EAGLE BANCORP INC
Form 10-K/A
June 25, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A

(Amendment No. 1)

ý **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2007

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

For the transition period from to
Commission file number: 0-25923

Eagle Bancorp, Inc.

(Exact Name of Registrant as Specified in its Charter)

Maryland	**52-2061461**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
7815 Woodmont Avenue, Bethesda, Maryland	**20814**
(Address of Principal Executive Offices)	(Zip Code)

Registrant's Telephone Number, including area code:
(301) 986-1800

Securities registered pursuant to Section 12(b) of the Act:
Common Stock $.01 par value

Securities registered pursuant to Section 12(g) of the Act:
None

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

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

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 ý No o

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

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

Large accelerated filer o	Accelerated filer ý	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

The aggregate market value of the outstanding Common Stock held by nonaffiliates as of June 30, 2007 was approximately $135 million.

EXPLANATORY NOTE

We filed our Annual Report on Form 10-K for the year ended December 31, 2007 on March 14, 2008 (the "Original Report"). We are filing this Amendment No. 1 on Form 10-K/A (this "Amendment") to revise the following:

1. Disclose information required by paragraph 17 of FASB Staff Position Nos. FAS 115-1 and 124-1 related to our available-for-sale securities for each period that a consolidated balance sheet was presented.

2. Provide an expanded discussion of the specific operations of Eagle Commercial Ventures ("ECV").

3. Managements Report on Internal Control Over Financial Reporting contained an inaccurate date reference.

4. Supplementing the executive compensation information contained in the Company's proxy statement for its annual meeting of shareholders held on May 22, 2008, which is incorporated by reference.

5. Exhibits 31.1, 31.2, 31.3 and 31.4 contained inappropriate modifications.

No other changes to the Original Report are included in this Amendment other than the items mentioned above and to provide currently-dated Exhibit Nos. 23, 31.1, 31.2, 31.3, 31.4, 32.1, 32.2, 32.3 and 32.4.

This Amendment is being filed in response to comments we received from the staff of the Division of Corporation Finance of the Securities and Exchange Commission (the "SEC") in connection with the staff's review of the Original Report. We have made no attempt in this Amendment to modify or update the disclosures presented in the Original Report other than as noted above. Also, this Amendment does not reflect events occurring after the filing of the Original Report. Accordingly, this Amendment should be read in conjunction with the Original Report and our other filings with the SEC subsequent to the filing of the Original Report.

As of March 11, 2008, the number of outstanding shares of the Common Stock, $.01 par value, of Eagle Bancorp, Inc. was 9,780,418.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 22, 2008 are incorporated by reference in part III hereof.

Form 10-K Cross Reference Sheet

The following shows the location in this Annual Report on Form 10-K or the Company's Proxy Statement for the Annual Meeting of Stockholders to be held on May 22, 2008, of the information required to be disclosed by the United States Securities and Exchange Commission Form 10-K. References to pages only are to pages in this report.

