and $95, respectively	82	58	206	175
Other comprehensive income	2,260	3,293	3,151	5,947
Comprehensive Income	$5,351	$3,565	$12,698	$7,433

See accompanying notes to unaudited consolidated financial statements.

Unaudited Consolidated Statements of Cash Flows

Nine months ended September 30, (In thousands)	2012	2011
Cash Flows from Operating Activities		
Net income	$9,547	$1,486
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	3,398	3,613
Net premium amortization of available for sale investment securities	3,921	2,520
Provision for loan losses	2,062	10,201
Deferred income tax expense	68	1,693
Noncash employee stock purchase plan expense	31	50
Mortgage loans originated for sale	(60,376)	(23,512)
Proceeds from sale of mortgage loans	60,099	24,393
Gain on sale of mortgage loans, net	(1,364)	(620)
Loss on disposal and write downs of premises and equipment, net	259	3
Net loss on sale and write downs of other real estate	2,443	5,263
Net gain on sale of available for sale investment securities	(964)	(1,209)
Decrease in accrued interest receivable	714	606
Increase in cash surrender value of company-owned life insurance	(732)	(689)
Death benefits in excess of cash surrender value on company-owned life insurance	(529)	-
Decrease (increase) in other assets	1,039	(3,044)
Decrease in accrued interest payable	(331)	(297)
Increase in other liabilities	3,089	1,776
Net cash provided by operating activities	22,374	22,233
Cash Flows from Investing Activities		
Proceeds from maturities and calls of available for sale investment securities	144,364	137,959
Proceeds from sale of available for sale investment securities	125,308	124,290
Purchase of available for sale investment securities	(270,836)	(395,997)
Principal collected on loans originated for investment, net	31,063	66,212
Proceeds from surrender of company-owned life insurance	-	2,248
Proceeds from death benefits of company-owned life insurance	1,051	-
Purchase of premises and equipment	(1,491)	(2,399)
Proceeds from sale of other real estate	7,427	6,444
Proceeds from sale of equipment	427	4
Net cash provided by (used in) investing activities	37,313	(61,239)
Cash Flows from Financing Activities		
Net decrease in deposits	(31,074)	(16,499)
Net decrease in federal funds purchased and other short-term borrowings	(1,282)	(16,686)
Repayments of securities sold under agreements to repurchase and other long-term borrowings	(10,314)	(7,441)
Dividends paid, preferred	(1,125)	(1,125)
Repurchase of common stock warrant	(75)	-
Shares issued under employee stock purchase plan	92	103
Net cash used in financing activities	(43,778)	(41,648)
Net increase (decrease) in cash and cash equivalents	15,909	(80,654)
Cash and cash equivalents at beginning of year	94,309	182,056
Cash and cash equivalents at end of period	$110,218	$101,402
Supplemental Disclosures		
Cash paid during the period for:		

Interest	$14,765	$19,216
Income taxes	2,500	1,300
Transfers from loans to other real estate	21,914	18,449
Sale and financing of other real estate	2,721	1,294
Cash dividends payable, preferred	188	188

See accompanying notes to unaudited consolidated financial statements.

Unaudited Consolidated Statements of Changes in Shareholders' Equity

(Dollars in thousands, except per share data)

Nine months ended September 30, 2012 and 2011	Preferred Stock	Common Stock Shares	Common Stock Amount	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders' Equity
Balance at January 1, 2012	$29,115	7,446	$931	$50,848	$69,520	$ 6,643	$ 157,057
Net income	-	-	-	-	9,547	-	9,547
Other comprehensive income	-	-	-	-	-	3,151	3,151
Preferred stock dividends, $37.50 per share	-	-	-	-	(1,125)	-	(1,125)
Preferred stock discount accretion	314	-	-	-	(314)	-	-
Repurchase of common stock warrant	-	-	-	(75)	-	-	(75)
Shares issued pursuant to employee stock purchase plan	-	20	2	90	-	-	92
Expense related to employee stock purchase plan	-	-	-	31	-	-	31
Balance at September 30, 2012	$29,429	7,466	$933	$50,894	$77,628	$ 9,794	$ 168,678
Balance at January 1, 2011	$28,719	7,412	$926	$50,675	$68,678	$898	$149,896
Net income	-	-	-	-	1,486	-	1,486
Other comprehensive income	-	-	-	-	-	5,947	5,947
Preferred stock dividends, $37.50 per share	-	-	-	-	(1,125)	-	(1,125)
Preferred stock discount accretion	294	-	-	-	(294)	-	-
Shares issued pursuant to employee stock purchase plan	-	25	4	99	-	-	103
Expense related to employee stock purchase plan	-	-	-	50	-	-	50
Balance at September 30, 2011	$29,013	7,437	$930	$50,824	$68,745	$6,845	$156,357

See accompanying notes to unaudited consolidated financial statements.

Notes to Unaudited Consolidated Financial Statements

1. Basis of Presentation and Nature of Operations

The consolidated financial statements include the accounts of Farmers Capital Bank Corporation (the “Company” or “Parent Company”), a bank holding company, and its bank and nonbank subsidiaries. Bank subsidiaries include Farmers Bank & Capital Trust Company (“Farmers Bank”) in Frankfort, KY, First Citizens Bank (“First Citizens”) in Elizabethtown, KY, United Bank & Trust Company (“United Bank”) in Versailles, KY, and Citizens Bank of Northern Kentucky, Inc. (“Citizens Northern”) in Newport, KY.

Farmers Bank’s significant subsidiaries include EG Properties, Inc., Leasing One Corporation (“Leasing One”), and Farmers Capital Insurance Corporation (“Farmers Insurance”). EG Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of Farmers Bank. Leasing One is a commercial leasing company in Frankfort, KY, and Farmers Insurance is an insurance agency in Frankfort, KY. United Bank has one wholly-owned subsidiary, EGT Properties, Inc. EGT Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of United Bank. First Citizens has one wholly-owned subsidiary, HBJ Properties, LLC. HBJ Properties, LLC is involved in real estate management and liquidation for certain repossessed properties of First Citizens. Citizens Northern has one wholly-owned subsidiary, ENKY Properties, Inc. ENKY Properties, Inc. is involved in real estate management and liquidation for certain repossessed properties of Citizens Northern.

The Company has three active nonbank subsidiaries, FCB Services, Inc. (“FCB Services”), FFKT Insurance Services, Inc. (“FFKT Insurance”), and EKT Properties, Inc. (“EKT”). FCB Services is a data processing subsidiary located in Frankfort, KY that provides services to the Company’s banks as well as unaffiliated entities. FFKT Insurance is a captive property and casualty insurance company insuring primarily deductible exposures and uncovered liability related to properties of the Company. EKT was formed to manage and liquidate certain real estate properties repossessed by the Company. In addition, the Company has three subsidiaries organized as Delaware statutory trusts that are not consolidated into its financial statements. These trusts were formed for the purpose of issuing trust preferred securities.

The Company provides financial services at its 36 locations in 23 communities throughout Central and Northern Kentucky to individual, business, agriculture, government, and educational customers. Its primary deposit products are checking, savings, and term certificate accounts. Its primary lending products are residential mortgage, commercial lending, and installment loans. Substantially all loans and leases are secured by specific items of collateral including business assets, consumer assets, and commercial and residential real estate. Commercial loans and leases are expected to be repaid from cash flow from operations of businesses. Other services include, but are not limited to, cash management services, issuing letters of credit, safe deposit box rental, and providing funds transfer services. Other financial instruments, which potentially represent concentrations of credit risk, include deposit accounts in other financial institutions and federal funds sold.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States (“U.S. GAAP”) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates used in the preparation of the financial statements are based on various factors including the current interest rate environment and the general strength of the local and state economy. Changes in the overall interest rate environment can significantly affect the Company’s net interest income and the value of its recorded assets and liabilities. Actual results could differ from those estimates used in the preparation of the financial statements. The allowance for loan losses, carrying value of other real estate owned, actuarial assumptions used to calculate postretirement benefits, and the fair values of financial instruments are estimates that are particularly subject to change.

The consolidated balance sheet as of December 31, 2011 has been derived from the audited financial statements of the Company as of that date. For further information, refer to the consolidated financial statements and footnotes thereto for the year ended December 31, 2011 included in the Company's annual report on Form 10-K. The accompanying consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X and do not include all of the information and the footnotes required by U.S. GAAP for complete statements. In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of such financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year. All significant intercompany transactions and balances are eliminated in consolidation.

2. Accounting Policy

Loans and Interest Income
Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their unpaid principal amount outstanding adjusted for any charge-offs and any deferred fees or costs on originated loans. Interest income on loans is recognized using the interest method based on loan principal amounts outstanding during the period. Interest income also includes amortization and accretion of any premiums or discounts over the expected life of acquired loans at the time of purchase or business acquisition. Loan origination fees, net of certain direct origination costs, are deferred and amortized as yield adjustments over the contractual term of the loans.

The Company disaggregates certain disclosure information related to loans, the related allowance for loan losses, and credit quality measures by either portfolio segment or by loan class. The Company segregates its loan portfolio segments based on similar risk characteristics as follows: real estate loans, commercial loans, and consumer loans.

The Company has a loan policy in place that is amended and approved from time to time as needed to reflect current economic conditions and product offerings in its markets. The policy establishes written procedures concerning areas such as the lending authorities of loan officers, committee review and approval of certain credit requests, underwriting criteria, policy exceptions, appraisal requirements, and loan review. Credit is extended to borrowers based primarily on their ability to repay as demonstrated by income and cash flow analysis.

Loans secured by real estate make up the largest segment of the Company’s loan portfolio. If a borrower fails to repay a loan secured by real estate, the Company may liquidate the collateral in order to satisfy the amount owed. Determining the value of real estate is a key component to the lending process for real estate backed loans. If the fair value of real estate (less estimated cost to sell) securing a collateral dependent loan declines below the outstanding loan amount, the Company will write down the carrying value of the loan and thereby incur a loss. The Company uses independent third party state-certified or licensed appraisers in accordance with its loan policy to mitigate risk when underwriting real estate loans. Cash flow analysis of the borrower, loan to value limits as adopted by loan policy, and other customary underwriting standards are also in place which are designed to maximize credit quality and mitigate risks associated with real estate lending.

Commercial loans are made to businesses and are secured mainly by assets such as inventory, accounts receivable, machinery, fixtures and equipment, or other business assets. Commercial lending involves significant risk, as loan repayments are more dependent on the successful operation or management of the business and its cash flows. Consumer lending includes loans to individuals mainly for personal autos, boats, or a variety of other personal uses and may be secured or unsecured. Loan repayment associated with consumer loans is highly dependent upon the borrower’s continuing financial stability, which is heavily influenced by local unemployment rates. The Company mitigates its risk exposure to each of its loan segments by analyzing the borrower’s repayment capacity, imposing restrictions on the amount it will loan compared to estimated collateral values, limiting the payback periods, and following other customary underwriting practices as adopted in its loan policy.

Generally, the accrual of interest on loans is discontinued when it is determined that the collection of interest or principal is doubtful, or when a default of interest or principal has existed for 90 days or more, unless such loan is well secured and in the process of collection. Past due status is based on the contractual terms of the loan. Interest accrued but not received for a loan placed on nonaccrual status is reversed against interest income. Cash payments received on nonaccrual loans generally are applied to principal, and interest income is only recorded once principal recovery is reasonably assured. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. The Company’s policy for placing a loan on nonaccrual status or subsequently returning a loan to accrual status does not differ based on its portfolio class or segment.

Commercial and real estate loans delinquent in excess of 120 days and consumer loans delinquent in excess of 180 days are charged off, unless the collateral securing the debt is of such value that any loss appears to be unlikely. In all cases, loans are charged off at an earlier date if classified as loss under its loan grading process or as a result of regulatory examination. The Company’s charge-off policy for impaired loans does not differ from the charge-off policy for loans outside the definition of impaired.

Provision and Allowance for Loan Losses

The provision for loan losses represents charges made to earnings to maintain an allowance for loan losses at a level considered adequate to provide for probable incurred credit losses at the balance sheet date. The allowance for loan losses is a valuation allowance increased by the provision for loan losses and decreased by net charge-offs. Loan losses are charged against the allowance when management believes the uncollectibility of a loan is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The Company estimates the adequacy of the allowance using a risk-rated methodology which is based on the Company's past loan loss experience, known and inherent risks in the loan portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral securing loans, composition of the loan portfolio, current economic conditions, and other relevant factors. This evaluation is inherently subjective as it requires significant judgment and the use of estimates that may be susceptible to change.

The allowance for loan losses consists of specific and general components. The specific component relates to loans that are individually classified as impaired. The general component covers non-impaired loans and is based on historical loss experience adjusted for current risk factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged off. Actual loan losses could differ significantly from the amounts estimated by management.

The Company's risk-rated methodology includes segregating watch list and past due loans from the general portfolio and allocating specific amounts to these loans depending on their status. For example, watch list loans, which may be identified by the internal loan review risk-rating process or by regulatory examiner classification, are assigned a certain loss percentage while loans past due 30 days or more are assigned a different loss percentage. Each of these percentages considers past experience as well as current factors. The remainder of the general loan portfolio is segregated into portfolio segments having similar risk characteristics identified as follows: real estate loans, commercial loans, and consumer loans. Each of these portfolio segments is assigned a loss percentage based on their respective actual twelve-quarter rolling historical loss rates, adjusted for qualitative risk factors.

A loan is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

The Company accounts for impaired loans in accordance with ASC Topic 310, "Receivables". ASC Topic 310 requires that impaired loans be measured at the present value of expected future cash flows, discounted at the loan's effective interest rate, at the loan's observable market price, or at the fair value of the collateral if the loan is collateral dependent. Generally, impaired loans are also in nonaccrual status. In certain circumstances, however, the Company may continue to accrue interest on an impaired loan. Cash receipts on impaired loans are typically applied to the recorded investment in the loan, including any accrued interest receivable. Loans that are part of a large group of smaller-balance homogeneous loans, such as residential mortgage, consumer, and smaller-balance commercial loans, are collectively evaluated for impairment and, accordingly, they are not separately identified for impairment disclosures. Troubled debt restructurings are measured at the present value of estimated future cash flows using the loan's effective interest rate at inception, or at the fair value of collateral. The Company determines the amount of reserve for troubled debt restructurings that subsequently default in accordance with its accounting policy for the allowance for loan losses.

Changes in Allowance Methodology

During the first quarter of 2012, the Company refined the methodology it uses for calculating the allowance for loan losses. The Company, with assistance from an independent third party advisor, adopted the revisions to better reflect the impact of adjustments made to historic loss percentages, which are based on an evaluation of certain qualitative risk factors used in estimating credit losses inherent in the general component of the allowance for loan losses. Like the previously established model, the new methodology consists of a formula-based approach applied at the subsidiary bank level to estimate the allowance for segments of loans in the general component as well as specific allocations for individually identified impaired loans. Both the revised and previous methodologies use historical loss rates adjusted for qualitative factors. Prior to being formally adopted, the Company tested the updated methodology with live data over a period of several months to ensure that the allowance was supported and directionally consistent with changes in overall credit quality and that fluctuations were explainable and supportable.

The Company’s new methodology includes enhancements to the qualitative risk factors applied to the general component of its real estate, commercial, and consumer loan portfolio segments. Qualitative risk factors are adjustments for current market conditions that are likely to cause estimated credit losses to differ from historical loss experience. The most significant parts of the change by the Company to its methodology includes the addition of a considerably greater amount of economic and other qualitative input which are more reflective of current market conditions, the removal of a qualitative factor in which the objective was to quantify losses based on a migration analysis of loans from performing to nonperforming status over time which is no longer reflective of current credit quality trends, and the removal of a qualitative component for which the objective was to identify and capture larger, unexpected losses which is no longer relevant to the current portfolio composition. The net effect of the changes in the methodology related to the qualitative risk factors was a reduction in the allowance for loan losses of $2.9 million.

The qualitative risk factors used in the methodology are consistent with the guidance in the most recent Interagency Policy Statement on the Allowance for Loan Losses issued in 2006. Each factor is supported by a detailed analysis performed at each subsidiary bank and are both measureable and supportable. Some factors include a minimum allocation in some instances where loss levels are extremely low and it is determined to be prudent from a safety and soundness perspective. Qualitative risk factors that are used in the methodology include the following for each loan portfolio segment:

- Delinquency trends
- Trends in net charge-offs
- Trends in loan volume
- Lending philosophy risk
- Management experience risk
- Concentration of credit risk
- Economic conditions risk

The qualitative risk factors above are used to adjust the actual twelve-quarter rolling historical loss rates for each loan segment. Components of the methodology that did not change include the computation of historical loss rates, loss estimates related to “Watch List” loans, and loss estimates related to loans 30 days or more past due that are not included in other components of the analysis.

In addition to the refinements made to the Company’s allowance for loans losses methodology as detailed above, the Company also made a policy change regarding how it identifies impaired loans. Previously, the Company identified as impaired all loans that were both in excess of a predetermined dollar threshold and that were also risk rated as substandard as part of its quarterly loan review analysis. Under the revised policy, certain substandard loans that previously were considered impaired may no longer be classified as such.

