

CHEMUNG FINANCIAL CORP

Form 10-K

March 28, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2011

OR
 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 0-13888

CHEMUNG FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

NEW YORK	16-123703-8
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
One Chemung Canal Plaza, P.O. Box 1522, Elmira, New York	14902
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (607) 737-3711

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

Common Stock, par value \$0.01 a share
(Title of class)

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if
any, every

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Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 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 NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will

not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in

Part III of this Form 10-K or any amendment to this Form 10-K.

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 definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2

of the Exchange Act.

Large Accelerated Non-accelerated Smaller Reporting
accelerated filer filer filer Company

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

YES NO

Based upon the closing price of the registrant's Common Stock as of June 30, 2011, the aggregate market value of the voting stock

held by non-affiliates of the registrant was \$67,262,296.

As of February 29, 2012 there were 4,579,692 shares of Common Stock, \$0.01 par value outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Shareholders to be held on May 10, 2012 are incorporated by reference

into Part III, Items 10, 11, 12, 13, and 14 of this Form 10-K.

CHEMUNG FINANCIAL CORPORATION

ANNUAL REPORT ON FORM 10-K FOR THE FISCAL YEAR ENDED DECEMBER 31, 2011

Form 10-K Item Number:	Page No.
PART I	1
Item 1. Business	1
Item 1A. Risk Factors	13
Item 1B. Unresolved Staff Comments	17
Item 2. Properties	17
Item 3. Legal Proceedings	17
Item 4. Mine Safety Disclosures	17
PART II	18
Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	18
Item 6. Selected Financial Data	20
Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation	22
Item 7A. Quantitative and Qualitative Disclosures about Market Risk	43
Item 8. Financial Statements and Supplementary Data	43
Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	43
Item 9A. Controls and Procedures	43
Item 9B. Other Information	44
PART III	45
Item 10. Directors, Executive Officers and Corporate Governance	45
Item 11. Executive Compensation	46
Item 12. Security Ownership of Certain Beneficial Owners and Management, and Related Stockholder Matters	46
Item 13. Certain Relationships and Related Transactions, and Director Independence	46
Item 14. Principal Accountant Fees and Services	46
PART IV	46
Item 15. Exhibits and Financial Statement Schedules	47

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Index to Consolidated Financial Statements	48
Report of Independent Registered Public Accounting Firm-Crowe Horwath LLP	F-1
SIGNATURES	F-56

Some of the information contained in this report concerning the markets and industry in which we operate is derived from publicly available information and from industry sources. Although we believe that this publicly available information and information provided by these industry sources are reliable, we have not independently verified the accuracy of any of this information.

PART I

ITEM 1. BUSINESS

General Development of Business

Chemung Financial Corporation (the "Corporation") was incorporated on January 2, 1985 under the laws of the State of New York. The Corporation was organized for the purpose of acquiring Chemung Canal Trust Company (the "Bank"). The Bank was established in 1833 under the name Chemung Canal Bank, and was subsequently granted a New York State bank charter in 1895. In 1902, the Bank was reorganized as a New York State trust company under the name Elmira Trust Company, and its name was changed to Chemung Canal Trust Company in 1903.

The Corporation has been a financial holding company since June 22, 2000. Financial holding company status provides the Corporation with the flexibility to offer an array of financial services, such as insurance products, mutual funds, and brokerage services, which provide additional sources of fee based income and allow the Corporation to better serve its customers. The Corporation established a financial services subsidiary, CFS Group, Inc., in September 2001 which offers non-banking financial services such as mutual funds, annuities, brokerage services, insurance and tax preparation services. As such, the Corporation currently operates as a financial holding company with two subsidiaries, Chemung Canal Trust Company, a full-service community bank with full trust powers, and CFS Group, Inc.