PART I	**Item 1.**	**Business.** See "Business" at Pages 66 through 70, "Employees" at Page 76, "Market Area and Competition" at Pages 77 through 78 and "Regulation" at Pages 78 through 83.
	Item 1A.	**Risk Factors.** See "Risk Factors" at Pages 70 through 75.
	Item 1B.	**Unresolved Staff Comments.** None.
	Item 2.	**Properties.** See "Properties" at Page 83 through 84.
	Item 3.	**Legal Proceedings.** From time to time the Company is a participant in various legal proceedings incidental to its business. In the opinion of management, the liabilities (if any) resulting from such legal proceedings will not have a material effect on the financial position of the Company.
	Item 4.	**Submission of Matters to a Vote of Security Holders.** No matter was submitted to a vote of the security holders of the Company during the fourth quarter of 2007.
PART II	**Item 5.**	**Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.** See "Market for Common Stock and Dividends" at Pages 32 though 34.
	Item 6.	**Selected Financial Data.** See "Six Year Summary of Financial Information" at Page 3.
	Item 7.	**Management's Discussion and Analysis of Financial Condition and Results of Operation.** See "Management's Discussion and Analysis of Financial Condition and Results of Operation" at Pages 4 through 32.
	Item 7A.	**Quantitative and Qualitative Disclosures About Market Risk.** See "Interest Rate Risk Management Asset/Liability Management and Quantitative and Qualitative Disclosure About Market Risk" at Page 28 through Page 31.
	Item 8.	**Financial Statements and Supplementary Data.** See Consolidated Financial Statements and Notes thereto at Pages 35 through 65.
	Item 9.	**Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.** None.
	Item 9A.	**Controls and Procedures.** See "Disclosure Controls and Procedures" at Page 84 and "Management Report on Internal Control Over Financial Reporting" at Page 85.
	Item 9B.	**Other Information.** None.
PART III	**Item 10.**	**Directors, Executive Officers and Corporate Governance.** The information required by this Item is incorporated by reference to the material appearing under the captions "Election of Directors" and "Compliance with Section 16(a) of the Securities Exchange Act of 1934" in the Proxy Statement. The Company has adopted a code of ethics that applies to its Chief Executive Officer and Chief Financial Officer. A copy of the code of ethics will be provided to any person, without charge, upon written request directed to Zandra Nichols, Corporate Secretary, Eagle Bancorp, Inc., 7815 Woodmont Avenue, Bethesda, Maryland 20814. There have been no material changes in the procedures previously disclosed by which shareholders may recommend nominees to the Company's Board of Directors.
	Item 11.	**Executive Compensation.** The information required by this Item is incorporated by reference to the material appearing under the captions "Election of Directors Director's Compensation" and "Executive Compensation" in the Proxy Statement, and is supplemented by the information under "Item 11" at page 84.
	Item 12.	**Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.** See "Market for Common Stock and Dividends Securities Authorized for Issuance Under Equity Compensation Plans" at page. The remainder of the information required by this Item is incorporated by reference to the material appearing under the caption "Voting Securities and Principal Shareholders" in the Proxy Statement.
	Item 13.	**Certain Relationships and Related Transactions and Director Independence.** The information required by this Item is incorporated by reference to the material appearing under the captions "Election of Directors" and "Certain Relationships and Related Transactions" in the Proxy Statement.
	Item 14.	**Principal Accountant Fees and Services.** The information required by this Item is incorporated by reference to the material appearing under the caption "Independent Registered Public Accounting Firm Fees Paid to Independent Accounting Firm" in the Proxy Statement.
PART IV	**Item 15.**	**Exhibits, Financial Statement Schedules.** See "Exhibits and Financial Statements" at Page 87.

Six Year Summary of Selected Financial Data

The following table shows selected historical consolidated financial data for Eagle Bancorp (the "Company"). It should be read in conjunction with the Company's audited consolidated financial statements appearing elsewhere in this report.