The determination of whether a loan is considered impaired is based on a loan's individual impairment analysis and not strictly by the fact that it is rated as substandard and in excess of a certain dollar amount. An impairment analysis may indicate that an impaired loan needs no specific reserve allocation, but nonetheless the loan is still considered impaired. These situations occur primarily as a result of loans that are on nonaccrual status, loans that are troubled debt restructurings, or loans with prior charge-offs. There were loans in the amount of $28.0 million during the first quarter of 2012 that are no longer considered impaired as a result of the policy change. This change resulted in an increase in the allowance for loan losses in the amount of $945 thousand. Although impaired loans decreased as a result of the policy change, the amount of overall reserves increased because these loans previously had no specific reserves allocated. When these loans were removed from the impaired loan classification due to the policy change, reserve amounts attributable to the general component of the allowance methodology became applicable.

3. Reclassifications

Certain reclassifications have been made to the consolidated financial statements of prior periods to conform to the current period presentation. These reclassifications do not affect net income or total shareholders' equity as previously reported.

4. Net Income Per Common Share

Basic net income per common share is determined by dividing net income available to common shareholders by the weighted average total number of common shares issued and outstanding. Net income available to common shareholders represents net income adjusted for preferred stock dividends including dividends declared, accretion of discounts on preferred stock issuances, and cumulative dividends related to the current dividend period that have not been declared as of the end of the period.

Diluted net income per common share is determined by dividing net income available to common shareholders by the total weighted average number of common shares issued and outstanding plus amounts representing the dilutive effect of stock options outstanding and outstanding warrants. The effects of stock options and outstanding warrants are excluded from the computation of diluted earnings per common share in periods in which the effect would be antidilutive. Dilutive potential common shares are calculated using the treasury stock method.

Net income (loss) per common share computations were as follows for the three and nine months ended September 30, 2012 and 2011.

(In thousands, except per share data)	Three Months Ended September 30, 2012	2011	Nine Months Ended September 30, 2012	2011
Net income, basic and diluted	$3,091	$272	$9,547	$1,486
Less preferred stock dividends and discount accretion	481	474	1,439	1,419
Net income (loss) available to common shareholders, basic and diluted	$2,610	$(202)	$8,108	$67
Average common shares issued and outstanding, basic and diluted	7,461	7,427	7,454	7,420
Net income (loss) per common share, basic and diluted	$.35	$(.03)	$1.09	$.01

For the three and nine months ended September 30, 2012 and 2011, options to purchase 24,049 common shares were excluded from the computation of diluted net income (loss) per common share because they were antidilutive. There were 223,992 potential common shares associated with a warrant issued to the U.S. Treasury ("Treasury") that were excluded from the computation of diluted net income (loss) per common share for the three and nine months ended September 30, 2011 because they were antidilutive. The Company repurchased the warrant from the Treasury during the third quarter of 2012.

5. Fair Value Measurements

ASC Topic 820, “Fair Value Measurements and Disclosures”, defines fair value, establishes a framework for measuring fair value, and sets forth disclosures about fair value measurements. ASC Topic 825, “Financial Instruments”, allows entities to choose to measure certain financial assets and liabilities at fair value. The Company has not elected the fair value option for any of its financial assets or liabilities.

ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. It also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. This Topic describes three levels of inputs that may be used to measure fair value:

Level 1:	Quoted prices for identical assets or liabilities in active markets that the entity has the ability to access at the measurement date.
Level 2:	Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
Level 3:	Significant unobservable inputs that reflect a reporting entity's own assumptions supported by little or no market activity, about the assumptions that market participants would use in pricing the asset or liability.

Following is a description of the valuation method used for financial instruments measured at fair value on a recurring basis. For this disclosure, the Company only has available for sale investment securities that meet the requirement.

Available for sale investment securities
Valued primarily by independent third party pricing services under the market valuation approach that include, but are not limited to, the following inputs:

- Mutual funds and equity securities are priced utilizing real-time data feeds from active market exchanges for identical securities and are considered Level 1 inputs.
- Government-sponsored agency debt securities, obligations of states and political subdivisions, mortgage-backed securities, corporate bonds, and other similar investment securities are priced with available market information through processes using benchmark yields, matrix pricing, prepayment speeds, cash flows, live trading data, and market spreads sourced from new issues, dealer quotes, and trade prices, among others sources and are considered Level 2 inputs.

Available for sale investment securities are the Company's only balance sheet item that meets the disclosure requirements for instruments measured at fair value on a recurring basis. Disclosures as of September 30, 2012 and December 31, 2011 are as follows:

(In thousands) Available For Sale Investment Securities	Fair Value	Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
September 30, 2012				
Obligations of U.S. government-sponsored entities	$74,698	$-	$74,698	$-
Obligations of states and political subdivisions	105,573	-	105,573	-
Mortgage-backed securities – residential	414,185	-	414,185	-
Mutual funds and equity securities	612	612	-	-
Corporate debt securities	5,488	-	5,488	-
Total	$600,556	$612	$599,944	$-

(In thousands) Available For Sale Investment Securities	Fair Value	Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2011				
Obligations of U.S. government-sponsored entities	$96,163	$-	$96,163	$-
Obligations of states and political subdivisions	84,619	-	84,619	-
Mortgage-backed securities – residential	408,863	-	408,863	-
Mortgage-backed securities – commercial	209	-	209	-
Mutual funds and equity securities	1,601	1,601	-	-
Corporate debt securities	6,364	-	6,364	-
Total	$597,819	$1,601	$596,218	$-

The Company is required to measure and disclose certain other assets and liabilities at fair value on a nonrecurring basis in periods following their initial recognition. The Company's disclosure about assets and liabilities measured at fair value on a nonrecurring basis consists of impaired loans and other real estate owned ("OREO"). The carrying value of these assets are adjusted to fair value on a nonrecurring basis through impairment charges as described more fully below.

Impairment charges on loans are recorded by either an increase to the provision for loan losses and related allowance or by direct loan charge-offs. The fair value of impaired loans with specific allocations of the allowance for loan losses is measured based on recent appraisals of the underlying collateral. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Appraisers take absorption rates into consideration and adjustments are routinely made in the appraisal process to identify differences between the comparable sales and income data available. Such adjustments consist mainly of estimated costs to sell that are not included in certain appraisals or to update appraised collateral values as a result of market declines of similar properties for which a newer appraisal is available. These adjustments can be significant and typically result in a Level 3 classification of the inputs for determining fair value.

OREO includes properties acquired by the Company through actual loan foreclosures and is carried at fair value less estimated costs to sell. Fair value of OREO at acquisition is generally based on third party appraisals of the property that includes comparable sales data and is considered as Level 3 inputs. The carrying value of each OREO property is updated at least annually and more frequently when market conditions significantly impact the value of the property. If the carrying amount of the OREO exceeds fair value less estimated costs to sell, an impairment loss is recorded through expense.

The following tables represent the carrying amount of assets measured at fair value on a nonrecurring basis and still held by the Company as of the dates indicated. The amounts in the tables only represent assets whose carrying amount has been adjusted by impairment charges during the period in a manner as described above; therefore, these amounts will differ from the total amounts outstanding. Impaired loan amounts in the tables below exclude restructured loans since they are measured based on present value techniques, which are outside the scope of the fair value reporting framework.

(In thousands)		Fair Value Measurements Using		
Description	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
September 30, 2012				
Impaired Loans				
Real estate-construction and land development	$14,601	$-	$-	$14,601
Real estate mortgage-residential	2,515	-	-	2,515
Real estate mortgage-farmland and other commercial enterprises	2,588	-	-	2,588
Commercial and industrial	6	-	-	6
Consumer-secured	4	-	-	4
Consumer-unsecured	115	-	-	115
Total	$19,829	$-	$-	$19,829
OREO				
Real estate-construction and land development	$9,418	$-	$-	$9,418
Real estate mortgage-residential	1,454	-	-	1,454
Real estate mortgage-farmland and other commercial enterprises	2,841	-	-	2,841
Total	$13,713	$-	$-	$13,713

(In thousands)		Fair Value Measurements Using		
Description	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)

December 31, 2011				
Impaired Loans				
Real estate-construction and land development	$18,636	$-	$-	$18,636
Real estate mortgage-residential	8,160	-	-	8,160
Real estate mortgage-farmland and other commercial enterprises	12,928	-	-	12,928
Commercial and industrial	293	-	-	293
Consumer	47	-	-	47
Total	$40,064	$-	$-	$40,064
OREO				
Real estate-construction and land development	$8,826	$-	$-	$8,826
Real estate mortgage-residential	1,217	-	-	1,217
Real estate mortgage-farmland and other commercial enterprises	4,785	-	-	4,785
Total	$14,828	$-	$-	$14,828

The following table presents quantitative information about unobservable inputs for assets measured on a nonrecurring basis using Level 3 measurements.

(In thousands)	Fair Value at September 30, 2012	Valuation Technique	Unobservable Inputs	Range	Weighted Average
Impaired loans	$ 19,829	Discounted appraisals	Marketability discount	.3% - 12.5%	5.0%
OREO	$ 13,713	Discounted appraisals	Marketability discount	.3% - 71.4%	6.8%

As previously discussed, the fair value of real estate securing impaired loans and OREO are based on current third party appraisals. It is often necessary, however, for the Company to discount the appraisal amounts supporting its impaired loans and OREO. These discounts relate primarily to marketing and other holding costs that are not included in certain appraisals or to update values as a result of market declines of similar properties for which newer appraisals are available. Discounts also result from contracts to sell properties entered into during the period. The range of discounts is presented in the table above for the nine months ended September 30, 2012. The upper end of the range identified in the table above related to OREO is the result of a few outlier transactions of small dollar properties, which magnified the percentage. The weighted average column is more of an indicator of the discounts applied to the appraisals.

The following table represents impairment charges recorded in earnings for the periods indicated on assets measured at fair value on a nonrecurring basis.

	Three Months Ended September 30,		Nine Months Ended September 30,	
(In thousands)	2012	2011	2012	2011
Impairment charges:				
Impaired loans	$ 584	$ 351	$ 5,817	$ 3,460
OREO	1,052	3,400	2,202	4,968
Total	$ 1,636	$ 3,751	$ 8,019	$ 8,428

Fair Value of Financial Instruments

The table that follows represents the estimated fair values of the Company's financial instruments made in accordance with the requirements of ASC 825, "Financial Instruments". ASC 825 requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet for which it is practicable to estimate that value. The estimated fair value amounts have been determined by the Company using available market information and present value or other valuation techniques. These derived fair values are subjective in nature, involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. ASC 825 excludes certain financial instruments and all nonfinancial instruments from the disclosure requirements. Accordingly, the aggregate fair value amounts presented are not intended to represent the underlying value of the Company.

The following methods and assumptions were used to estimate the fair value of each of the financial instruments in the table that follows.

Cash and Cash Equivalents, Accrued Interest Receivable, and Accrued Interest Payable
The carrying amount is a reasonable estimate of fair value due to the relatively short time between the origination of the instrument and its expected realization or settlement.

Investment Securities Held to Maturity
Fair value is based on quoted market price, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities or with available market information through processes using benchmark yields, matrix pricing, prepayment speeds, cash flows, live trading data, and market spreads sourced from new issues, dealer quotes, and trade prices, among others sources.

Loans
The fair value of loans is estimated by discounting expected future cash flows using current discount rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. Expected future cash flows are projected based on contractual cash flows adjusted for estimated prepayments.

Deposit Liabilities

The fair value of demand deposits, savings accounts, and certain money market deposits is the amount payable on demand at the reporting date and fair value approximates carrying value. The fair value of fixed maturity certificates of deposit is estimated by discounting the expected future cash flows using the rates currently offered for certificates of deposit with similar remaining maturities.

Federal Funds Purchased and Other Short-term Borrowings

The carrying amount is the estimated fair value for these borrowings which reprice frequently in the near term.

Securities Sold Under Agreements to Repurchase, Subordinated Notes Payable, and Other Long-term Borrowings

The fair value of these borrowings is estimated by discounting the expected future cash flows using rates currently available for debt with similar terms and remaining maturities. For subordinated notes payable, the Company uses its best estimate to determine an appropriate discount rate since active markets for similar debt transactions are very limited.

Commitments to Extend Credit and Standby Letters of Credit

Pricing of these financial instruments is based on the credit quality and relationship, fees, interest rates, probability of funding, compensating balance, and other covenants or requirements. Loan commitments generally have fixed expiration dates, variable interest rates and contain termination and other clauses that provide for relief from funding in the event there is a significant deterioration in the credit quality of the customer. Many loan commitments are expected to, and typically do, expire without being drawn upon. The rates and terms of the Company’s commitments to lend and standby letters of credit are competitive with others in the various markets in which the Company operates. There are no unamortized fees relating to these financial instruments, as such the carrying value and fair value are both zero.

The following table presents the estimated fair values of the Company's financial instruments and the level within the fair value hierarchy in which the fair value measurements fall at September 30, 2012 and December 31, 2011. Information for available for sale investment securities is presented within this footnote in greater detail above.

			Fair Value Measurements Using		
(In thousands)	Carrying Amount	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
September 30, 2012					
Assets					
Cash and cash equivalents	$110,218	$110,218	$110,218	$-	$ -
Held to maturity investment securities	875	1,008	-	1,008	-
Loans, net	993,167	990,603	-	-	990,603
Accrued interest receivable	5,905	5,905	-	5,905	-
Liabilities					
Deposits	1,403,991	1,408,221	840,842	-	567,379
Federal funds purchased and other short-term borrowings	25,740	25,740	-	25,740	-
Securities sold under agreements to repurchase and other long-term borrowings	180,380	201,360	-	201,360	-
Subordinated notes payable to unconsolidated trusts	48,970	20,324	-	-	20,324
Accrued interest payable	2,044	2,044	-	2,044	-
December 31, 2011					
Assets					
Cash and cash equivalents	$94,309	$94,309	$94,309	$-	$-
Held to maturity investment securities	875	974	-	974	-
Loans, net	1,043,844	1,043,824	-	-	1,043,824
Accrued interest receivable	6,619	6,619	-	6,619	-
Liabilities					
Deposits	1,435,065	1,441,490	787,396	-	654,094
Federal funds purchased and other short-term borrowings	27,022	27,022	-	27,022	-
Securities sold under agreements to repurchase and other long-term borrowings	190,694	212,176	-	212,176	-
Subordinated notes payable to unconsolidated trusts	48,970	20,982	-	-	20,982
Accrued interest payable	2,375	2,375	-	2,375	-

6. Investment Securities

The following tables summarize the amortized costs and estimated fair value of the securities portfolio at September 30, 2012 and December 31, 2011. The summary is divided into available for sale and held to maturity investment securities.

September 30, 2012 (In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available For Sale				
Obligations of U.S. government-sponsored entities	$74,407	$293	$2	$74,698
Obligations of states and political subdivisions	100,192	5,417	36	105,573
Mortgage-backed securities – residential	400,240	13,983	38	414,185
Mutual funds and equity securities	579	33	-	612
Corporate debt securities	6,741	46	1,299	5,488
Total securities – available for sale	$582,159	$19,772	$1,375	$600,556
Held To Maturity				
Obligations of states and political subdivisions	$875	$133	$-	$1,008

December 31, 2011 (In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available For Sale				
Obligations of U.S. government-sponsored entities	$95,770	$408	$15	$96,163
Obligations of states and political subdivisions	80,801	3,903	85	84,619
Mortgage-backed securities – residential	397,675	11,384	196	408,863
Mortgage-backed securities – commercial	203	6	-	209
Mutual funds and equity securities	1,601	-	-	1,601
Corporate debt securities	7,901	-	1,537	6,364
Total securities – available for sale	$583,951	$15,701	$1,833	$597,819
Held To Maturity				
Obligations of states and political subdivisions	$875	$99	$-	$974

The amortized cost and estimated fair value of the debt securities portfolio at September 30, 2012, by contractual maturity, are detailed below. The summary is divided into available for sale and held to maturity securities. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Mortgage-backed securities are stated separately due to the nature of payment and prepayment characteristics of these securities, as principal is not due at a single date.

	Available For Sale		Held To Maturity	
September 30, 2012 (In thousands)	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	$3,143	$3,145	$-	$-
Due after one year through five years	58,570	59,380	-	-
Due after five years through ten years	99,166	103,288	-	-
Due after ten years	20,461	19,946	875	1,008
Mortgage-backed securities	400,240	414,185	-	-
Total	$581,580	$599,944	$875	$1,008

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Gross realized gains and losses on the sale of available for sale investment securities were as follows:

(In thousands)	Three Months Ended September 30, 2012	2011	Nine Months Ended September 30, 2012	2011
Gross realized gains	$ 343	$ 400	$ 1,038	$ 1,226
Gross realized losses	67	14	74	17
Net realized gains	$ 276	$ 386	$ 964	$ 1,209

Investment securities with unrealized losses at September 30, 2012 and December 31, 2011 not recognized in income are presented in the tables below. The tables segregate investment securities that have been in a continuous unrealized loss position for less than twelve months from those that have been in a continuous unrealized loss position for twelve months or more. The tables also include the fair value of the related securities.