The Securities and Exchange Commission (the "SEC") maintains a web site at www.sec.gov that contains reports, proxy and information statements, and other information regarding the Corporation. You may also read and copy materials we file with the SEC at the SEC's Public Reference Room at 100 F St., NE, Washington, D.C. 20549. You may obtain information concerning the operation of the Public Reference Room by calling 1-800-SEC-0330. In addition, we maintain a corporate web site at www.chemungcanal.com. We make available free of charge through our web site our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and any amendments to those reports pursuant to Section 13(a) or 15(d) of the Exchange Act and filed with the SEC. These items are available as soon as reasonably practicable after we electronically file or furnish such material with or to the SEC. These items are also available on our website as Interactive Data Files as required pursuant to Rule 405 of Regulation S-T (§232.405). The contents of our web site are not a part of this report. These materials are also available free of charge by written request to: Jane H. Adamy, Senior Vice President and Secretary, Chemung Canal Trust Company, One Chemung Canal Plaza, Elmira, NY 14901.

Description of Business

Business

The Bank is a New York State chartered commercial bank which engages in full-service commercial and consumer banking and wealth management business. The Bank's services include accepting time, demand and savings deposits, including NOW accounts, savings accounts, insured money market accounts, investment certificates, fixed-rate certificates of deposit and club accounts. The Bank's services also include making secured and unsecured commercial and consumer loans, financing commercial transactions (either directly or participating with regional industrial development and community lending corporations), and making commercial, residential and home equity mortgage loans, revolving credit loans with overdraft checking protection and small business loans. Additional services include renting safe deposit facilities, the provision of networked automated teller facilities and an internet banking product

featuring bill payment services.

1

Wealth management services provided by the Bank include services as executor and trustee under wills and agreements, and guardian, custodian, trustee and agent for pension, profit-sharing and other employee benefit trusts, as well as various investment, pension, estate planning and employee benefit administrative services.

CFS Group, Inc. offers an array of financial services including mutual funds, full and discount brokerage services, annuity and other insurance products and tax preparation services.

For additional information, including information concerning the results of operations of the Corporation and its subsidiaries, see Management's Discussion and Analysis of Financial Condition and Results of Operations in Part II, Item 7.

There have been no material changes in the manner of doing business by the Corporation or its subsidiaries during the fiscal year ended December 31, 2011.

Market Area and Competition

Seven of the Bank's 28 full-service offices, including the main office, are located in Chemung County, New York. The Bank has thirteen full-service offices located in the nearby counties of Broome, Schuyler, Steuben, Tioga and Tompkins. In April 2011, Chemung Canal Trust Company, as part of the Fort Orange Financial Corp. acquisition by Chemung Financial Corporation, added five full service branch offices to its footprint in Albany and Saratoga counties under the name Capital Bank, a division of Chemung Canal Trust Company. The Bank also operates 3 full-service offices in Bradford County, Pennsylvania and full service Wealth Management Centers located in Chemung and Broome counties. The Corporation defines its primary market areas as those areas within a 25-mile radius of its New York offices in Albany, Broome, Chemung, Saratoga, Steuben, Schuyler, Tioga and Tompkins counties, including the northern tier of Pennsylvania.

Within these market areas, the Bank encounters intense competition in the lending and deposit gathering aspects of its business from commercial and thrift banking institutions, credit unions and other providers of financial services, such as brokerage firms, investment companies, insurance companies and Internet banking institutions. The Bank also competes with non-financial institutions, including retail stores and certain utilities that maintain their own credit programs, as well as governmental agencies that make available loans to certain borrowers. Unlike the Bank, many of these competitors are not subject to regulation as extensive as that affecting the Bank and, as a result, they may have a competitive advantage over the Bank in certain respects. This is particularly true of credit unions because their pricing structure is not encumbered by income taxes.

Competition for the Bank's Wealth Management Group services comes primarily from brokerage firms and independent investment advisors. These firms devote much of their considerable resources toward gaining larger positions in these markets. The market value of the Bank's Wealth Management Group assets under administration totaled approximately \$1.6 billion at year-end 2011. The Wealth Management Group division is responsible for the largest component of non-interest revenue.