	Year Ended December 31,						
	2007	**2006**	**2005**	**2004**	**2003**	**2002**	**5 Year Compound Growth Rate**
	(dollars in thousands except per share data)						
Selected Balances Period End							
Total assets	$ 846,400	$ 773,451	$ 672,252	$ 553,453	$ 442,997	$ 347,829	19%
Total stockholders' equity	81,166	72,916	64,964	58,534	53,012	20,028	32%
Total loans	716,677	625,773	549,212	415,509	317,533	236,860	25%
Total deposits	630,936	628,515	568,893	462,287	335,514	278,434	18%
Selected Balances Averages							
Total assets	$ 800,437	$ 712,297	$ 610,245	$ 487,853	$ 375,802	$ 292,921	22%
Total stockholders' equity	76,760	68,973	61,563	55,507	34,028	18,381	33%
Total loans	659,204	575,854	479,311	353,537	266,811	210,303	26%
Total deposits	634,332	585,621	512,416	397,788	292,953	237,910	22%
Results of Operations							
Interest income	$ 57,077	$ 50,318	$ 36,726	$ 24,195	$ 18,403	$ 16,661	28%
Interest expense	23,729	17,880	8,008	4,328	3,953	5,170	36%
Net interest income	33,348	32,438	28,718	19,867	14,450	11,491	24%
Provision for credit losses	1,643	1,745	1,843	675	1,175	843	14%
Net interest income after provision for credit losses	31,705	30,693	26,875	19,192	13,275	10,648	24%
Noninterest income	5,186	3,846	3,998	3,753	2,850	2,107	20%
Noninterest expense	24,921	21,824	18,960	14,952	11,007	8,530	24%
Income before taxes	11,970	12,715	11,913	7,993	5,118	4,225	23%
Income tax expense	4,269	4,690	4,369	2,906	1,903	1,558	22%
Net income	7,701	8,025	7,544	5,087	3,215	2,667	24%
Dividends declared	2,302	2,147	1,994				
Per Share Data(1)							
Net income, basic	$ 0.80	$ 0.85	$ 0.82	$ 0.56	$ 0.49	$ 0.54	8%
Net income, diluted	0.78	0.81	0.77	0.53	0.46	0.51	9%
Book value	8.35	7.69	6.95	6.38	5.85	4.09	15%
Dividends declared per share	0.24	0.23	0.22				
Dividend payout ratio(2)	29.89%	27.06%	26.42%				
Financial Ratios							
Return on average assets	0.96%	1.13%	1.24%	1.04%	0.86%	0.91%	
Return on average equity	10.03%	11.63%	12.25%	9.16%	9.45%	14.51%	
Average equity to average assets	9.59%	9.68%	10.09%	11.38%	9.05%	6.28%	
Net interest margin	4.37%	4.81%	4.99%	4.35%	4.14%	4.16%	
Efficiency ratio(3)	64.67%	60.15%	57.95%	63.30%	63.62%	62.73%	

(1) Presented giving retroactive effect to stock splits in the form of 30% stock dividends paid on July 5, 2006 and February 28, 2005.

(2) Computed by dividing dividends declared per share by net income per share.

(3) Computed by dividing noninterest expense by the sum of net interest income and noninterest income.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion provides information about the results of operations, financial condition, liquidity, and capital resources of Eagle Bancorp, Inc. (the "Company") and its subsidiaries, EagleBank (the "Bank") and Eagle Commercial Ventures ("ECV"). This discussion and analysis should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto, appearing elsewhere in this report.

This report contains forward looking statements within the meaning of the Securities Exchange Act of 1934, as amended, including statements of goals, intentions, and expectations as to future trends, plans, events or results of Company operations and policies and regarding general economic conditions. In some cases, forward looking statements can be identified by use of such words as "may", "will", "anticipate", "believes", "expects", "plans", "estimates", "potential", "continue", "should", and similar words or phases. These statements are based upon current and anticipated economic conditions, nationally and in the Company's market, interest rates and interest rate policy, competitive factors and other conditions which, by their nature, are not susceptible to accurate forecast, and are subject to significant uncertainty. Because of these uncertainties and the assumptions on which this discussion and the forward looking statements are based, actual future operations and results in the future may differ materially from those indicated herein. Readers are cautioned against placing undue reliance on any such forward looking statements.

GENERAL

The Company is a growth oriented, one-bank holding company headquartered in Bethesda, Maryland. We provide general commercial and consumer banking services through our wholly owned banking subsidiary EagleBank, a Maryland chartered bank which is a member of the Federal Reserve System. We were organized in October 1997, to be the holding company for the Bank. The Bank was organized as an independent, community oriented, and full-service banking alternative to the super regional financial institutions, which dominate our primary market area. Our philosophy is to provide superior, personalized service to our customers. We focus on relationship banking, providing each customer with a number of services, becoming familiar with and addressing customer needs in a proactive, personalized fashion.