	Less than 12 Months		12 Months or More		Total	
September 30, 2012 (In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. government-sponsored entities	$7,872	$2	$-	$-	$7,872	$2
Obligations of states and political subdivisions	4,882	36	-	-	4,882	36
Mortgage-backed securities – residential	7,259	38	-	-	7,259	38
Corporate debt securities	-	-	4,548	1,299	4,548	1,299
Total	$20,013	$76	$4,548	$1,299	$24,561	$1,375

	Less than 12 Months		12 Months or More		Total	
December 31, 2011 (In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. government-sponsored entities	$13,494	$15	$-	$-	$13,494	$15
Obligations of states and political subdivisions	2,913	20	6,886	65	9,799	85
Mortgage-backed securities – residential	56,249	196	-	-	56,249	196
Corporate debt securities	-	-	4,299	1,537	4,299	1,537
Total	$72,656	$231	$11,185	$1,602	$83,841	$1,833

Unrealized losses included in the tables above have not been recognized in income since they have been identified as temporary. The Company evaluates investment securities for other-than-temporary impairment ("OTTI") at least quarterly, and more frequently when economic or market conditions warrant. Many factors are considered, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was effected by macroeconomic conditions, and (4) whether the Company has the intent to sell the security or more likely than not will be required to sell the security before its anticipated recovery. The assessment of whether an OTTI charge exists involves a high degree of subjectivity and judgment and is based on the information available to the Company at a point in time.

At September 30, 2012, the Company's investment securities portfolio had gross unrealized losses of $1.4 million, an improvement of $458 thousand or 25.0% from year-end 2011. Of the total gross unrealized losses at September 30, 2012, $1.3 million relates to investments that have been in a continuous loss position for 12 months or more. All of the investments with an unrealized losses position for 12 or more months consist of corporate debt securities. The unrealized loss position of corporate debt securities has improved $238 thousand or 15.5% from year-end 2011 and $203 thousand or 13.5% from June 30, 2012.

Corporate debt securities in the Company's investment securities portfolio at September 30, 2012 include $4.5 million carrying value of single-issuer trust preferred capital securities issued by a national and global financial services firm. These securities are currently performing and, although downgraded in the second quarter of 2012, continue to be rated as investment grade by major rating agencies. The unrealized losses on corporate debt securities is mainly a result of the general decline in financial markets and illiquidity events that began in 2008 and is not due to adverse changes in the expected cash flows of the individual securities. Overall market declines, particularly of banking and financial institutions, are a result of significant stress throughout the regional and national economy that began during 2008 and has not fully stabilized.

The Company attributes the unrealized losses in other sectors of its investment securities portfolio to changes in market interest rates. In general, market rates for these securities exceed the yield available at the time many of the securities in the portfolio were purchased. The Company does not expect to incur a loss on these securities unless they are sold prior to maturity. The Company's current intent is to hold these securities until recovery.

Investment securities with unrealized losses at September 30, 2012 are performing according to their contractual terms. The Company does not have the intent to sell these securities and likely will not be required to sell these securities before their anticipated recovery. The Company does not consider any of the securities to be impaired due to reasons of credit quality or other factors.

7. Loans and Allowance for Loan Losses

Major classifications of loans outstanding are summarized as follows:

(In thousands)	September 30, 2012	December 31, 2011
Real Estate:		
Real estate – construction and land development	$ 115,324	$ 119,989
Real estate mortgage – residential	413,284	445,464
Real estate mortgage – farmland and other commercial enterprises	377,696	384,331
Commercial:		
Commercial and industrial	48,452	48,771
States and political subdivisions	22,489	23,601
Lease financing	3,510	7,578
Other	19,032	21,435
Consumer:		
Secured	12,154	14,214
Unsecured	6,531	7,151
Total loans	1,018,472	1,072,534
Less unearned income	(161)	(426)
Total loans, net of unearned income	$ 1,018,311	$ 1,072,108

Activity in the allowance for loan losses by portfolio segment was as follows for the periods indicated.

(In thousands)	Real Estate	Commercial	Consumer	Total
Three months ended September 30, 2012				
Balance, beginning of period	$24,221	$2,137	$755	$27,113
Provision for loan losses	(1,114)	591	267	(256)
Recoveries	50	8	80	138
Loans charged off	(1,716)	(36)	(99)	(1,851)
Balance, end of period	$21,441	$2,700	$1,003	$25,144
Nine months ended September 30, 2012				
Balance, beginning of period	$23,538	$3,508	$1,218	$28,264
Provision for loan losses	2,916	(790)	(64)	2,062
Recoveries	252	129	192	573
Loans charged off	(5,265)	(147)	(343)	(5,755)
Balance, end of period	$21,441	$2,700	$1,003	$25,144

(In thousands)	Real Estate	Commercial	Consumer	Total
Three months ended September 30, 2011				
Balance, beginning of period	$25,432	$3,369	$937	$29,738
Provision for loan losses	3,742	(775)	265	3,232
Recoveries	105	622	90	817
Loans charged off	(2,614)	(114)	(187)	(2,915)
Balance, end of period	$26,665	$3,102	$1,105	$30,872
Nine months ended September 30, 2011				
Balance, beginning of period	$24,527	$3,260	$997	$28,784
Provision for loan losses	10,367	(517)	351	10,201
Recoveries	188	702	217	1,107
Loans charged off	(8,417)	(343)	(460)	(9,220)
Balance, end of period	$26,665	$3,102	$1,105	$30,872

The following tables present individually impaired loans by class of loans for the dates indicated.

September 30, 2012 (In thousands)	Recorded Investment	Unpaid Principal Balance	Allowance for Loan Losses Allocated
Impaired loans with no related allowance recorded:			
Real Estate			
Real estate – construction and land development	$22,576	$30,405	
Real estate mortgage – residential	4,060	4,578	
Real estate mortgage – farmland and other commercial enterprises	15,860	17,527	
Total	$42,496	$52,510	
Impaired loans with an allowance recorded:			
Real Estate			
Real estate – construction and land development	$10,733	$10,700	$696
Real estate mortgage – residential	6,179	6,164	1,303
Real estate mortgage – farmland and other commercial enterprises	19,211	19,191	1,735
Commercial			
Commercial and industrial	250	247	244
Consumer			
Secured	22	22	18
Unsecured	277	275	162
Total	$36,672	$36,599	$4,158

December 31, 2011 (In thousands)	Recorded Investment	Unpaid Principal Balance	Allowance for Loan Losses Allocated
Impaired loans with no related allowance recorded:			
Real Estate			
Real estate – construction and land development	$26,363	$26,337	
Real estate mortgage – residential	22,923	22,843	
Real estate mortgage – farmland and other commercial enterprises	43,765	43,438	
Commercial			
Commercial and industrial	2,982	2,939	
Consumer			
Unsecured	19	18	
Total	$96,052	$95,575	
Impaired loans with an allowance recorded:			
Real Estate			
Real estate – construction and land development	$13,440	$13,425	$139
Real estate mortgage – residential	13,239	13,197	998
Real estate mortgage – farmland and other commercial enterprises	15,070	15,035	600
Commercial			

Commercial and industrial	456	453	159
Consumer			
Secured	60	58	30
Total	$42,265	$42,168	$1,926

(In thousands)	Three Months Ended September 30, 2012	2011	Nine Months Ended September 30, 2012	2011
Average of individually impaired loans:				
Real Estate				
Real estate – construction and land development	$26,902	$44,832	$37,921	$55,755
Real estate mortgage – residential	8,979	27,731	14,744	29,665
Real estate mortgage – farmland and other commercial enterprises	35,076	53,957	38,967	62,980
Commercial				
Commercial and industrial	214	2,989	426	3,947
Other	-	665	-	224
Consumer				
Secured	22	74	66	74
Unsecured	374	-	251	-
Total average of impaired loans	$71,567	$130,248	$92,375	$152,645
Interest income recognized during impairment:				
Real Estate				
Real estate – construction and land development	$249	$229	$630	$862
Real estate mortgage – residential	52	270	308	1,024
Real estate mortgage – farmland and other commercial enterprises	418	560	1,419	2,038
Commercial				
Commercial and industrial	8	39	22	147
Other	-	10	-	10
Consumer				
Secured	-	1	5	4
Unsecured	8	-	13	-
Total interest income recognized during impairment	$735	$1,109	$2,397	$4,085
Cash-basis interest income recognized:				
Real Estate				
Real estate – construction and land development	$204	$229	$573	$765
Real estate mortgage – residential	44	265	298	986
Real estate mortgage – farmland and other commercial enterprises	608	550	1,437	1,925
Commercial				
Commercial and industrial	8	39	22	146
Consumer				
Secured	-	1	5	4
Unsecured	7	-	12	-
Total cash-basis interest income recognized	$871	$1,084	$2,347	$3,826

The following tables present the balance of the allowance for loan losses and the recorded investment in loans by portfolio segment based on impairment method as of September 30, 2012 and December 31, 2011.

September 30, 2012 (In thousands)	Real Estate	Commercial	Consumer	Total
Allowance for Loan Losses				
Ending allowance balance attributable to loans:				
Individually evaluated for impairment	$3,734	$244	$180	$4,158
Collectively evaluated for impairment	17,707	2,456	823	20,986
Total ending allowance balance	$21,441	$2,700	$1,003	$25,144
Loans				
Loans individually evaluated for impairment	$78,619	$250	$299	$79,168
Loans collectively evaluated for impairment	827,685	93,072	18,386	939,143
Total ending loan balance, net of unearned income	$906,304	$93,322	$18,685	$1,018,311

December 31, 2011 (In thousands)	Real Estate	Commercial	Consumer	Total
Allowance for Loan Losses				
Ending allowance balance attributable to loans:				
Individually evaluated for impairment	$1,737	$159	$30	$1,926
Collectively evaluated for impairment	21,801	3,349	1,188	26,338
Total ending allowance balance	$23,538	$3,508	$1,218	$28,264
Loans				
Loans individually evaluated for impairment	$134,800	$3,438	$79	$138,317
Loans collectively evaluated for impairment	814,984	97,521	21,286	933,791
Total ending loan balance, net of unearned income	$949,784	$100,959	$21,365	$1,072,108

The following tables present the recorded investment in nonperforming loans by class of loans as of September 30, 2012 and December 31, 2011.

September 30, 2012 (In thousands)	Nonaccrual	Restructured Loans	Loans Past Due 90 Days or More and Still Accruing
Real Estate:			
Real estate – construction and land development	$16,652	$8,736	$28
Real estate mortgage – residential	8,891	717	-
Real estate mortgage – farmland and other commercial enterprises	16,778	16,996	-
Commercial:			
Commercial and industrial	645	-	-
Lease financing	162	-	-
Consumer:			
Secured	21	-	-

Unsecured	1	-	-
Total	$43,150	$26,449	$28

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December 31, 2011 (In thousands)	Nonaccrual	Restructured Loans	Loans Past Due 90 Days or More and Still Accruing
Real Estate:			
Real estate – construction and land development	$30,744	$6,207	$-
Real estate mortgage – residential	14,578	4,894	-
Real estate mortgage – farmland and other commercial enterprises	13,831	8,024	-
Commercial:			
Commercial and industrial	386	-	-
Lease financing	124	-	-
Consumer:			
Secured	80	-	-
Unsecured	12	-	1
Total	$59,755	$19,125	$1

The Company has allocated $1.6 million of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as of September 30, 2012. The Company has no commitments to lend additional amounts to customers with outstanding loans that are classified as troubled debt restructurings.

During the nine months ended September 30, 2012, the Company had two credits that were modified as troubled debt restructurings. One restructuring includes a commercial real estate credit whereby the stated interest rate was reduced to 5.0% from 7.25% and repayment terms that include an initial six month interest only component. This credit had a pre and post-modification recorded investment of $8.8 million and $8.7 million, respectively. The restructuring resulted in an increase in the allowance for loan losses of $437 thousand and there were no related charge-offs recorded. The remaining restructured credit included reducing the stated interest rate on the loan to 4.125% from 6.0% and extending the due date by three months. This loan is secured by residential real estate and had a pre and post-modification recorded investment of $72 thousand. This restructuring increased the allowance for loan losses by $5 thousand and there were no related charge-offs recorded. The Company had no restructured credits during the first nine months of 2012 for which there was a payment default within twelve months following the modification.

During the nine months ending September 30, 2011, the Company had one restructured credit for which there was a payment default within twelve months following the modification. This credit represents a real estate construction and land development project with an outstanding balance of $2.9 million at September 30, 2011. This credit has a specific reserve allocation of $68 thousand at September 30, 2011 and related charge-offs were recorded during 2011 in the amount of $232 thousand.

The tables below present an age analysis of past due loans 30 days or more by class of loans as of the dates indicated. Past due loans that are also classified as nonaccrual are included in their respective past due category.

September 30, 2012 (In thousands)	30-89 Days Past Due	90 Days or More Past Due	Total	Current	Total Loans
Real Estate:					
Real estate – construction and land development	$104	$10,224	$10,328	$104,996	$115,324
Real estate mortgage – residential	2,298	4,430	6,728	406,556	413,284
Real estate mortgage – farmland and other commercial enterprises	537	14,631	15,168	362,528	377,696
Commercial:					
Commercial and industrial	99	462	561	47,891	48,452
States and political subdivisions	-	-	-	22,489	22,489
Lease financing, net	8	162	170	3,179	3,349
Other	39	5	44	18,988	19,032
Consumer:					
Secured	67	10	77	12,077	12,154
Unsecured	138	-	138	6,393	6,531
Total	$3,290	$29,924	$33,214	$985,097	$1,018,311

December 31, 2011 (In thousands)	30-89 Days Past Due	90 Days or More Past Due	Total	Current	Total Loans
Real Estate:					
Real estate – construction and land development	$3,343	$18,970	$22,313	$97,676	$119,989
Real estate mortgage – residential	5,836	7,352	13,188	432,276	445,464
Real estate mortgage – farmland and other commercial enterprises	1,684	12,497	14,181	370,150	384,331
Commercial:					
Commercial and industrial	98	300	398	48,373	48,771
States and political subdivisions	-	-	-	23,601	23,601
Lease financing, net	80	96	176	6,976	7,152
Other	29	-	29	21,406	21,435
Consumer:					
Secured	200	17	217	13,997	14,214
Unsecured	61	5	66	7,085	7,151
Total	$11,331	$39,237	$50,568	$1,021,540	$1,072,108

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends and conditions. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis includes large-balance loans and non-homogeneous loans, such as commercial real estate and certain residential real estate loans. Loan rating grades, as described further below, are assigned based on a continuous process. The Company uses the following definitions for its risk ratings:

Special Mention. Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the borrower's repayment ability, weaken the collateral or inadequately protect the Company's credit position at some future date. These credits pose elevated risk, but their weaknesses do not yet justify a substandard classification.

Substandard. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful. Loans classified as doubtful have all the weaknesses inherent of those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loans not meeting the criteria above which are analyzed individually as part of the above described process are considered to be pass rated loans. Based on the most recent analysis performed, the risk category of loans by class of loans is as follows for the dates indicated.

	Real Estate			Commercial			
September 30, 2012 (In thousands)	Real Estate-Construction and Land Development	Real Estate Mortgage-Residential	Real Estate Mortgage-Farmland and Other Commercial Enterprises	Commercial and Industrial	States and Political Subdivisions	Lease Financing	Other
Credit risk profile by internally assigned rating grades:							
Pass	$72,675	$ 366,496	$ 296,834	$41,249	$ 22,489	$3,187	$18,532
Special mention	7,576	19,467	31,254	6,159	-	-	492
Substandard	35,073	27,172	47,976	968	-	162	8
Doubtful	-	149	1,632	76	-	-	-
Total	$115,324	$ 413,284	$ 377,696	$48,452	$ 22,489	$3,349	$19,032

	Real Estate			Commercial			
December 31, 2011 (In thousands)	Real Estate-Construction and Land Development	Real Estate Mortgage-Residential	Real Estate Mortgage-Farmland and Other Commercial Enterprises	Commercial and Industrial	States and Political Subdivisions	Lease Financing	Other
Credit risk profile by internally assigned rating grades:							
Pass	$65,306	$ 386,134	$ 303,512	$41,556	$ 23,601	$7,022	$20,415
Special mention	7,443	16,585	19,393	2,969	-	6	1,000
Substandard	47,091	41,468	59,395	4,103	-	124	20
Doubtful	149	1,277	2,031	143	-	-	-
Total	$119,989	$ 445,464	$ 384,331	$48,771	$ 23,601	$7,152	$21,435

The Company considers the performance of the loan portfolio and its impact on the allowance for loan losses. For consumer loan classes, the Company evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. The following table presents the consumer loans outstanding based on payment activity as of September 30, 2012 and December 31, 2011.