Supervision and Regulation

The Corporation is regulated under the Bank Holding Company Act of 1956, as amended (the "BHC Act"), and is subject to the supervision of the Board of Governors of the Federal Reserve System (the "Federal Reserve Board"). As a bank holding company, the Corporation generally may engage in the activities permissible for a bank holding company, which includes banking, managing or controlling banks, performing certain servicing activities for subsidiaries, and engaging in other activities that the Federal Reserve Board has determined to be so closely related

to banking as to be a proper incident thereto. Because the Corporation also has elected financial holding company status, it may also engage in a broader range of activities that are determined by the Federal Reserve and the Secretary of the Treasury to be financial in nature or incidental to financial activities or activities that are determined by the Federal Reserve Board to be complementary to a financial activity and that do not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally.

The Corporation is also under the jurisdiction of the SEC and is subject to the disclosure and regulatory requirements of the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, as administered by the SEC.

The Bank is chartered under the laws of New York State and is supervised by the New York State Department of Financial Services ("NYSDFS"). The Bank also is a member bank of the Federal Reserve System and, therefore, the Federal Reserve Board serves as its primary federal regulator.

CFS Group, Inc. is subject to supervision by other regulatory authorities as determined by the activities in which it is engaged. Insurance activities are supervised by the NYSD, and brokerage activities are subject to supervision by the SEC and the Financial Industry Regulatory Authority ("FINRA").

The Corporation is subject to capital adequacy guidelines of the Federal Reserve Board. The guidelines apply on a consolidated basis and require bank holding companies to maintain a minimum ratio of Tier 1 capital to total assets (or "leverage ratio") of 4%. For the most highly rated bank holding companies, the minimum ratio is 3%. The Federal Reserve Board capital adequacy guidelines also require bank holding companies to maintain a minimum ratio of Tier 1 capital to risk-weighted assets of 4% and a minimum ratio of qualifying total capital to risk-weighted assets of 8%. Any bank holding company whose capital does not meet the minimum capital adequacy guidelines is considered to be undercapitalized, and is required to submit an acceptable plan to the Federal Reserve Board for achieving capital adequacy. In addition, an undercapitalized company's ability to pay dividends to its shareholders and expand its lines of business through the acquisition of new banking or non-banking subsidiaries also could be restricted by the Federal Reserve Board. The Federal Reserve Board may set higher minimum capital requirements for bank holding companies where circumstances warrant, such as companies anticipating significant growth or facing unusual risks. As of December 31, 2011, the Corporation's leverage ratio was 8.27%, its ratio of Tier 1 capital to risk-weighted assets was 11.84% and its ratio of qualifying total capital to risk-weighted assets was 13.28%. The Federal Reserve Board has not advised the Corporation that it is subject to any special capital requirements.

Pursuant to Federal Reserve Board regulations and supervisory policies, bank holding companies also are expected to serve as a source of financial and managerial strength to their subsidiary depository institutions. Therefore, to the extent the Bank is in need of capital, the Corporation could be expected to provide additional capital to the Bank, including, potentially, raising new capital for that purpose.

The Bank is subject to leverage and risk-based capital requirements and minimum capital guidelines of the Federal Reserve Board that are similar to those applicable to the Corporation. As of December 31, 2011, the Bank was in compliance with all minimum capital requirements. The Bank's leverage ratio as of that date was 7.92%, its ratio of Tier 1 capital to risk-weighted assets was 11.36%, and its ratio of qualifying total capital to risk-weighted assets was 12.80%.

The Bank also is subject to substantial regulatory restrictions relating to its ability to pay dividends to the Corporation. Under Federal Reserve Board and NYSDFS regulations, the Bank may not pay a dividend without prior approval of the Federal Reserve and the NYSDFS if the total amount of all dividends declared during such calendar year, including the proposed dividend, exceeds the sum of its retained net income to date during the calendar year and its retained net income over the preceding two calendar years. As of December 31, 2011, approximately \$4.6 million was available for the payment of dividends by the Bank to the Corporation without prior approval, after giving effect to the payment of dividends in the fourth quarter of 2011. The Bank's ability to pay dividends also is subject to the Bank being in compliance with regulatory capital requirements. The Bank is currently in compliance with these requirements.