The Company offers a broad range of commercial banking services to our business and professional clients as well as full service consumer banking services to individuals living and/or working primarily in our service area. We emphasize providing commercial banking services to sole proprietors, small and medium-sized businesses, partnerships, corporations, non-profit organizations and associations, and investors living and working in and near our primary service area. A full range of retail banking services are offered to accommodate the individual needs of both corporate customers as well as the community we serve. These services include the usual deposit functions of commercial banks, including business and personal checking accounts, "NOW" accounts and money market and savings accounts, business, construction, and commercial loans, equipment leasing, residential mortgages and consumer loans and cash management services. We have developed significant expertise and commitment as an SBA lender, have been designated a Preferred Lender by the Small Business Administration (SBA), and are a leading community bank SBA lender in the Washington D.C. district.

PENDING ACQUISITION

In December 2007, the Company announced the signing of a definitive agreement to acquire Fidelity & Trust Financial Corporation ("Fidelity & Trust"), parent of Fidelity & Trust Bank. At September 30, 2007, Fidelity & Trust had $452 million of assets. Fidelity & Trust Bank operates six locations, with one in Northern Virginia, three in Montgomery County, Maryland and two in the District of Columbia. The transaction is subject to regulatory and shareholder approvals and the satisfaction of other conditions, as set forth in the merger agreement. The transaction is currently anticipated to be completed mid 2008. For further information about the proposed acquisition, please refer to "Business Pending Acquisition" at page 61.

Refer to "Note 16 of Notes to Consolidated Financial Statements" on page 54 for further information on this transaction.

CRITICAL ACCOUNTING POLICIES

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and follow general practices within the banking industry. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions and judgments are based on information available as of the date of the consolidated financial statements; accordingly, as this information changes, the consolidated financial statements could reflect different estimates, assumptions, and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions, and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the financial statements at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. The fair values and the information used to record valuation adjustments for investment securities available for sale are based either on quoted market prices or are provided by other third-party sources, when available. As of December 31, 2007, the Company had not adopted the provisions of Statement on Financial Accounting Standards ("SFAS") 157, which establishes a common definition of fair value.

The allowance for credit losses is an estimate of the losses that may be sustained in our loan portfolio. The allowance is based on two principles of accounting: (a) Statement on Financial Accounting Standards ("SFAS") 5, "Accounting for Contingencies", which requires that losses be accrued when they are probable of occurring and are estimable and (b) SFAS No. 114, "Accounting by Creditors for Impairment of a Loan", which requires that losses be accrued when it is probable that the Company will not collect all principal and interest payments according to the contractual terms of the loan. The loss, if any, can be determined by the difference between the loan balance and the value of collateral, the present value of expected future cash flows, or values observable in the secondary markets.

Three components comprise our allowance for credit losses: a specific allowance, a formula allowance, and a nonspecific unallocated allowance. Each component of the allowance is based upon estimates that can and do change when actual events occur.

The specific allowance is used to individually allocate an allowance for loans identified as impaired. Impairment testing includes consideration of the borrower's overall financial condition, resources and payment history, support available from guarantors, and the fair market value of collateral. These factors are combined to estimate the probability and severity of inherent losses. When an impairment is identified, a specific reserve is established based upon the Company's assessment of the estimated loss embedded in the individual loan. Large groups of smaller balance homogenous loans are collectively evaluated for impairment. Accordingly, the Company does not individually evaluate consumer and residential loans for impairment.

The formula allowance is used to estimate the loss on internally risk rated loans, exclusive of those identified as impaired. Loans identified in the risk rating evaluation as meeting the criteria for substandard, doubtful, and loss classification, (classified loans), are segregated from non-classified loans within the portfolio. Unimpaired internally classified loans are stratified by loan type; with each loan type assigned an allowance factor based upon management's estimate of the associated risk. Allowance factors increase with the worsening of internal risk ratings.