	September 30, 2012 Consumer		December 31, 2011 Consumer	
(In thousands)	Secured	Unsecured	Secured	Unsecured

Credit risk profile based on payment activity:				
Performing	$ 12,133	$ 6,530	$ 14,134	$ 7,138
Nonperforming	21	1	80	13
Total	$ 12,154	$ 6,531	$ 14,214	$ 7,151

8. Other Real Estate Owned

OREO was as follows as of the dates indicated:

(In thousands)		September 30, 2012		December 31, 2011
Construction and land development	$	30,096	$	21,951
Residential real estate		6,382		5,591
Farmland and other commercial enterprises		11,002		10,615
Total	$	47,480	$	38,157

OREO activity for the nine months ended September 30, 2012 and 2011 was as follows:

Nine months ended September 30, (In thousands)		2012			2011	
Beginning balance	$	38,157		$	30,545	
Transfers from loans		21,914			18,449	
Proceeds from sales		(10,148	)		(7,738	)
Loss on sales		(241	)		(298	)
Write downs and other decreases, net		(2,202	)		(4,965	)
Ending balance	$	47,480		$	35,993	

9. Postretirement Medical Benefits

Prior to 2003, the Company provided lifetime medical and dental benefits upon retirement for certain employees meeting the eligibility requirements as of December 31, 1989 (Plan 1). During 2003, the Company implemented an additional postretirement health insurance program (Plan 2). Under Plan 2, any employee meeting the service requirement of 20 years of full time service to the Company and is at least age 55 years of age upon retirement is eligible to continue their health insurance coverage. Under both plans, retirees not yet eligible for Medicare have coverage identical to the coverage offered to active employees. Under both plans, Medicare-eligible retirees are provided with a Medicare Advantage plan. The Company pays 100% of the cost of Plan 1. The Company and the retirees each pay 50% of the cost under Plan 2. Both plans are unfunded.

The following disclosures of the net periodic benefit cost components of Plan 1 and Plan 2 were measured at January 1, 2012 and 2011.

	Three Months Ended September 30,				Nine Months Ended September 30,			
(In thousands)		2012		2011		2012		2011
Service cost	$	155	$	108	$	463	$	324
Interest cost		152		152		456		454
Amortization of transition obligation		24		24		76		76
Recognized prior service cost		65		65		193		193
Recognized net actuarial loss		14		-		42		-
Net periodic benefit cost	$	410	$	349	$	1,230	$	1,047

The Company expects benefit payments of $330 thousand for 2012, of which $65 thousand and $196 thousand have been made during the three and nine months ended September 30, 2012, respectively.

10. Regulatory Matters

The Company and its subsidiary banks are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements will initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the banks must meet specific capital guidelines that involve quantitative measures of the banks' assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Company and its subsidiary banks' capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

The regulatory ratios of the consolidated Company and its subsidiary banks were as follows for the dates indicated.

	September 30, 2012			December 31, 2011		
	Tier 1 Risk-based Capital1	Total Risk-based Capital1	Tier 1 Leverage2	Tier 1 Risk-based Capital1	Total Risk-based Capital1	Tier 1 Leverage2
Consolidated	17.89 %	19.15 %	10.79 %	16.68 %	17.95 %	9.99 %
Farmers Bank	17.70	18.96	9.47	17.58	18.84	9.47
First Citizens	12.61	13.41	8.99	13.47	14.21	8.93
United Bank	15.32	16.60	9.41	13.51	14.79	8.44
Citizens Northern	12.84	14.09	9.01	12.24	13.49	8.48

1Tier 1 Risk-based and Total Risk-based Capital ratios are computed by dividing a bank's Tier 1 or Total Capital, as defined by regulation, by a risk-weighted sum of the bank's assets, with the risk weighting determined by general standards established by regulation. The safest assets (e.g., government obligations) are assigned a weighting of 0% with riskier assets receiving higher ratings (e.g., ordinary commercial loans are assigned a weighting of 100%).

2Tier 1 Leverage ratio is computed by dividing a bank's Tier 1 Capital, as defined by regulation, by its total quarterly average assets.

Summary of Regulatory Agreements

Below is a summary of the regulatory agreements that the Parent Company and three of its subsidiary banks have entered into with their primary regulators. For a more complete discussion and additional information regarding these regulatory actions, please refer to the section captioned "Capital Resources" under Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" of the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

Parent Company

Primarily due to the regulatory actions and capital requirements at three of the Company's subsidiary banks (as discussed below), the Federal Reserve Bank of St. Louis ("FRB St. Louis") and Kentucky Department of Financial Institutions ("KDFI") proposed the Company enter into a Memorandum of Understanding ("Memorandum"). The Company's board approved entry into the Memorandum at a regular board meeting during the fourth quarter of 2009. Pursuant to the Memorandum, the Company agreed that it would develop an acceptable capital plan to ensure that the consolidated organization remains well-capitalized and each of its subsidiary banks meet the capital requirements imposed by their regulator as summarized below.

The Company also agreed to reduce its common stock dividend in the fourth quarter of 2009 from $.25 per share down to $.10 per share and not make interest payments on the Company's trust preferred securities or dividends on its common or preferred stock without prior approval from FRB St. Louis and KDFI. Representatives of the FRB St. Louis and KDFI have indicated that any such approval for the payment of dividends will be predicated on a demonstration of adequate, normalized earnings on the part of the Company's subsidiaries sufficient to support quarterly payments on the Company's trust preferred securities and quarterly dividends on the Company's common and preferred stock. While both regulatory agencies have granted approval of all subsequent quarterly Company requests to make interest payments on its trust preferred securities and dividends on its preferred stock, the Company has not (based on the assessment by Company management of both the Company's capital position and the earnings of its subsidiaries) sought regulatory approval for the payment of common stock dividends since the fourth quarter of

2009. Moreover, the Company will not pay any such dividends on its common stock in any subsequent quarter until the regulator's assessment of the earnings of the Company's subsidiaries, and the Company's assessment of its capital position, both yield the conclusion that the payment of a Company common stock dividend is warranted.

Other components in the regulatory order for the parent company include requesting and receiving regulatory approval for the payment of new salaries/bonuses or other compensation to insiders; assisting its subsidiary banks in addressing weaknesses identified in their reports of examinations; providing periodic reports detailing how it will meet its debt service obligations; and providing progress reports with its compliance with the regulatory Memorandum.

Farmers Bank

In November of 2009, the KDFI and FRB St. Louis entered into a Memorandum with Farmers Bank. The Memorandum requires that Farmers Bank obtain written consent prior to declaring or paying the Parent Company a cash dividend and to achieve and maintain a Tier 1 Leverage ratio of 8.0% by June 30, 2010. The Parent Company injected from its reserves $11 million in capital into Farmers Bank subsequent to the Memorandum and an additional $200 thousand during 2010. During the third quarter of 2012, Farmers Bank paid dividends in the amount of $4.0 million to the Parent Company after receiving approval from its regulators. At September 30, 2012, Farmers Bank had a Tier 1 Leverage ratio of 9.47% and a Total Risk-based Capital ratio of 18.96%.

Other parts of the regulatory order include the development and documentation of plans for reducing problem loans, providing progress reports on compliance with the Memorandum, developing and implementing a written profit plan and strategic plans, and evaluating policies and procedures for monitoring construction loans and use of interest reserves. It also restricts the bank from extending additional credit to borrowers with credits classified as substandard, doubtful or special mention in the report of examination.

United Bank

In November of 2009, the Federal Deposit Insurance Corporation (“FDIC”) and United Bank entered into a Cease and Desist Order (“C&D”) primarily as a result of its level of nonperforming assets. The C&D was terminated in December 2011 coincident with the issuance of a Consent Order (“Consent Order”) entered into between the parties. The Consent Order is substantially the same as the C&D, with the primary exception being that United Bank must achieve and maintain a Tier 1 Leverage ratio of 9.0% and a Total Risk-based Capital ratio of 13.0% no later than March 31, 2012.

During the first quarter of 2012, the Parent Company injected from its reserves $2.5 million in capital into United Bank in order for it to comply with the Consent Order. At September 30, 2012, United Bank had a Tier 1 Leverage ratio of 9.41% and a Total Risk-based Capital ratio of 16.60%. The Parent Company has injected from its reserves $18.9 million of capital into United Bank since the fourth quarter of 2009.

Other components in the regulatory order include stricter oversight and reporting to its regulators in terms of complying with the Order. It also includes an increase in the level of reporting by management to its board of directors of its financial results, budgeting, and liquidity analysis, as well as restricting the bank from extending additional credit to borrowers with credits classified as substandard, doubtful or special mention in the report of examination. There is also a requirement to obtain written consent prior to declaring or paying a dividend and to develop a written contingency plan if the bank is unable to meet the capital levels established in the Consent Order.

Citizens Northern

The KDFI and the FDIC entered into a Memorandum with Citizens Northern in September of 2010. The Memorandum requires that Citizens Northern obtain written consent prior to declaring or paying a dividend and to increase Tier 1 Leverage ratio to equal or exceed 7.5% prior to September 30, 2010 and to achieve and maintain Tier 1 Leverage ratio to equal or exceed 8.0% prior to December 31, 2010. In December 2010, the Parent Company injected $250 thousand of capital into Citizens Northern to bring its Tier 1 Leverage ratio up to 8.04% as of year-end 2010. At September 30, 2012, Citizens Northern had a Tier 1 Leverage ratio of 9.01% and a Total Risk-based Capital ratio of 14.09%.

Other parts of the regulatory order include the development and documentation of plans for reducing problem loans, providing progress reports on compliance with the Memorandum, and for the development and implementation of a written profit plan and strategic plans. It also restricts the bank from extending additional credit to borrowers with credits classified as substandard, doubtful or special mention in the report of examination.

Regulators continue to monitor the Company’s progress and compliance with the regulatory agreements through periodic on-site examinations, regular communications, and quarterly data analysis. At the Parent Company and at each of its bank subsidiaries, the Company believes it is adequately addressing all issues of the regulatory agreements to which it is subject. However, only the respective regulatory agencies can determine if compliance with the applicable regulatory agreements has been met. The Company believes that it and its subsidiary banks are in compliance with the requirements identified in the regulatory agreements as of September 30, 2012.

The Parent Company maintains cash available to fund a certain amount of additional injections of capital to its bank subsidiaries as determined by management or if required by its regulators. If needed, further amounts in excess of available cash may be funded by future public or private sales of securities, although the Parent Company is currently under no directive by its regulators to raise any additional capital.

11. Preferred Stock and Warrant

In January of 2009, as part of the Treasury’s Capital Purchase Program (“CPP”), the Company issued 30 thousand shares of Series A, no par value cumulative perpetual preferred stock to the Treasury for $30.0 million pursuant to a Letter Agreement and Securities Purchase Agreement. These agreements required the Company to comply with certain executive compensation limitations included in the Emergency Economic Stabilization Act of 2008 for the period during which Treasury held the Company’s preferred shares. The Company also issued a warrant to the Treasury as part of the CPP allowing it to purchase 223,992 shares of the Company’s common stock at an exercise price of $20.09.

During June 2012, the Treasury conducted an auction as part of ongoing efforts to wind down and recover its remaining CPP investments. The auction included preferred stock positions held by the Treasury of seven banks participating in the CPP, including the $30.0 million investment in the Company’s Series A preferred stock. The Treasury was successful in selling all of its investment in the Company’s Series A preferred stock to private investors through a registered public offering. The Company received no proceeds as part of the transaction. Since the Treasury no longer owns the preferred stock, the executive compensation and other restrictions put in place by the Treasury no longer apply. The Company continues to view the outstanding preferred stock as an important component of its capital structure.

On July 18, 2012, the Company repurchased the warrant it issued to the Treasury as part of the CPP. The Company repurchased the warrant at a mutually agreed upon price of $75 thousand. The repurchase of the warrant had no impact on the Company’s results of operations, although cash and shareholders’ equity declined by the amount of the purchase price. Upon settlement of the warrant repurchase, the Treasury has no remaining equity stake in the Company.

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

FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements with the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), under the Private Securities Litigation Reform Act of 1995 that involve risks and uncertainties. Statements in this report that are not statements of historical fact are forward-looking statements. In general, forward-looking statements relate to a discussion of future financial results or projections, future economic performance, future operational plans and objectives, and statements regarding the underlying assumptions of such statements. Although management of Farmers Capital Bank Corporation (the "Company" or "Parent Company") believes that the assumptions underlying the forward-looking statements contained herein are reasonable, any of the assumptions could be inaccurate, and therefore, there can be no assurance that the forward-looking statements included herein will prove to be accurate.

Various risks and uncertainties may cause actual results to differ materially from those indicated by the Company's forward-looking statements. In addition to the risks described under Part 1, Item 1A "Risk Factors" in the Company's most recent annual report on Form 10-K, factors that could cause actual results to differ from the results discussed in the forward-looking statements include, but are not limited to: economic conditions (both generally and more specifically in the markets in which the Company and its subsidiaries operate) and lower interest margins; competition for the Company's customers from other providers of financial services; deposit outflows or reduced demand for financial services and loan products; government legislation, regulation, and changes in monetary and fiscal policies (which changes from time to time and over which the Company has no control); changes in interest rates; changes in prepayment speeds of loans or investment securities; inflation; material unforeseen changes in the liquidity, results of operations, or financial condition of the Company's customers; changes in the level of non-performing assets and charge-offs; changes in the number of common shares outstanding; the capability of the Company to successfully enter into a definitive agreement for and close anticipated transactions; the possibility that acquired entities may not perform as well as expected; unexpected claims or litigation against the Company; technological or operational difficulties; the impact of new accounting pronouncements and changes in policies and practices that may be adopted by regulatory agencies; acts of war or terrorism; the ability of the parent company to receive dividends from its subsidiaries; the impact of larger or similar financial institutions encountering difficulties, which may adversely affect the banking industry or the Company; the Company or its subsidiary banks' ability to maintain required capital levels and adequate funding sources and liquidity; and other risks or uncertainties detailed in the Company's filings with the Securities and Exchange Commission, all of which are difficult to predict and many of which are beyond the control of the Company.

The Company's forward-looking statements are based on information available at the time such statements are made. The Company expressly disclaims any intent or obligation to update any forward-looking statements to reflect changes in underlying assumptions or factors, new information, future events, or other changes.

RESULTS OF OPERATIONS

Third Quarter 2012 Compared to Third Quarter 2011

The Company reported net income of $3.1 million for the quarter ended September 30, 2012, an increase of $2.8 million compared with net income of $272 thousand for the third quarter a year ago. On a per common share basis, net income for the current quarter was $.35, an increase of $.38 compared to a net loss of $.03 reported for the third quarter of 2011. Selected income statement amounts and related data are presented in the table below.

(In thousands except per share data) Three Months Ended September 30,	2012	2011	Change
Interest income	$17,578	$19,493	$(1,915)
Interest expense	4,511	6,096	(1,585)
Net interest income	13,067	13,397	(330)
Provision for loan losses	(256)	3,232	(3,488)
Net interest income after provision for loan losses	13,323	10,165	3,158
Noninterest income	6,166	6,260	(94)
Noninterest expenses	15,347	16,959	(1,612)
Income (loss) before income tax expense	4,142	(534)	4,676
Income tax expense (benefit)	1,051	(806)	1,857
Net income	$3,091	$272	$2,819
Less preferred stock dividends and discount accretion	481	474	7
Net income (loss) available to common shareholders	$2,610	$(202)	$2,812
Basic and diluted net income (loss) per common share	$.35	$(.03)	$.38
Weighted average common shares outstanding – basic and diluted	7,461	7,427	34
Return on average assets	.65%	.06%	59 bp
Return on average equity	7.38%	.69%	669 bp

bp = basis points.

The $2.8 million or $.38 per common share increase in net income for the third quarter of 2012 compared to the same quarter a year ago was mainly driven by a decrease of $3.5 million or 108% and $2.0 million or 57.1% in the provision for loan losses and expenses associated with repossessed real estate, respectively, partially offset by an increase in income tax expense of $1.9 million. Further information related to the more significant components making up the increase in net income follows.

Net Interest Income

The overall interest rate environment at September 30, 2012, as measured by the Treasury yield curve, remains at very low levels in historical terms. Shorter-term yields for three and six-month maturities have increased 8 basis points and 7 basis points, respectively since year-end 2011. For longer-term maturities, three year maturities decreased 5 basis points while the five, ten, and thirty year maturity periods declined 21, 24, and 7 basis points, respectively. At September 30, 2012, the short-term federal funds target interest rate was between zero and .25%, which has remained unchanged since December 2008. The Federal Reserve Board has indicated an objective of holding short-term interest rates at exceptionally low levels through mid-2015. The near historical low rate environment makes managing the Company's net interest margin very challenging.

Net interest income was $13.1 million for the current quarter, a decrease of $330 thousand or 2.5% compared to $13.4 million for the prior-year third quarter. The decrease in net interest income is attributed mainly to a $1.9 million or 9.8% decrease in interest income, primarily on loans, which was partially offset by a $1.6 million or 26.0% decrease in interest expense, primarily on deposits. The decrease in total interest income and interest expense is attributed to both rate and volume declines related mainly to loans and deposits and are the result of the overall weak economic environment combined with the Company's balance sheet management strategy. The overall weak economy has generally resulted in lower interest rates while the Company has become more selective in pricing deposits and extending loans, chiefly to reduce its costs of funds and improve net interest margin, overall profitability, and its capital position. The Company is generally earning and paying less interest from its earning assets and funding sources as the average rates earned and paid have decreased. This includes repricing of variable and floating rate assets and liabilities that have reset to overall lower amounts since their previous repricing date as well as activity related to new earning assets and funding sources. Additionally, an increase in available funds has been invested in lower yielding investment securities or cash equivalents in response to a decrease in high quality loan demand.

Interest income and interest expense related to nearly all categories of the Company's earning assets and interest paying liabilities have declined in the quarterly comparison. The $1.9 million decrease from interest income in the comparison is primarily made up of lower interest on loans and investment securities of $1.4 million or 8.9% and $550 thousand or 13.1%, respectively. The decrease in interest on loans was driven primarily by an $86.7 million or 7.7% decrease in average volume and, to a lesser extent, a decrease in the average rate earned of six basis points to 5.4% from 5.5%. For investment securities, the decrease in interest income is rate driven, as a 50 basis point decrease in the average rate earned of 2.5% more than offset a higher average balance outstanding of $40.0 million or 6.8%.

The $1.6 million decrease in interest expense is primarily a result of lower interest expense on deposits of $1.4 million or 39.7% followed by lower interest on borrowings of $173 thousand or 6.8%. The decrease in interest expense on deposits was driven by lower interest on time deposits of $1.2 million or 39.1% due to both a decrease in the average rate paid and volume declines. The average rate paid on time deposits was 1.3% and 1.8% for the current and prior years' third quarter, respectively. Average outstanding balances of time deposits were $574 million for the current quarter, a decrease of $107 million or 15.7% compared to a year earlier. Interest expense on borrowings decreased mainly as a result of maturities related to outstanding long-term Federal Home Loan Bank ("FHLB") advances.

The net interest margin on a taxable equivalent basis increased six basis points to 3.13% for the third quarter of 2012 compared to 3.07% in the same quarter of 2011. The increase in net interest margin was driven by an eight basis point increase in the spread between the average rate earned on earning assets and the average rate paid on interest bearing liabilities to 2.91% in the current quarter from 2.83% for the same quarter of 2011. The Company expects its net interest margin to trend upward in the near term according to internal modeling using expectations about future market interest rates, the maturity structure of the Company's earning assets and liabilities, and other factors. In particular, the Company's cost of funds is expected to decrease in the near term primarily from the maturity of $50.0 million of 3.98% fixed rate FHLB borrowings combined with $23.2 million of 6.60% fixed rate borrowings that reprice downward to a floating interest rate of three-month LIBOR plus 132 basis points. Each of these events occur during the fourth quarter of 2012. Future results could be significantly different than expectations.

The following tables present an analysis of net interest income for the quarterly periods ended September 30.

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

Three Months Ended September 30,	2012				2011			
(In thousands)	Average Balance	Interest	Average Rate		Average Balance	Interest	Average Rate	
Earning Assets								
Investment securities								
Taxable	$532,577	$3,084	2.30	%	$524,016	$3,746	2.84	%
Nontaxable1	92,634	843	3.62		61,214	677	4.39	
Interest bearing deposits in banks, federal funds sold and securities purchased under agreements to resell	64,181	38	.24		77,277	41	.21	
Loans1,2,3	1,032,914	14,073	5.42		1,119,634	15,456	5.48	
Total earning assets	1,722,306	$18,038	4.17	%	1,782,141	$19,920	4.43	%
Allowance for loan losses	(26,806)				(30,166)			
Total earning assets, net of allowance for loan losses	1,695,500				1,751,975			
Nonearning Assets								
Cash and due from banks	25,543				16,956			
Premises and equipment, net	37,386				39,579			
Other assets	127,983				124,275			
Total assets	$1,886,412				$1,932,785			
Interest Bearing Liabilities								
Deposits								
Interest bearing demand	$277,654	$58	.08	%	$252,176	$87	.14	%
Savings	316,077	157	.20		296,843	305	.41	
Time	574,044	1,926	1.33		681,038	3,161	1.84	
Federal funds purchased and other short-term borrowings	24,158	24	.40		35,466	43	.48	
Securities sold under agreements to repurchase and other long-term borrowings	229,380	2,346	4.07		244,804	2,500	4.05	
Total interest bearing liabilities	1,421,313	$4,511	1.26	%	1,510,327	$6,096	1.60	%
Noninterest Bearing Liabilities								
Other demand deposits	240,120				216,694			
Other liabilities	58,257				49,628			
Total liabilities	1,719,690				1,776,649			
Shareholders' equity	166,722				156,136			
Total liabilities and shareholders' equity	$1,886,412				$1,932,785			
Net interest income		13,527				13,824		
TE basis adjustment		(460)				(427)		
Net interest income		$13,067				$13,397		
Net interest spread			2.91	%			2.83	%
Impact of noninterest bearing sources of funds			.22				.24	

Net interest margin	3.13	%	3.07	%

1Income and yield stated at a fully tax equivalent basis using the marginal corporate Federal tax rate of 35%.
2Loan balances include principal balances on nonaccrual loans.
3Loan fees included in interest income amounted to $235 thousand and $136 thousand in 2012 and 2011, respectively.

Analysis of Changes in Net Interest Income (tax equivalent basis)

(In thousands)	Variance	Variance Attributed to	
Three Months Ended September 30,	2012/2011 [1]	Volume	Rate
Interest Income			
Taxable investment securities	$ (662)	$ 395	$ (1,057)
Nontaxable investment securities[2]	166	826	(660)
Interest bearing deposits in banks, federal funds sold and securities purchased under agreements to resell	(3)	(27)	24
Loans[2]	(1,383)	(1,212)	(171)
Total interest income	(1,882)	(18)	(1,864)
Interest Expense			
Interest bearing demand deposits	(29)	53	(82)
Savings deposits	(148)	124	(272)
Time deposits	(1,235)	(447)	(788)
Federal funds purchased and other short-term borrowings	(19)	(13)	(6)
Securities sold under agreements to repurchase and other long-term borrowings	(154)	(234)	80
Total interest expense	(1,585)	(517)	(1,068)
Net interest income	$ (297)	$ 499	$ (796)
Percentage change	100.0 %	(168.0)%	268.0 %

1The changes that are not solely due to rate or volume are allocated on a percentage basis using the absolute values of rate and volume variances as a basis for allocation.
2Income stated at fully tax equivalent basis using the marginal corporate Federal tax rate of 35%.

Provision for Loan Losses

The provision for loan losses represents charges (or credits) to earnings that maintain an allowance for loan losses at an adequate level based on credit losses specifically identified in the loan portfolio, as well as management's best estimate of incurred probable loan losses in the remainder of the portfolio at the balance sheet date. The Company's loan quality, while beginning to improve, has been negatively impacted in recent years by adverse conditions in certain real estate sectors since the downturn in the overall economy and financial markets beginning in late 2007 and more significantly during 2008. This has led to declines in real estate values and deterioration in the financial condition of many of the Company's borrowers over the last several years, particularly borrowers in the commercial and real estate development industry. Declining real estate values have resulted in loans that have become under collateralized, which has elevated nonperforming loans, net charge-offs, and the provision for loan losses in recent years, particularly during the early and middle stages of the economic downturn. While the Company is beginning to experience improvement in overall credit quality, it has been necessary to lower the loan quality ratings on certain commercial and real estate development credits throughout the period of the economic downturn.

The Company recorded a credit of $256 thousand to the provision for loan losses for the third quarter of 2012, representing a decrease of $3.5 million or 108% compared to a $3.2 million charge for the third quarter of 2011. The allowance for loan losses as a percentage of outstanding loans (net of unearned income) was 2.47% at September 30, 2012 compared to 2.64% and 2.80% at year-end 2011 and September 30, 2011, respectively. The decrease in the provision for loan losses is attributed to an overall improvement in the credit quality of the loan portfolio and a decrease in loan balances outstanding. For further information about improvements in the Company's overall credit quality, please refer to the discussion under the captions "Allowance for Loan Losses" and "Nonperforming Loans" in this

Form 10-Q that follows.

Net charge-offs were $1.7 million for the current quarter, a decrease of $385 thousand or 18.4% when compared to the third quarter of 2011. Of the $1.7 million in net charge-offs in the current quarter, $1.0 million is attributed to four separate credit relationships. Of these four credit relationships, charge-offs totaling $845 thousand relate to three real estate development projects and $170 thousand is attributed to a not-for-profit, special needs educational center. On an annualized basis, quarterly net charge-offs were .66% of average loans outstanding for the three months ended September 30, 2012 compared to .74% for the third quarter of a year ago.

Noninterest Income

The components of noninterest income are as follows for the periods indicated:

Three Months Ended September 30, (In thousands)	2012	2011	Change
Service charges and fees on deposits	$ 2,062	$ 2,251	$ (189)
Allotment processing fees	1,304	1,342	(38)
Other service charges, commissions, and fees	1,104	1,055	49
Data processing income	47	156	(109)
Trust income	469	507	(38)
Investment securities gains, net	276	386	(110)
Gain on sale of mortgage loans, net	603	328	275
Income from company-owned life insurance	301	230	71
Other	-	5	(5)
Total noninterest income	$ 6,166	$ 6,260	$ (94)

The more significant items for discussion are included below.

- Service charges and fees on deposits decreased $189 thousand or 8.4% driven by a decline in fees from overdraft/insufficient funds of $220 thousand or 15.0% related to lower transaction volume. Transaction volume has declined similar to trends experienced by the banking industry as a whole, mainly as a result of increased consumer compliance regulations and changes in customer behavior that have evolved over the last several years.
- The decrease in data processing income of $109 thousand or 69.9% is driven by a $74 thousand or 78.7% decline in fees related to the winding down of the Commonwealth of Kentucky ("Commonwealth") depository services contract. Decreases in data processing revenues related to the general depository contract have been partially offset by noninterest expense reductions spread over multiple line items categories. Data processing fees have also declined $34 thousand or 93.5% due to lower processing volumes attributed to an increase in paperless payment transactions related to the Commonwealth's Women, Infants, and Children ("WIC") supplemental nutrition program. Such transactions are now being processed by an unrelated third party. The Company expects to continue processing only a small number of transactions that are subject to manual processing.
- The $110 thousand or 28.5% decrease in gains on the sale of investment securities is attributed to the volume, timing, and market value of the individual securities sold. Such sales take place at irregular intervals based on current asset and liability management strategies and market conditions. The Company periodically sells investment securities to lock in gains, increase yield, restructure expected future cash flows, and/or enhance its capital position as opportunities occur.
- Net gains on the sale of mortgage loans increased $275 thousand or 83.8% as the volume of loans sold increased to $21.4 million from $11.5 million in the comparison. The increase in loans sold has been helped significantly by the overall low interest rate environment, which is below already low levels from a year ago.

Noninterest Expense

The components of noninterest expense are as follows for the periods indicated:

Three Months Ended September 30, (In thousands)	2012	2011	Change
Salaries and employee benefits	$ 7,019	$ 6,646	$ 373
Occupancy expenses, net	1,235	1,254	(19)
Equipment expenses	576	659	(83)
Data processing and communication expense	1,059	1,147	(88)
Bank franchise tax	605	637	(32)
Amortization of intangibles	254	286	(32)
Deposit insurance expense	667	643	24
Other real estate expenses, net	1,531	3,569	(2,038)
Legal expenses	251	164	87
Other	2,150	1,954	196
Total noninterest expense	$ 15,347	$ 16,959	$ (1,612)

The more significant items for discussion are included below.

- Salaries and employee benefits increased $373 thousand or 5.6% in the comparison due mainly to an increase in the number of full time equivalent employees, including higher salaried positions in the credit administration and nonperforming asset management areas.
- Data processing and communications expenses decreased $88 thousand or 7.7% mainly as a result of an agreement the Company announced during the first quarter of 2012 to reduce its debit card processing expenses combined with costs savings related to the winding down of the Company's depository services contract with the Commonwealth.
- The $2.0 million or 57.1% decrease in other real estate expense is mainly due to lower impairment charges recorded of $2.3 million or 69.1% in the comparison. The decrease in impairment charges is attributed primarily to the recording of a $2.8 million impairment charge during the third quarter of 2011 related to a single real estate development project.
- Legal expenses increased $87 thousand or 53.0% due primarily to issues involving problem loans in the normal course of business.
- The $196 thousand or 10.0% increase in other noninterest expense was driven by a $260 thousand write-down to fair value of a property that was reclassified from bank premises to other real estate. The property was reclassified and written down to fair value after it was determined that the property would no longer be used for future banking purposes.

Income Taxes

Income tax expense was $1.1 million for the third quarter of 2012, with an effective income tax rate of 25.4%. The Company recorded an income tax benefit of $806 thousand for the third quarter of 2011. The effective income tax rate for that period is not meaningful. Income derived from tax exempt sources continues to be a substantial amount and the Company recorded a loss before income taxes in the comparable period.

First Nine Months of 2012 Compared to First Nine Months of 2011

Net income for the first nine months of 2012 was $9.5 million or $1.09 per common share. This represents an increase of $8.1 million or $1.08 per common share compared to the first nine months of 2011. Selected income statement amounts and related data are presented in the table below.

(In thousands except per share data)

Nine Months Ended September 30,	2012	2011	Change
Interest income	$54,075	$59,794	$(5,719)
Interest expense	14,434	18,919	(4,485)
Net interest income	39,641	40,875	(1,234)
Provision for loan losses	2,062	10,201	(8,139)
Net interest income after provision for loan losses	37,579	30,674	6,905
Noninterest income	18,606	18,493	113
Noninterest expenses	44,341	47,748	(3,407)
Income before income tax expense	11,844	1,419	10,425
Income tax expense (benefit)	2,297	(67)	2,364
Net income	$9,547	$1,486	$8,061
Less preferred stock dividends and discount accretion	1,439	1,419	20
Net income available to common shareholders	$8,108	$67	$8,041
Basic and diluted net income per common share	$1.09	$.01	$1.08
Weighted average common shares outstanding – basic and diluted	7,454	7,420	34
Return on average assets	.67 %	.10 %	57 bp
Return on average equity	7.82 %	1.29 %	653 bp

bp = basis points.

The $8.1 million or $1.08 per common share increase in net income for the nine months ending September 30, 2012 compared to the first nine months of 2011 is primarily due to decreases in the provision for loan losses and noninterest expenses of $8.1 million and $3.4 million, respectively, partially offset by lower net interest income of $1.2 million. Income tax expense increased $2.4 million. Further information related to the more significant components making up the increase in net income follows.

Net Interest Income

Net interest income was $39.6 million for the first nine months of 2012, a decrease of $1.2 million or 3.0% compared to $40.9 million for the first nine months of 2011. The decrease in net interest income is attributed to a $5.7 million or 9.6% decrease in interest income, primarily on loans, which was partially offset by a $4.5 million or 23.7% decrease in interest expense, primarily on deposits. Similar to the quarterly comparison, the decrease in total interest income and interest expense is mainly attributed to both rate and volume declines related to loans and deposits and are the result of both an overall weak economic environment and the Company's balance sheet management strategy. This strategy includes being more selective in pricing deposits and extending loans in an effort to improve net interest margin, overall profitability, and capital position. The Company is generally earning and paying less interest from its earning assets and funding sources as the average rates earned and paid have decreased. This includes repricing of variable and floating rate assets and liabilities that have reset to net overall lower amounts since their previous repricing date as well as activity related to new earning assets and funding sources. Moreover, an increase in available funds has been invested in lower yielding investment securities or cash equivalents in response to a decrease in high quality loan demand.

Nearly all of the Company's interest income and interest expense categories have declined in the nine-month comparison. The $5.7 million decrease from interest income in the comparison is primarily made up of lower interest on loans and investment securities of $4.9 million or 10.3% and $772 thousand or 6.2%, respectively. The decrease in interest on loans was driven primarily by a $101 million or 8.8% decrease in average volume and, to a lesser extent, a decrease in the average rate earned of 10 basis points to 5.5% from 5.6%. For investment securities, the decrease in interest income is driven primarily by a 62 basis point decrease in the average rate earned to 2.7% from 3.3%, which offset a $91.0 million or 16.9% increase in the average balance outstanding.

The $4.5 million decrease in interest expense is primarily a result of lower interest expense on deposits of $4.0 million or 35.1% followed by lower interest on borrowings of $533 thousand or 7.0%. The decrease in interest expense on deposits was driven by lower interest on time deposits of $3.3 million or 33.2% due to decreases in both the volume and average rate paid. Average outstanding balances of time deposits were $601 million for the current nine months, a decrease of $94.9 million or 13.6% compared to a year earlier. The average rate paid on time deposits was 1.5% and 1.9% for the first nine months of 2012 and 2011, respectively. The decrease in interest expense on borrowings was driven mainly by maturities related to outstanding long-term FHLB advances.

The net interest margin on a taxable equivalent basis was 3.16% for the first nine months of 2012, up two basis points compared to 3.14% for the first nine months of 2011. The spread between the average rate earned on earning assets and the average rate paid on interest bearing liabilities was 2.94% and 2.90% for the first nine months of 2012 and 2011, respectively. The increase in spread was driven by a 32 basis point decrease in the overall cost of funds, which offset a 28 basis point decline in the overall yield on earning assets. The Company expects its net interest margin to trend upward in the near term according to internal modeling using expectations about future market interest rates, the maturity structure of the Company's earning assets and liabilities, and other factors. In particular, the Company's cost of funds is expected to decrease in the near term primarily from the maturity of $50.0 million of 3.98% fixed rate FHLB borrowings combined with $23.2 million of 6.60% fixed rate borrowings that reprice downward to a floating interest rate of three-month LIBOR plus 132 basis points. Each of these events occur during the fourth quarter of 2012. Future results could be significantly different than expectations.