The unallocated formula allowance is used to estimate the loss associated with non-classified loans. These unclassified loans are also stratified by loan type and risk rating, and allowance factors are assigned by management based upon a number of factors, including delinquencies, loss history, changes in lending policy and procedures, changes in business and economic conditions, changes in the nature and volume of the portfolio, management expertise, concentrations within the portfolio, quality of loan review systems, competition, and legal and regulatory requirements. The factors assigned differ by loan type and internal risk rating. The unallocated allowance captures losses inherent in the portfolio which have not yet been recognized. Allowance factors and the overall size of the allowance may change from period to period based upon management's assessment of the above described factors and the relative weights given to each factor.

Management has significant discretion in making the judgments inherent in the determination of the provision and allowance for credit losses, including, in connection with the valuation of collateral, a borrower's prospects of repayment, and in establishing allowance factors on the formula allowance and nonspecific or environmental allowance components of the allowance. The establishment of allowance factors is a continuing evaluation, based on management's ongoing assessment of the global factors discussed above and their impact on the portfolio. The allowance factors may change from period to period, resulting in an increase or decrease in the amount of the provision or allowance, based upon the same volume and classification of loans. Changes in allowance factors have a direct impact on the amount of the provision, and a related, after tax effect on net income. Errors in management's perception and assessment of the global factors and their impact on the portfolio could result in the allowance not being adequate to cover losses in the portfolio, and may result in additional provisions or charge-offs. Alternatively, errors in management's perception and assessment of the global factors and their impact on the portfolio could result in the allowance being in excess of amounts necessary to cover losses in the portfolio, and may result in lower provision in the future. For additional information regarding the allowance for credit losses, refer to the discussion under the caption "Allowance for Credit Losses" below.

Beginning in January 2006, the Company adopted the provisions of SFAS No. 123R, which requires the expense recognition for the fair value of stock-based compensation awards, such as stock options, restricted stock units, and performance based shares and the like. This standard allows management to establish modeling assumptions as to expected stock price volatility, option terms, forfeiture rates and dividend rates which directly impact estimated fair value. The accounting standard also allows for the use of alternative option pricing models which may impact fair value as determined. The Company's practice is to utilize reasonable and supportable assumptions which are reviewed with the appropriate Board Committee.

RESULTS OF OPERATIONS

Overview

The Company reported net income of $7.7 million for the year ended December 31, 2007, a 4% decrease from net income of $8.0 million for the year ended December 31, 2006, as compared to $7.5 million for the year ended December 31, 2005.

The decrease in net income for the twelve months ended December 31, 2007 can be attributed substantially to an increase in interest expense of 33% while interest income increased by 13% as compared to the same period in 2006. Net interest income showed an increase of 3% on growth in average earning assets of 13%. For the twelve months ended December 31, 2007, the Company has experienced a 44 basis point decline in its net interest margin from 4.81% in 2006 to 4.37% in 2007. This change was primarily due to reliance on more expensive sources of funds which has increased interest expense at a faster rate than increases in interest income.

Earnings per basic share were $0.80 for the year ended December 31, 2007, as compared to $0.85 for 2006 and $0.82 for 2005. Earnings per diluted share were $0.78 for the year ended December 31, 2007, as compared to $0.81 for 2006 and $0.77 for 2005.

For the three months ended December 31, 2007, the Company reported net income of $2.3 million as compared to $2.2 million for the same period in 2006. Earnings per basic share was $0.24 and $0.23 per diluted share for the three months ended December 31, 2007, as compared to $0.23 per basic share and $0.22 per diluted share for the same period in 2006.

The Company had a return on average assets of .96% and a return on average equity of 10.03% for the year of 2007, as compared to returns on average assets and average equity of 1.13% and 11.63%, respectively, for the year of 2006 and 1.24% and 12.25% respectively, for the year of 2005.