The following tables present an analysis of net interest income for the nine months ended September 30.

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

Nine Months Ended September 30,	2012			2011		
(In thousands)	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
Earning Assets						
Investment securities						
Taxable	$542,536	$10,044	2.47 %	$475,951	$11,022	3.10 %
Nontaxable1	86,828	2,444	3.76	62,389	2,139	4.58
Interest bearing deposits in banks, federal funds sold and securities purchased under agreements to resell	59,500	102	.23	111,883	191	.23
Loans1,2,3	1,044,271	42,849	5.48	1,145,584	47,771	5.58
Total earning assets	1,733,135	$55,439	4.27 %	1,795,807	$61,123	4.55 %
Allowance for loan losses	(27,400)			(29,429)		
Total earning assets, net of allowance for loan losses	1,705,735			1,766,378		
Nonearning Assets						
Cash and due from banks	24,814			18,010		
Premises and equipment, net	37,968			39,402		
Other assets	127,658			125,293		
Total assets	$1,896,175			$1,949,083		
Interest Bearing Liabilities						
Deposits						
Interest bearing demand	$279,357	$183	.09 %	$257,860	$275	.14 %
Savings	308,452	466	.20	291,667	1,007	.46
Time	601,147	6,671	1.48	696,094	9,990	1.92
Federal funds purchased and other short-term borrowings	26,010	74	.38	41,217	154	.50
Securities sold under agreements to repurchase and other long-erm borrowings	230,556	7,040	4.08	246,959	7,493	4.06
Total interest bearing liabilities	1,445,522	$14,434	1.33 %	1,533,797	$18,919	1.65 %
Noninterest Bearing Liabilities						
Other demand deposits	232,474			213,769		
Other liabilities	55,038			47,649		
Total liabilities	1,733,034			1,795,215		
Shareholders' equity	163,141			153,868		
Total liabilities and shareholders' equity	$1,896,175			$1,949,083		
Net interest income		41,005			42,204	
TE basis adjustment		(1,364)			(1,329)	
Net interest income		$39,641			$40,875	
Net interest spread			2.94 %			2.90 %
Impact of noninterest bearing sources of funds			.22			.24

Net interest margin	3.16	%	3.14	%

1Income and yield stated at a fully tax equivalent basis using the marginal corporate Federal tax rate of 35%.
2Loan balances include principal balances on nonaccrual loans.
3Loan fees included in interest income amounted to $931 thousand and $655 thousand in 2012 and 2011, respectively.

Analysis of Changes in Net Interest Income (tax equivalent basis)

(In thousands)	Variance	Variance Attributed to	
Nine Months Ended September 30,	2012/2011 1	Volume	Rate
Interest Income			
Taxable investment securities	$ (978)	$ 2,046	$ (3,024)
Nontaxable investment securities2	305	912	(607)
Interest bearing deposits in banks, federal funds sold and securities purchased under agreements to resell	(89)	(89)	-
Loans2	(4,922)	(4,092)	(830)
Total interest income	(5,684)	(1,223)	(4,461)
Interest Expense			
Interest bearing demand deposits	(92)	31	(123)
Savings deposits	(541)	90	(631)
Time deposits	(3,319)	(1,238)	(2,081)
Federal funds purchased and other short-term borrowings	(80)	(49)	(31)
Securities sold under agreements to repurchase and other long-term borrowings	(453)	(513)	60
Total interest expense	(4,485)	(1,679)	(2,806)
Net interest income	$ (1,199)	$ 456	$ (1,655)
Percentage change	100.0 %	(38.0)%	138.0 %

1The changes that are not solely due to rate or volume are allocated on a percentage basis using the absolute values of rate and volume variances as a basis for allocation.
2Income stated at fully tax equivalent basis using the marginal corporate Federal tax rate of 35%.

Provision for Loan Losses

The provision for loan losses for the first nine months of 2012 was $2.1 million, a decrease of $8.1 million or 79.8% compared to $10.2 million for the first nine months of 2011. The allowance for loan losses as a percentage of outstanding loans (net of unearned income) was 2.47% at September 30, 2012 compared to 2.64% and 2.80% at year-end 2011 and September 30, 2011, respectively. The decrease in the provision for loan losses is attributed to an overall improvement in the credit quality of the loan portfolio and a decrease in loan balances outstanding. For further information about improvements in the Company's overall credit quality, please refer to the discussion under the captions "Allowance for Loan Losses" and "Nonperforming Loans" in this Form 10-Q that follows.

Net charge-offs were $5.2 million for the current nine months, a decrease of $2.9 million or 36.1% when compared to the first nine months of 2011. Net charge-offs for 2012 include $2.6 million related to eight larger-balance credits. Four of these credits secured by real estate development projects had charge-offs totaling $1.2 million, three credits secured by commercial real estate had charge-offs of $940 thousand, and one credit secured by multi-family residential real estate with a charge-off of $405 thousand. On an annualized basis, net charge-offs were .66% of average loans outstanding for the nine months ended September 30, 2012 compared to .95% for the first nine months of 2011.

Noninterest Income

The components of noninterest income are as follows for the periods indicated:

Nine Months Ended September 30, (In thousands)	2012	2011	Change
Service charges and fees on deposits	$ 6,080	$ 6,481	$ (401)
Allotment processing fees	3,932	4,027	(95)
Other service charges, commissions, and fees	3,332	3,146	186
Data processing income	215	691	(476)
Trust income	1,404	1,593	(189)
Investment securities gains, net	964	1,209	(245)
Gain on sale of mortgage loans, net	1,364	620	744
Income from company-owned life insurance	1,289	706	583
Other	26	20	6
Total noninterest income	$ 18,606	$ 18,493	$ 113

The more significant items for discussion are included below.

- The $401 thousand or 6.2% decrease in service charges and fees on deposits was driven by a decline in fees from overdraft/insufficient funds of $582 thousand or 14.0% related to lower transaction volume. Transaction volume has declined similar to trends experienced throughout the banking industry mainly as a result of increased consumer compliance regulations and changes in customer behavior that have evolved over the last several years.
- Other service charges, commissions, and fees are up $186 thousand or 5.9% due to an assortment of relatively small increases within this line item category.
- The decrease in data processing income of $476 thousand or 68.9% is driven by a $337 thousand or 70.6% decline in fees related to the winding down of the depository services contract with the Commonwealth, which have been partially offset by noninterest expense reductions spread over multiple line items categories. Data processing fees have also declined $138 thousand or 97.0% due to lower processing volumes as a result of an increase in paperless payment transactions related to the Commonwealth's WIC supplemental nutrition program. Such transactions are now being processed by an unrelated third party. The Company expects to continue processing only a small number of transactions that are subject to manual processing.
- The $189 thousand or 11.9% decrease in trust income is due mainly to accrual refinements in the prior-year second quarter that resulted in a one-time increase in the amount of $165 thousand.
- The $245 thousand or 20.3% decrease in the gain on the sale of investment securities is attributed to the volume, timing, and market value of the individual securities sold. The sale of investment securities take place at irregular intervals based on current asset and liability management strategies and market conditions. The Company periodically sells investment securities to lock in gains, increase yield, restructure expected future cash flows, and/or enhance its capital position as opportunities occur.
- Net gains on the sale of mortgage loans increased $744 thousand or 120% as the volume of loans sold increased $35.0 million or 147%. The increase in loans sold has been boosted by the overall low interest rate environment. The interest rate environment during 2012 has declined beyond the already low levels that existed during 2011, which has spurred home refinancing and purchasing activity.
- The $583 thousand or 82.6% increase in income from company-owned life insurance is mainly the result of a $529 thousand gain related to death benefit proceeds received in the current year. There was no similar transaction in the comparable period of 2011.

Noninterest Expense

The components of noninterest expense are as follows for the periods indicated:

Nine Months Ended September 30, (In thousands)	2012	2011	Change
Salaries and employee benefits	$ 20,999	$ 20,281	$ 718
Occupancy expenses, net	3,606	3,696	(90)
Equipment expenses	1,757	1,836	(79)
Data processing and communication expense	3,211	3,574	(363)
Bank franchise tax	1,793	1,930	(137)
Amortization of intangibles	761	858	(97)
Deposit insurance expense	2,039	2,254	(215)
Other real estate expenses, net	3,197	6,184	(2,987)
Legal expenses	989	581	408
Other	5,989	6,554	(565)
Total noninterest expense	$ 44,341	$ 47,748	$ (3,407)

The more significant items for discussion are included below.

- The $718 thousand or 3.5% increase in salaries and employee benefits was driven mainly by an increase in higher-salaried personnel in the credit administration and nonperforming asset management positions and modest annual employee pay increases.
- Data processing and communications expenses decreased $363 thousand or 10.2% mainly as a result of an agreement the Company announced during the first quarter of 2012 to reduce its debit card processing expenses combined with costs savings related to the winding down of the Company’s depository services contract with the Commonwealth.
- Bank franchise tax expense is down $137 thousand or 7.1% due to a lower taxable base at certain of the Company’s bank subsidiaries.
- Deposit insurance expense decreased $215 thousand or 9.5% mainly as a result of the change in the FDIC’s assessment base and rate structure that went into effect during the second quarter of 2011. Under the revised rules, the assessment base was changed from a deposit based approach to average assets less average tangible equity during the assessment period. The new assessment methodology generally shifts a greater share of total assessments to banks with more than $10 billion in assets, resulting in a lower amount attributed to many smaller community banks.
- The $3.0 million or 48.3% decrease in other real estate expense was driven by lower impairment charges of $2.8 million or 55.7%. Other real estate expense in the prior year includes an impairment charge of $2.8 million attributed to a single real estate development project that was written down to its fair value of $1.9 million.
- Legal expenses increased $408 thousand or 70.2% due primarily to issues involving problem loans in the normal course of business. The increase in legal expense also includes $122 thousand related to registering the Company’s Series A preferred shares for their sale by the Treasury to third party investors during the second quarter of 2012.
- Other expenses decreased $565 thousand or 8.6% in the nine month comparison due mainly to a $700 thousand deposit fraud loss recorded in 2011. The loss relates to a fraudulent transaction on a deposit account involving one of the Company’s customers that occurred during the first quarter of 2011. No comparable transaction occurred in 2012. The $700 thousand decrease related to the fraud loss was partially offset by a $260 thousand write-down to fair value of a property that was reclassified from bank premises to other real estate. The property was reclassified and written down to fair value after it was determined that the property would no longer be used for future banking purposes.

Income Taxes

Income tax expense was $2.3 million for the first nine months of 2012, resulting in an effective income tax rate of 19.4%. The Company recorded an income tax benefit of $67 thousand for the same period of 2011. The effective income tax rate for that period is not meaningful. Income derived from tax exempt sources continues to be a substantial amount which resulted in a tax benefit in the comparable period.

As has been previously disclosed, the Company accrued an additional $449 thousand of income tax expense in the first quarter of 2011 after learning that one of its tax-exempt customers had received notification that the Internal Revenue Service intended to issue an adverse ruling to the customer regarding the qualified status of their debt arrangement with the Company. The loan contract contains provisions that the customer will indemnify the Company for any penalties, taxes, or interest thereon for which the Company becomes liable as a result of a determination of taxability. The Company intends to exercise its rights under the contract; however, due to the contingent nature of the indemnification provisions, the Company will not record the effects of the indemnification until it is realized. Due to the running of the statute of limitations, $131 thousand and $151 thousand of the original accrual was reversed during the third quarter of 2012 and 2011, respectively.

FINANCIAL CONDITION

Total assets were $1.9 billion at September 30, 2012, a decrease of $28.6 million or 1.5% from year-end 2011. The net decrease in total assets is attributed mainly to a decline in net loans of $50.7 million or 4.9%. The decrease in net loans was partially offset by an increase in cash and cash equivalents and other real estate owned of $15.9 million or 16.9% and $9.3 million or 24.4%, respectively.

The decrease in net loans reflects the lack of high quality loan demand sought by the Company as it continues a cautious and measured approach to new lending while working to reduce its high level of nonperforming assets. This has resulted in principal repayments on existing loans or loans transferred into other real estate through foreclosure that has exceeded new loans. Cash and cash equivalents have increased in preparation of the Company repaying $50.0 million of outstanding borrowings scheduled to mature in the fourth quarter related to the balance sheet leverage transaction that was initiated during 2007. The increase in other real estate owned was driven by the repossession of four properties totaling $8.8 million during the third quarter of 2012.

Total liabilities were $1.7 billion at September 30, 2012, a decrease of $40.2 million or 2.3% compared to December 31, 2011. Total deposits decreased $31.1 million or 2.2% in the comparison. Interest bearing deposits decreased $55.6 million or 4.6%, partially offset by an increase in noninterest bearing deposits of $24.6 million or 11.0%. Long-term borrowings decreased $10.3 million or 4.3% due to principal repayments related to scheduled maturities of FHLB borrowings.

Shareholders’ equity was $169 million at September 30, 2012 compared to $157 million at year-end 2011. This represents an increase of $11.6 million or 7.4% from year-end 2011. The increase in shareholders’ equity is due mainly to net income of $9.5 million in the current period and a $2.9 million increase in unrealized gains on the investment securities included in other comprehensive income.

Temporary Investments

Temporary investments consist of interest bearing deposits in other banks and federal funds sold and securities purchased under agreements to resell. The Company uses these funds in the management of liquidity and interest rate sensitivity or as a short-term holding prior to subsequent movement into other investments with higher yields or for other purposes. At September 30, 2012, temporary investments were $82.2 million, an increase of $16.7 million or 25.5% compared to $65.5 million at year-end 2011. Temporary investments have been boosted as the Company has reinvested some of the cash inflows from securities transactions into interest bearing deposits in preparation for repaying $50.0 million of outstanding borrowings scheduled to mature during the fourth quarter related to the balance sheet leverage transaction that took place during 2007.

Investment Securities

The investment securities portfolio is comprised primarily of residential mortgage-backed securities, U.S. government-sponsored agency securities, and tax-exempt securities of states and political subdivisions. Substantially all of the Company's investment securities are designated as available for sale. Total investment securities were $601 million at September 30, 2012, an increase of $2.7 million or .5% compared to $599 million at year-end 2011. Investment securities have remained relatively flat when compared to year-end 2011, but have decreased $16.3 million or 2.6% from the previous quarter end. The Company has reinvested some of the cash inflows from securities transaction during the current quarter into temporary investments in order to position itself to repay $50.0 million in borrowings that mature during the fourth quarter.

The net amortized cost amount of investment securities decreased $1.8 million or .3% compared to year-end 2011 and the net unrealized gain related to investments in the available for sale portfolio increased $4.5 million or 32.7%. During the first nine months of 2012, the Company purchased $271 million of available for sale investment securities, which was offset by amounts sold, matured, and called of $125 million, $15.5 million, and $129 million, respectively. The increase in the net unrealized gain was driven by a downward movement in longer-term market interest rates. As market interest rates decrease, the value of fixed rate investments generally increases.

At September 30, 2012, the Company held $5.8 million amortized cost amounts of single-issuer trust preferred capital securities of a global and national financial services firm with an estimated fair value of $4.5 million. These securities had an estimated fair value of $4.3 million at June 30, 2012 and year-end 2011. The unrealized loss related to this investment improved by $238 thousand or 15.5% from year-end 2011, including an improvement of $203 thousand or 13.5% during the third quarter of 2012.

The Company's investment in the trust preferred capital securities continue to perform according to contractual terms and, although downgraded during the second quarter of 2012, the securities continue to be rated as investment grade by major rating agencies. The issuer announced in the first quarter of 2012 that it had passed stringent regulatory stress testing as well as receiving regulatory approval to both increase per share common dividend payments and initiate a new equity repurchase program. The Company does not intend to sell these securities nor does the Company believe it is likely that it will be required to sell these securities prior to their anticipated recovery. The Company believes these securities are not impaired due to reasons of credit quality or other factors, but rather the unrealized loss is primarily attributed to general uncertainties in the financial markets and market volatility. The Company believes that it will be able to collect all amounts due according to the contractual terms of these securities and that the fair values of these securities will continue to recover as they approach their maturity dates.

Loans

Loans, net of unearned income, were $1.0 billion at September 30, 2012, a decrease of $53.8 million or 5.0% compared to year-end 2011. The Company continues to take a measured and cautious approach to loan originations by strengthening its overall credit culture and by maintaining tight underwriting standards. The Company seeks higher quality loan demand while working to reduce its elevated levels of nonperforming assets in a sluggish economy that has been slow to recover from one of the most severe recession in recent history. Nonperforming assets increased sharply in the fourth quarter of 2009 and into the first quarter of 2010 as a result of the lingering effects of the economic downturn. While nonperforming assets have declined from their peak, they remain elevated.

The composition of the loan portfolio, net of unearned income, is summarized in the table below.