For the twelve months ended December 31, 2007, average interest bearing liabilities funding average earning assets increased to 77% as compared to 73% for the first twelve months of 2006. Additionally, while the average rate on earning assets for the twelve month period ended December 31, 2007, as compared to 2006 has increased by 2 basis points from 7.46% to 7.48%, the cost of interest bearing liabilities has increased by 44 basis points from 3.62% to 4.06%, resulting in a decline in the net interest spread of 42 basis points from 3.84% for the twelve months ended December 31, 2006 to 3.42% for the twelve months ended December 31, 2007. The 44 basis point decline in the net interest margin (from 4.81% for the twelve months ended December 31, 2006 to 4.37% for the twelve months ended December 31, 2007) has been slightly greater than the decline in the net interest spread as the Company's benefit from average noninterest bearing funding sources in 2007 declined modestly as compared to 2006. For the twelve months ended December 31, 2007, average noninterest sources funding earning assets were $178 million as compared to $181 million for the same period in 2006. The slight decline in noninterest funding sources has resulted in a slight decrease in the value of noninterest sources funding earning assets from 97 basis points in 2006 to 95 basis points in 2007.

Due to the need to meet loan funding objectives in excess of deposit growth, the Bank has relied to a larger extent on alternative funding sources, such as FHLB Advances and brokered deposits, the higher costs of which have contributed to a narrowing of the net interest margin. If significant reliance on alternative funding sources continues, the Company's earnings could be adversely impacted.

Loans, which generally have higher yields than securities and other earning assets, increased to 86% of average earning assets in 2007 from 85% of average earning assets for 2006. Investment securities accounted for 11% of average earning assets for both 2007 and 2006. Federal funds sold averaged 2% and 3% of average earning assets for 2007 and 2006, respectively. This decline was directly related to average loan growth over the past twelve month period exceeding the growth of average deposits and other funding sources.

For the quarter ended December 31, 2007, average interest bearing liabilities funding average earning assets increased to 73% as compared to 72% for the same period in 2006. Additionally, while the average rate on earning assets for the quarter ended December 31, 2007, as compared to the same period in 2006, has declined by 33 basis points from 7.56% to 7.23%, the cost of interest bearing liabilities has decreased by 15 basis points from 3.98% to 3.83%, resulting in a decline in the net interest spread of 17 basis points from 3.58% for the quarter ended December 31, 2006 to 3.41% for the quarter ended December 31, 2007. The net interest margin decreased 25 basis points from 4.55% for the quarter ended December 31, 2006 to 4.30% for the quarter ended December 31, 2007, a higher decline than the net interest spread as the benefit of average noninterest sources funding earning assets declined from 97 basis points for the quarter ended December 31, 2006 to 89 basis points for the quarter ended December 31, 2007.

For the quarter ended December 31, 2007 average loans increased 13% over the same period in 2006, maintaining a constant level of approximately 84% of average earning assets. Investment securities for the quarter ended December 31, 2007 amounted to 13% of average earning assets, an increase of 2% from an average of 11% for the same period in 2006. Federal funds sold averaged 3% and 4% of average earning assets for the quarters ended December 31, 2007 and 2006, respectively.

The provision for credit losses was $1.6 million for the year ended December 31, 2007 as compared to $1.7 million in 2006. For the full year 2007, the Company recorded net charge-offs of $979 thousand, as compared to $357 thousand for the same period in 2006. The ratio of net-charge offs to average loans was .15% for 2007 and .06% for 2006. The increase in net charge-offs in 2007 is associated with one large commercial loan relationship identified in prior periods.

At December 31, 2007, the allowance for credit losses was $8.0 million or 1.12% of total loans, as compared to $7.4 million or 1.18% of total loans at December 31, 2006.

The provision for credit losses was $883 thousand for the three months ended December 31, 2007 as compared to $327 thousand for the same period in 2006, the increase being attributable to increases in environmental reserve factors associated with current economic conditions and not to any specific problem loan. For the fourth quarter of 2007, the Company recorded net charge-offs of $250 thousand, as compared to no net charge-offs for the fourth quarter of 2006. The charge-offs in the fourth quarter of 2007 related to one problem loan relationship identified several quarters ago for which specific reserves had been established.