	September 30, 2012		December 31, 2011	
(Dollars in thousands)	Amount	%	Amount	%
Commercial, financial, and agriculture	$ 89,973	8.8 %	$ 93,807	8.7 %
Real estate – construction and land development	115,324	11.3	119,989	11.2
Real estate mortgage - residential	413,284	40.6	445,464	41.6
Real estate mortgage - farmland and other commercial enterprises	377,696	37.1	384,331	35.8
Installment	18,685	1.9	21,365	2.0
Lease financing	3,349	.3	7,152	.7
Total	$ 1,018,311	100.0 %	$ 1,072,108	100.0 %

On average, loans represented 60.3% of earning assets for the current nine month period, a decrease of 273 basis points compared to 63.0% for year-end 2011. Average loans represent a lower percentage of earning assets as outstanding loan balances have declined and funds are reinvested in other earning assets or used for other purposes. As loan demand fluctuates, available funds are typically reallocated between loans and temporary investments or investment securities, which typically involve a decrease in credit risk and lower yields. Investment securities make up a larger percentage of average earning assets at September 30, 2012 compared to year-end 2011.

The Company does not have direct exposure to the subprime mortgage market. The Company does not originate subprime mortgages nor has it invested in bonds that are secured by such mortgages. Subprime mortgage lending is defined by the Company generally as lending to a borrower that would not qualify for a mortgage loan at prevailing market rates or whereby the underwriting decision is based on limited or no documentation of the ability to repay.

Allowance for Loan Losses

The allowance for loan losses is maintained at a level believed to be adequate by management to cover probable losses in the loan portfolio. The calculation of the appropriate level of allowance for loan losses requires significant judgment to reflect the credit losses specifically identified in the Company's loan portfolio as well as management's best estimate of probable incurred credit losses in the loan portfolio at the balance sheet date. The allowance for loan losses is a valuation allowance increased by the provision for loan losses and decreased by net charge-offs. Loan losses are charged against the allowance when management believes the uncollectibility of a loan is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses and related provision for loan losses generally fluctuate as the relative level of nonperforming and impaired loans vary. However, other factors impact the amount of the allowance for loan losses such as the Company's historical loss experience, the borrowers' financial condition, general economic conditions, and other risk factors as described in the Company's most recent annual report on Form 10-K and Note 2 to the unaudited consolidated financial statements of this Form 10-Q.

The allowance for loan losses was $25.1 million or 2.47% of outstanding loans (net of unearned income) at September 30, 2012. This compares to $28.3 million or 2.64% of net loans outstanding at year-end 2011. The decrease in the allowance for loan losses as a percentage of net loans from year-end 2011 is the result of net charge-offs that exceed the provision for loan losses by $3.1 million combined with a $53.8 million or 5.0% decrease in loans outstanding (net of unearned income). As a percentage of nonaccrual and total nonperforming loans, the allowance for loan losses was 58.3% and 36.1% at September 30, 2012, respectively. At year-end 2011, the allowance was 47.3% of nonaccrual loans and 35.8% of total nonperforming loans.

The decrease in the allowance for loan losses from year-end 2011 is mainly a result of improving credit quality, including a lower level of nonperforming and substandard loans and early stage delinquencies. Historical loss rates and adjustments for current risk factors have also improved. Nonperforming loans have declined to $69.6 million or 6.8% of net loans outstanding at September 30, 2012. This compares to $78.9 million or 7.4% of net loans and $89.1 million or 8.1% of net loans at December 31, 2011 and September 30, 2011, respectively. Loans graded substandard or below were $113 million or 11.1% of the loan portfolio at September 30, 2012 compared to $156 million or 14.5% of the loan portfolio at December 31, 2011 and $169 million or 15.4% at September 30, 2011. Loans identified as impaired have declined as well, totaling $79.2 million, $138 million, and $151 million at September 30, 2012, December 31, 2011, and September 30, 2011, respectively. The decrease in the level of impaired loans in the comparison is due both to an improvement in credit quality along with a policy change by the Company regarding how it identifies impaired loans. Loans previously considered impaired in the amount of $28.0 million were no longer considered impaired during the first quarter of 2012 as a result of the policy change. See Note 2 to the unaudited consolidated financial statements of this Form 10-Q for further detail regarding the policy change related to impaired loans.

Loans past due 30-89 days and still accruing improved to $2.7 million at September 30, 2012 compared to $5.8 million and $3.4 million at year-end 2011 and September 30, 2011, respectively. Historical loss rates have improved as a result of lower recent charge-off activity that has replaced the higher levels that spiked upward during 2009 and are beginning to roll out of the Company's twelve-quarter look-back period. The improvement to current risk factors, which are adjustments to the historical loss rates used in the determination of the allowance for loan losses, resulted primarily from a refinement to the Company's allowance for loan losses methodology that occurred during the first quarter of 2012. The Company, with assistance from an independent third party advisor, adopted revisions to its methodology primarily in order to better reflect the impact of qualitative factors used in estimating credit losses inherent in the general component of the allowance for loan losses. Prior to being formally adopted, the Company tested the updated methodology with live data over a period of several months to ensure that significant changes in the allowance were supported and directionally consistent with changes in overall credit quality and that significant fluctuations were explainable and supportable. For additional detail related to the revised methodology, please refer to Note 2 to the unaudited consolidated financial statements of this Form 10-Q.

Nonperforming Loans

Nonperforming loans consist of nonaccrual loans, accruing restructured loans, and loans 90 days or more past due and still accruing interest. The accrual of interest on loans is discontinued when it is determined that the collection of interest or principal is doubtful, or when a default of interest or principal has existed for 90 days or more, unless such loan is well secured and in the process of collection. Restructured loans occur when a lender, because of economic or legal reasons related to a borrower’s financial difficulty, grants a concession to the borrower that it would not otherwise consider. Restructured loans typically include a reduction of the stated interest rate or an extension of the maturity date, among other possible concessions. The Company gives careful consideration to identifying which of its challenged credits merit a restructuring of terms that it believes will result in maximum loan repayments and mitigate possible losses. Cash flow projections are carefully scrutinized prior to restructuring any credits; past due credits are typically not granted concessions.

Nonperforming loans were $69.6 million at September 30, 2012, a decrease of $9.3 million or 11.7% compared to $78.9 million at year-end 2011. While nonperforming loan totals have improved, the high level that still exists is a result of the ongoing weaknesses in the overall economy that continues to strain the Company and many of its customers. Nonperforming loans at September 30, 2012 and December 31, 2011, presented by loan class, are summarized in the table that follows.

Nonperforming Loans

(In thousands)	September 30, 2012	December 31, 2011
Nonaccrual Loans		
Real Estate:		
Real estate-construction and land development	$ 16,652	$ 30,744
Real estate mortgage-residential	8,891	14,578
Real estate mortgage-farmland and other commercial enterprises	16,778	13,831
Commercial:		
Commercial and industrial	645	386
Lease financing	162	124
Consumer:		
Secured	21	80
Unsecured	1	12
Total nonaccrual loans	$ 43,150	$ 59,755
Restructured Loans		
Real Estate:		
Real estate-construction and land development	$ 8,736	$ 6,207
Real estate mortgage-residential	717	4,894
Real estate mortgage-farmland and other commercial enterprises	16,996	8,024
Total restructured loans	$ 26,449	$ 19,125
Past Due 90 Days or More and Still Accruing		
Real Estate:		
Real estate-construction and land development	$ 28	$ -
Consumer:		
Unsecured	-	1
Total past due 90 days or more and still accruing	$ 28	$ 1
Total nonperforming loans	$ 69,627	$ 78,881
Ratio of total nonperforming loans to total loans (net of unearned income)	6.8 %	7.4 %

Nonaccrual loans make up the largest component of nonperforming assets. Nonaccrual loans were $43.2 million at September 30, 2012, a decrease of $16.6 million or 27.8% compared to $59.8 million at year-end 2011. While there were $16.2 million of newly classified nonaccrual loans during the first nine months of 2012, this amount was offset by a combination of $20.1 million transferred to other real estate owned through foreclosure, principal paydowns of $7.7 million, charge-offs of $4.5 million, and $528 thousand reclassified to performing status. Restructured loans increased $7.3 million or 38.3% since year-end 2011, driven by the addition of a previously identified impaired, but accruing, single commercial real estate credit in the amount of $9.1 million.

The Company's comprehensive risk-grading and loan review program includes a review of loans to assess risk and assign a grade to those loans, a review of delinquencies, and an assessment of loans for needed charge-offs or placement on nonaccrual status. The Company had loans in the amount of $110 million and $125 million at September 30, 2012 and year-end 2011, respectively, which were performing but considered potential problem loans and are not included in the nonperforming loan totals in the table above. These loans, however, are considered in establishing an appropriate allowance for loan losses. The balance outstanding for potential problem credits is mainly a result of ongoing weaknesses in the overall economy that continue to strain the Company and many of its customers. Potential problem loans include a variety of borrowers and are secured primarily by real estate. At September 30, 2012, the five largest potential problem credits were $22.7 million in the aggregate compared to $33.6 million at year-end 2011 and secured by various types of real estate including commercial, construction properties, and residential real estate development.

Potential problem loans are identified on the Company's watch list and consist of loans that require close monitoring by management. Credits may be considered as a potential problem loan for reasons that are temporary or correctable, such as for a deficiency in loan documentation or absence of current financial statements of the borrower. Potential problem loans may also include credits where adverse circumstances are identified that may affect the borrower's ability to comply with the contractual terms of the loan. Other factors which might indicate the existence of a potential problem loan include the delinquency of a scheduled loan payment, deterioration in a borrower's financial condition identified in a review of periodic financial statements, a decrease in the value of the collateral securing the loan, or a change in the economic environment in which the borrower operates. Certain potential problem loans on the Company's watch list are also considered impaired and specific allowances related to these loans were established in accordance with the appropriate accounting guidance.

Other Real Estate

Other real estate owned ("OREO") includes real estate properties acquired by the Company through foreclosure. At September 30, 2012, OREO was $47.5 million, an increase of $9.3 million or 24.4% compared to $38.2 million at year-end 2011. The overall increase in other real estate owned was driven mainly by the Company receiving possession of properties previously securing real estate loans totaling $21.9 million, primarily reclassified from nonaccrual loans. The Company sold repossessed properties with a carrying amount of $10.4 million during the period and recorded impairment charges in the amount of $2.2 million to write down certain properties to their estimated fair value.

Deposits

A summary of the Company's deposits are as follows for the periods indicated.

	End of Period			Average		
(In thousands)	September 30, 2012	December 31, 2011	Difference	(Nine Months) September 30, 2012	(Twelve Months) December 31, 2011	Difference
Noninterest Bearing	$ 248,822	$ 224,259	$ 24,563	$ 232,474	$ 217,357	$ 15,117
Interest Bearing						
Demand	275,428	261,920	13,508	279,357	258,244	21,113
Savings	316,592	301,217	15,375	308,452	293,526	14,926
Time	563,149	647,669	(84,520)	601,147	687,517	(86,370)
Total interest bearing	1,155,169	1,210,806	(55,637)	1,188,956	1,239,287	(50,331)
Total Deposits	$ 1,403,991	$ 1,435,065	$ (31,074)	$ 1,421,430	$ 1,456,644	$ (35,214)

The decrease in end of period deposits compared with the prior year-end was driven by lower time deposits of $84.5 million or 13.0%, which offset higher balances outstanding of $24.6 million, $13.5 million, and $15.4 million for noninterest bearing demand, interest bearing demand, and savings accounts, respectively. The decrease in time deposits is a result of the Company's overall liquidity position, which correlates with a strategy to lower its cost of funds mainly by allowing higher-rate certificates of deposit to roll off or reprice at significantly lower interest rates. Many of those balances have been rolled into either interest bearing or noninterest bearing demand accounts by the customer. As rates have decreased throughout the deposit portfolio, many customers have opted to transfer funds from maturing time deposits or investments from other sources into short-term demand or savings accounts.

Borrowed Funds

Total borrowed funds were $255 million at September 30, 2012, a decrease of $11.6 million or 4.3% from $267 million at year-end 2011. Long-term borrowings were $229 million at September 30, 2012, a decrease of $10.3 million or 4.3% from year-end due to principal repayments related to scheduled maturities of FHLB borrowings. Short-term borrowings totaled $25.7 million, a decrease of $1.3 million or 4.7% from year-end. Short-term borrowings primarily represent repurchase agreements entered into with commercial depositors and, to a lesser extent, federal funds purchased through relationships with downstream correspondent banks.

LIQUIDITY

The primary source of funds for the Parent Company is the receipt of dividends and management fees from its subsidiaries, cash balances maintained, temporary investments, and the ability to borrow from nonaffiliated sources. Payment of dividends by the Company's subsidiary banks is subject to certain regulatory restrictions as set forth in national and state banking laws and regulations. In addition, Farmers Bank & Capital Trust Company ("Farmers Bank"), United Bank & Trust Company ("United Bank"), and Citizens Bank of Northern Kentucky, Inc. ("Citizens Northern") each must obtain regulatory approval to declare or pay dividends to the Parent Company as a result of increased capital required in connection with prior regulatory exams. Farmers Bank received regulatory approval for the payment of a dividend to the Parent Company during the third quarter of 2012. The dividend payment by Farmers Bank represents the first such payment made since it entered into the agreement with its regulators during 2009. Capital ratios at each of the Company's four subsidiary banks exceed regulatory established "well-capitalized" status at September 30, 2012 under the prompt corrective action regulatory framework; however, Farmers Bank, United Bank, and Citizens Northern are required to maintain capital ratios at higher levels as outlined in their regulatory agreements. The capital ratios at each of these three banks exceed the higher amounts required under their respective regulatory agreement. Capital ratios for the Company and its subsidiary banks are summarized in tabular format under the caption "Capital Resources" that follows.

The Parent Company's primary uses of cash include the payment of dividends to its preferred and common shareholders, injecting capital into subsidiaries, paying interest expense on borrowings, and paying for general operating expenses. Due to an agreement with its regulators, the Parent Company must obtain regulatory approval prior to making dividend payments on its preferred and common stock and interest payments on its trust preferred borrowings. While regulatory agencies have so far granted approval to all of the Company's requests to make dividend payments on its preferred stock and interest payments on its trust preferred securities, the Company has not (based on the assessment by Company management of both the Company's capital position and the earnings of its subsidiaries) sought regulatory approval to pay any common stock dividends since the fourth quarter of 2009. Moreover, the Company will not pay any such dividend on its common stock in any subsequent quarter until the regulator's assessment of the earnings of the Company's subsidiaries, and the Company's assessment of its capital position, both yield the conclusion that the payment of a Company common stock dividend is warranted.

The Parent Company had cash balances of $25.7 million at September 30, 2012, an increase of $7.3 million or 39.9% from $18.4 million at year-end 2011. Significant cash receipts of the Parent Company during 2012 include dividends from subsidiaries in the amount of $12.0 million, management fees from subsidiaries of $2.6 million, and a $500 thousand return of capital from its data processing subsidiary, FCB Services, Inc. Dividends from subsidiaries include $6.0 million received from First Citizens Bank ("First Citizens"), $4.0 million received from Farmers Bank, and $2.0 million from FFKT Insurance Services Inc. The dividend payment by Farmers Bank, which required regulatory approval, is the first such payment made since entering into an agreement with its regulators during 2009. Significant cash payments by the Parent Company during 2012 include an additional capital investment in United Bank of $2.5 million, salaries, payroll taxes, and employee benefits of $1.8 million, interest on borrowed funds of $1.4 million, and the payment of dividends on preferred stock of $1.1 million.

The Company's objective as it relates to liquidity is to ensure that its subsidiary banks have funds available to meet deposit withdrawals and credit demands without unduly penalizing profitability. In order to maintain a proper level of liquidity, the subsidiary banks have several sources of funds available on a daily basis that can be used for liquidity purposes. For assets, those sources primarily include cash and due from banks, federal funds sold, and cash flow generated by the repayment of principal and interest on loans and investment securities. They also include liquid assets that are readily marketable or that can be pledged, or which mature in the near future. For liabilities, sources of funds primarily include the subsidiary banks' core deposits, FHLB and other borrowings, and federal funds purchased and securities sold under agreements to repurchase. While maturities and scheduled amortization of loans and investment securities are generally a predictable source of funds, deposit outflows and mortgage prepayments are influenced significantly by general interest rates, economic conditions, and competition in our local markets.

As of September 30, 2012, the Company had $212 million of additional borrowing capacity under various FHLB, federal funds, and other borrowing agreements. However, there is no guarantee that these sources of funds will continue to be available to the Company, or that current borrowings can be refinanced upon maturity, although the Company is not aware of any events or uncertainties that are likely to cause a decrease in the Company's liquidity from these sources. The Company's borrowing capacity increased $25.0 million or 13.4% since year-end 2011 primarily as a result of additional borrowings available from the FHLB. This additional borrowing capacity resulted from improving credit metrics at one of the Company's subsidiary banks. As such, the FHLB in the first quarter of 2012 updated the collateral pledging method of the subsidiary bank to blanket lien status from possession (delivery) status. Blanket lien status is the least restrictive collateral arrangement used by the FHLB. This status is generally assigned to lower risk institutions that pledge loan collateral related to their borrowings.