Total noninterest income was $5.2 million for the year 2007 as compared to $3.8 million for 2006, an increase of 35%. These amounts include net investment gains of $6 thousand for the year of 2007 and $124 thousand in 2006. Excluding securities gains, total noninterest income increased by 39%. The increase was attributed primarily to higher amounts of gains on the sale of residential mortgage loans ($416 thousand versus $301 thousand); higher deposit account activity fees ($1.5 million versus $1.4 million) and income from subordinated financing of a real estate project ($1.2 million versus $0). Income from subordinated financing activities can fluctuate greatly between periods, as it is based on the progress of a limited number of development projects. Refer to "Loan Portfolio" section below for further discussion of subordinated financing activity.

For the three months ended December 31, 2007, total noninterest income increased 107% to $2.0 million as compared to $945 thousand for the same period in 2006. Excluding securities losses of $1 thousand during the fourth quarter of 2007 and gains of $39 thousand for the same period in 2006, total noninterest income increased by 116%. The increase was attributed substantially to income ($1.0 million) from the subordinated financing transaction noted above.

Total noninterest expense increased from $21.8 million for 2006 to $24.9 million for 2007, an increase of 14%. The primary reasons for this increase were increases in staff levels over the past twelve months and related personnel cost, occupancy cost (due in part to a new banking office and an expanded lending center facility), higher software licensing costs and expense associated with a reinstated FDIC deposit insurance assessment. The efficiency ratio which measures the level of noninterest expense to total revenue was 64.67% for 2007 as compared to 60.15% for 2006. The higher efficiency ratio relates in part to a lower net interest margin in 2007 as compared to 2006.

The efficiency ratio, improved to 59.87% for the fourth quarter of 2007, as compared to 61.57% for the fourth quarter of 2006, owing to substantial noninterest income in the final three months of 2007. For the three months ended December 31, 2007, total noninterest expense was $6.5 million, as compared to $5.7 million for the same period in 2006, an increase of 13%. This increase was due substantially to the same factors mentioned above which affected the increase for the full year 2007 over 2006.

Net Interest Income and Net Interest Margin

Net interest income is the difference between interest income on earning assets and the cost of funds supporting those assets. Earning assets are composed primarily of loans and investment securities. The cost of funds represents interest expense on deposits, customer repurchase agreements and other borrowings, which comprise federal funds purchased and advances from the Federal Home Loan Bank of Atlanta ("FHLBA"). Noninterest bearing deposits and capital are other components representing funding sources. Changes in the volume and mix of assets and funding sources, along with the changes in yields earned and rates paid, determine changes in net interest income. Net interest income in 2007 was $33.3 million compared to $32.4 million in 2006 and $28.7 million in 2005. For the three months ended December 31, 2007, net interest income was $8.8 million as compared to $8.4 million for the same period in 2006, a 5% increase.

The following table labeled "Average Balances, Interest Yields and Rates and Net Interest Margin" presents the average balances and rates of the various categories of the Company's assets and liabilities. Included in the table is a measurement of interest rate spread and margin. Interest spread is the difference (expressed as a percentage) between the interest rate earned on earning assets less the interest rate paid on interest bearing liabilities. While net interest spread provides a quick comparison of earnings rates versus cost of funds, management believes that the net interest margin provides a better measurement of performance, since the net interest margin includes the effect of noninterest bearing sources in its calculation, which are significant factors in the Company's financial performance. The net interest margin is net interest income (annualized) expressed as a percentage of average earning assets.

Average Balances, Interest Yields and Rates and Net Interest Margin

	Year Ended December 31,								
	2007			2006			2005		
	Average Balance	Interest	Average Yield/ Rate	Average Balance	Interest	Average Yield/ Rate	Average Balance	Interest	Average Yield/ Rate
	(dollars in thousands)								
ASSETS:									
Interest earning assets:									