For the longer term, the Company's liquidity position is managed by balancing the maturity structure of the balance sheet. This process allows for an orderly flow of funds over an extended period of time. The Company's Asset and Liability Management Committee, both at the bank subsidiary level and on a consolidated basis, meets regularly and monitors the composition of the balance sheet to ensure comprehensive management of interest rate risk and liquidity.

Liquid assets consist of cash, cash equivalents, and available for sale investment securities. At September 30, 2012, consolidated liquid assets were $711 million, an increase of $18.6 million or 2.7% from year-end 2011. The increase in liquid assets is comprised of higher cash and cash equivalents of $15.9 million or 16.9% and higher available for sale investment securities of $2.7 million or .5%. Liquid assets remain elevated mainly as a result of the Company's overall net funding position, which has been influenced by a strategy that included realigning the balance sheet and reducing its overall size while managing a high level of nonperforming assets. The overall funding position of the Company changes as loan demand, deposit levels, and other sources and uses of funds fluctuate. Liquid assets have also increased as the Company positions itself to repay $50.0 million in outstanding borrowings that mature during the fourth quarter related to the balance sheet leverage transaction initiated during 2007.

Net cash provided by operating activities was $22.4 million for the first nine months of 2012, relatively unchanged compared to $22.2 million for the same period of 2011. Net cash provided by investing activities was $37.3 million for 2012 compared to a net use of cash in 2011 of $61.2 million. The $98.6 million change is mainly related to investment securities and loan activity. For investment securities, the Company had net cash outflows in 2012 of $1.2 million, which represents a decrease of $133 million compared to net cash outflows of $134 million for 2011. Net cash outflows for investment securities represent purchases made during the period, net of proceeds from sales, maturities, and calls. Net purchases of investment securities were significantly higher in the prior year and correlate to a much steeper decrease in loans in 2011 along with investing excess cash into higher yielding investment securities. For loans, the Company had net principal collections of $31.1 million for 2012, a decrease of $35.1 million compared to $66.2 million for 2011. Net principal collections on loans have declined as the pace of net repayment activity between the periods has slowed.

Net cash used in financing activities was $43.8 million and $41.6 million for the first nine months of 2012 and 2011, respectively. This represents an increase of $2.1 million or 5.1%. Net cash used in financing activities increased in the comparison mainly due to deposit activity, which offset the impact related to borrowings. Net cash used related to deposit outflows were $31.1 million for 2012, an increase of $14.6 million compared to $16.5 million for 2011. This was partially offset by an overall decrease in net repayments on borrowed funds of $12.5 million in the comparison.

Commitments to extend credit are entered into with customers in the ordinary course of providing traditional banking services and are considered in addressing the Company's liquidity management. The Company does not expect these commitments to significantly affect the liquidity position in future periods. The Company has not entered into any contracts for financial derivative instruments such as futures, swaps, options, or similar instruments.

CAPITAL RESOURCES

Shareholders' equity was $169 million at September 30, 2012 compared to $157 million at year-end 2011. This represents an increase of $11.6 million or 7.4% and is attributed mainly to net income and other comprehensive income of $9.5 million and $3.2 million, respectively, partially offset by dividends on preferred stock of $1.1 million. Other comprehensive income increased mainly due to a $2.9 million or 32.7% increase in the unrealized gain on available for sale investment securities (net of tax), which was driven by an overall decrease in the market interest rate environment since year-end 2011. As market interest rates decrease, the value of fixed rate investment securities generally increases.

During January of 2009, as part of the Treasury's Capital Purchase Program ("CPP"), the Company issued 30 thousand shares of Series A, no par value cumulative perpetual preferred stock to the Treasury for $30.0 million. The Company also issued a warrant to the Treasury allowing it to purchase 223,992 shares of the Company's common stock at an exercise price of $20.09. The Series A preferred shares pay a cumulative cash dividend quarterly at 5% per annum during the first five years the preferred shares are outstanding and reset to 9% thereafter if not redeemed. The Company's goal is to repurchase the preferred shares either in whole or in part prior to the dividend rate resetting to 9%, using internally generated cash flows for the potential repurchase.

During June 2012, the Treasury auctioned its investment in the Company's Series A preferred stock as part of its effort to wind down its CPP investments. The Treasury was successful in selling all of its investment in the Company's Series A preferred stock to private investors through a registered public offering. The Company received no proceeds as part of the transaction. Since the Treasury no longer owns the preferred stock, the executive compensation and other restrictions put in place by the Treasury are no longer applicable. The Company continues to view the outstanding preferred stock as an important component of its capital structure.

On July 18, 2012, the Company repurchased the warrant issued to the Treasury at a mutually agreed upon price of $75 thousand. The repurchase of the warrant had no impact on the Company's results of operations, although cash and shareholders' equity declined by the amount of the purchase price. The Treasury has no remaining equity stake in the Company.

Although the Parent Company is under no directive by its regulators to raise any additional capital, the Company filed a registration statement on Form S-3 with the SEC that became effective on October 19, 2009. Currently, as part of that filing, equity securities of the Company of approximately one-third of the market value of Company common stock held by non-affiliates (which as of October 31, 2012 one-third of the market value of common stock held by non-affiliates would have equaled approximately $81.4 million) could be offered for sale by the Company in one or more public offerings at an appropriate time. Similarly, the Company could also seek to offer for sale debt or equity securities in a private placement exempt from the registration requirements of the Securities Act of 1933. The Company periodically evaluates potential capital raising scenarios and could seek a securities offering in the future. However, no determination has been made as to if or when a capital raise will be completed. Net proceeds from a potential sale of securities could be used for any corporate purpose determined by the Company's board of directors.

At September 30, 2012, the Company's tangible capital ratio was 9.01%, up 79 basis points compared to 8.22% at year-end 2011. The tangible capital ratio is defined as tangible equity as a percentage of tangible assets and excludes intangible assets. Tangible common equity to tangible assets, which further excludes outstanding preferred stock, was 7.42% at September 30, 2012, an increase of 75 basis points compared to 6.67% at year-end 2011.

Consistent with the objective of operating a sound financial organization, the Company's goal is to maintain capital ratios well above the regulatory minimum requirements. The Company's capital ratios and the regulatory minimums are as follows as of the dates indicated.

	September 30, 2012			December 31, 2011		
	Tier 1 Risk-based Capital1	Total Risk-based Capital1	Tier 1 Leverage2	Tier 1 Risk-based Capital1	Total Risk-based Capital1	Tier 1 Leverage2
Consolidated	17.89 %	19.15 %	10.79 %	16.68 %	17.95 %	9.99 %
Farmers Bank 3	17.70	18.96	9.47	17.58	18.84	9.47
First Citizens	12.61	13.41	8.99	13.47	14.21	8.93
United Bank3	15.32	16.60	9.41	13.51	14.79	8.44

Citizens Northern3	12.84	14.09	9.01	12.24	13.49	8.48
Regulatory minimum	4.00	8.00	4.00	4.00	8.00	4.00
Well-capitalized status	6.00	10.00	5.00	6.00	10.00	5.00

1Tier 1 Risk-based and Total Risk-based Capital ratios are computed by dividing a bank's Tier 1 or Total Capital, as defined by regulation, by a risk-weighted sum of the bank's assets, with the risk weighting determined by general standards established by regulation. The safest assets (e.g., government obligations) are assigned a weighting of 0% with riskier assets receiving higher ratings (e.g., ordinary commercial loans are assigned a weighting of 100%).

2Tier 1 Leverage ratio is computed by dividing a bank's Tier 1 Capital, as defined by regulation, by its total quarterly average assets.

3See Note 10 to the Company's unaudited consolidated financial statements included as part of this Form 10-Q for minimum capital ratios required as part of the bank's regulatory agreement.

Regulatory Agreements

The Parent Company, Farmers Bank, United Bank, and Citizens Northern have each entered into supervisory agreements with their primary banking regulator. These agreements are summarized in Note 10 to the unaudited consolidated financial statements of this Form 10-Q. These agreements are also discussed in significantly greater detail in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 under the caption "Capital Resources" in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

There have been no changes to the regulatory agreements since year-end 2011. The Company believes that it is adequately addressing all issues included in the regulatory agreements. However, only the respective regulatory agencies can determine if compliance with the applicable regulatory agreements have been met. The Company believes it and its subsidiary banks are in compliance with the requirements identified in the regulatory agreements as of September 30, 2012. Regulators continue to monitor the Company's progress and compliance with the agreements through periodic on-site examinations, regular communications, and quarterly data analysis. The results of these examinations and communications show satisfactory progress toward meeting the requirements included in the regulatory agreements.

The Parent Company maintains cash available to fund a certain amount of additional injections of capital to its bank subsidiaries if required by its regulators. If needed, further amounts in excess of available cash may be funded by future public or private sales of securities, although the Parent Company is currently under no directive by its regulators to raise any additional capital.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company uses a simulation model as a tool to monitor and evaluate interest rate risk exposure. The model is designed to measure the sensitivity of net interest income and net income to changing interest rates over future time periods. Forecasting net interest income and its sensitivity to changes in interest rates requires the Company to make assumptions about the volume and characteristics of many attributes, including assumptions relating to the replacement of maturing earning assets and liabilities. Other assumptions include, but are not limited to, projected prepayments, projected new volume, and the predicted relationship between changes in market interest rates and changes in customer account balances. These effects are combined with the Company's estimate of the most likely rate environment to produce a forecast of net interest income and net income. The forecasted results are then adjusted for the effect of a gradual increase and decrease in market interest rates on the Company's net interest income and net income. Because assumptions are inherently uncertain, the model cannot precisely estimate net interest income or net income or the effect of interest rate changes on net interest income and net income. Actual results could differ significantly from simulated results.

At September 30, 2012, the model indicated that if rates were to gradually increase by 75 basis points during the remainder of the calendar year, then net interest income and net income would decrease .01% and increase .13%, respectively for the year ending December 31, 2012 when compared to the forecasted results for the most likely rate environment. The model indicated that if rates were to gradually decrease by 75 basis points over the same period, then net interest income and net income would decrease .11% and .56%, respectively.

In the current relatively low interest rate environment, it is not practical or possible to reduce certain deposit rates by the same magnitude as rates on earning assets. The average rate paid on many of the Company's deposits is below 2%. This situation magnifies the model's predicted results when modeling a decrease in interest rates, as earning assets with higher yields have more of an opportunity to reprice at lower rates than lower-rate deposits.

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Item 4. Controls and Procedures

The Company's Chief Executive Officer and Chief Financial Officer have reviewed and evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this report, and have concluded that the Company's disclosure controls and procedures were adequate and effective to ensure that all material information required to be disclosed in this report has been made known to them in a timely fashion.

The Company's Chief Executive Officer and Chief Financial Officer have also concluded that there were no significant changes during the quarter ended September 30, 2012 in the Company's internal control over financial reporting or in other factors that have materially affected, or are reasonably likely to materially affect, the registrant's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

As of September 30, 2012, there were various pending legal actions and proceedings against the Company arising from the normal course of business and in which claims for damages are asserted. Management, after discussion with legal counsel, believes that these actions are without merit and that the ultimate liability resulting from these legal actions and proceedings, if any, will not have a material effect upon the consolidated financial statements of the Company.

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

At various times, the Company's Board of Directors has authorized the purchase of shares of the Company's outstanding common stock. No stated expiration dates have been established under any of the previous authorizations. There were no Company shares purchased during the quarter ended September 30, 2012. There are 84,971 shares that may still be purchased under the various authorizations. However, the Company must be granted permission by the Federal Reserve Bank of St. Louis and the Kentucky Department of Financial Institutions before it can repurchase or redeem any of its outstanding common or preferred stock as a result of its regulatory agreement.

In January of 2009, the Company issued 30 thousand shares of Series A, no par value cumulative perpetual preferred stock to the Treasury for $30.0 million pursuant to a Letter Agreement and Securities Purchase Agreement. The Company also issued a warrant to the Treasury allowing it to purchase 223,992 shares of its Company's common stock at an exercise price of $20.09. The Series A preferred stock and warrant were issued in a private placement exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended. During June 2012, the Treasury sold its entire investment in the Company's Series A preferred stock to private investors through a registered public offering. On July 18, 2012, the Company repurchased the warrant from the Treasury at a mutually agreed upon amount of $75 thousand. The Treasury has no remaining equity stake in the Company.

Item 6. Exhibits

List of Exhibits

3.1 Second Amended and Restated Articles of Incorporation of Farmers Capital Bank Corporation (incorporated by reference to the Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2006 (File No. 000-14412)).

3.2 Articles of Amendment to Second Amended and Restated Articles of Incorporation of Farmers Capital Bank Corporation dated January 6, 2009 (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).

3.3 Articles of Amendment to Second Amended and Restated Articles of Incorporation of Farmers Capital Bank Corporation dated November 16, 2009 (incorporated by reference to the Current Report on Form 8-K dated November 17, 2009 (File No. 000-14412)).

3.4 Amended and Restated Bylaws of Farmers Capital Bank Corporation (incorporated by reference to the Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2009 (File No. 000-14412)).

4.1* Junior Subordinated Indenture, dated as of July 21, 2005, between Farmers Capital Bank Corporation and Wilmington Trust Company, as Trustee, relating to unsecured junior subordinated deferrable interest notes that mature in 2035.

4.2* Amended and Restated Trust Agreement, dated as of July 21, 2005, among Farmers Capital Bank Corporation, as Depositor, Wilmington Trust Company, as Property and Delaware Trustee, the Administrative Trustees (as named therein), and the Holders (as defined therein).

4.3* Guarantee Agreement, dated as of July 21, 2005, between Farmers Capital Bank Corporation, as Guarantor, and Wilmington Trust Company, as Guarantee Trustee.

4.4* Junior Subordinated Indenture, dated as of July 26, 2005, between Farmers Capital Bank Corporation and Wilmington Trust Company, as Trustee, relating to unsecured junior subordinated deferrable interest notes that mature in 2035.

4.5* Amended and Restated Trust Agreement, dated as of July 26, 2005, among Farmers Capital Bank Corporation, as Depositor, Wilmington Trust Company, as Property and Delaware Trustee, the Administrative Trustees (as named therein), and the Holders (as defined therein).

4.6* Guarantee Agreement, dated as of July 26, 2005, between Farmers Capital Bank Corporation, as Guarantor, and Wilmington Trust Company, as Guarantee Trustee.

4.7* Indenture, dated as of August 14, 2007 between Farmers Capital Bank Corporation, as Issuer, and Wilmington Trust Company, as Trustee, relating to fixed/floating rate junior subordinated debt due 2037.

4.8* Amended and Restated Declaration of Trust, dated as of August 14, 2007, by Farmers Capital Bank Corporation, as Sponsor, Wilmington Trust Company, as Delaware and Institutional Trustee, the Administrative Trustees (as named therein), and the Holders (as defined therein).

4.9*	Guarantee Agreement, dated as of August 14, 2007, between Farmers Capital Bank Corporation, as Guarantor, and Wilmington Trust Company, as Guarantee Trustee.
4.10	Form of Certificate for Fixed Rate Cumulative Perpetual Preferred Stock, Series A (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).
4.11	Articles of Amendment to Second Amended and Restated Articles of Incorporation of Farmers Capital Bank Corporation dated January 6, 2009 (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).

4.12 Warrant for Purchase of Shares of Common Stock, which was repurchased by Farmers Capital Bank Corporation and cancelled on July 18, 2012 (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).

4.13 Letter Agreement, dated January 9, 2009, between Farmers Capital Bank Corporation and the United States Treasury, with respect to the issuance and sale of the Series A preferred stock and the warrant, and Securities Purchase Agreement-Standard Terms attached thereto as Exhibit A (incorporated by reference to the Current Report on Form 8-K dated January 13, 2009 (File No. 000-14412)).

10.1 Employee Stock Purchase Plan of Farmers Capital Bank Corporation (incorporated by reference to Form S-8 effective June 24, 2004 (File No. 333-116801)).

10.2 Nonqualified Stock Option Plan of Farmers Capital Bank Corporation (incorporated by reference to Form S-8 effective September 8, 1998 (File No. 333-63037)).

31.1** CEO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2** CFO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32** CEO & CFO Certifications Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

101*** The following financial information from Farmers Capital Bank Corporation's Quarterly Report on Form 10-Q for the quarter ended September 30, 2012, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income (iv) the Consolidated Statements of Cash Flows, (v) the Consolidated Statements of Changes in Shareholders' Equity, and (vi) the Notes to the Consolidated Financial Statements.

* Exhibit not included pursuant to Item 601(b)(4)(iii) and (v) of Regulation S-K. The Company will provide a copy of such exhibit to the Securities and Exchange Commission upon request.

** Filed with this Quarterly Report on Form 10-Q.

*** As provided in Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 are deemed not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities and Exchange Act of 1934.

SIGNATURES

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

Date:	November 7, 2012	/s/ Lloyd C. Hillard, Jr. Lloyd C. Hillard, Jr. President and CEO (Principal Executive Officer)
Date:	November 7, 2012	/s/ Doug Carpenter C. Douglas Carpenter Executive Vice President, Secretary, and CFO (Principal Financial and Accounting Officer)