The deposits of the Bank are insured up to regulatory limits by the Federal Deposit Insurance Corporation (the "FDIC") and are subject to the deposit insurance premium assessments of the Deposit Insurance Fund ("DIF"). The FDIC currently maintains a risk-based assessment system under which assessment rates vary based on the level of risk posed by the institution to the DIF. The assessment rate may, therefore, change after any of these measurements change.

In February 2011, the FDIC adopted a final rule making certain changes to the deposit insurance assessment system. Among other things, the rule revised the assessment rate schedule effective April 1, 2011, and adopted additional rate schedules that will go into effect when the DIF reserve ratio reaches various milestones. The rule changed the deposit insurance assessment system from one that was based on domestic deposits to one that is based on average consolidated total assets minus average tangible equity. In addition, the rule provides that FDIC dividend payments will be suspended if the DIF reserve ratio exceeds 1.5 percent but that assessment rates will decrease when the DIF reserve ratio reaches certain thresholds.

All institutions with deposits insured by the FDIC are required to pay assessments to fund interest payments on bonds issued by the Financing Corporation ("FICO"), an agency of the Federal government established to recapitalize the predecessor to the Savings Association Insurance Fund. These assessments will continue until the FICO bonds mature in 2017. The FDIC's FICO assessment authority is separate from its authority to assess risk-based premiums for deposit insurance. The FICO assessment rate is adjusted quarterly to reflect changes in the assessment bases of the fund and is not risk-based by institution. The FICO assessment rate for the first quarter of 2012, due December 30, 2011, was .066% of insured deposits.

The Bank is also a member of the Federal Home Bank ("FHLB") of New York, which provides a central credit facility primarily for member institutions for home mortgage and neighborhood lending. The Bank is subject to the rules and requirements of the FHLB, including the requirement to acquire and hold shares of capital stock in the FHLB. The Bank was in compliance with the rules and requirements of the FHLB at December 31, 2011.

The Dodd-Frank Act

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), enacted on July 21, 2010, significantly changed the bank regulatory landscape and has impacted and will continue to impact the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act requires various federal agencies to adopt a broad range of new rules and regulations, and to prepare various studies and reports for Congress.

The Dodd-Frank Act directs the federal banking agencies to establish minimum leverage and risk-based capital requirements for insured depository institutions and bank holding companies with assets greater than \$500 million, among others, that should be no lower than the minimum requirements applicable to banks as of the date of enactment of the Dodd-Frank Act. On June 14, 2011, the FRB, along with other federal banking supervisors, issued a final rule implementing the minimum leverage and risk-based capital requirements. The Dodd-Frank Act also directs the appropriate federal banking supervisors, subject to Council recommendations, to develop capital requirements for all insured depository institutions, depository institution holding companies and systemically important non-bank financial companies to address systemically risky activities.

As noted above, the Dodd-Frank Act broadened the base for Federal Deposit Insurance Corporation insurance assessments. Assessments are now be based on the average consolidated total assets less tangible equity capital of a financial institution. The Dodd-Frank Act also permanently increases the maximum amount of deposit insurance for banks, savings institutions and credit unions to \$250,000 per depositor per insured institution, retroactive to January 1, 2008, and provided qualifying non-interest bearing transaction accounts with unlimited deposit insurance through

December 31, 2012.

4

The Dodd-Frank Act requires publicly traded companies to give stockholders a non-binding vote on executive compensation and so-called "golden parachute" payments. The legislation also authorizes the SEC to promulgate rules that would allow stockholders to nominate their own candidates using the company's proxy materials. Additionally, the Dodd-Frank Act directs the federal banking regulators to promulgate rules requiring the reporting of incentive-based compensation and prohibiting excessive incentive-based compensation paid to executives of depository institutions and their holding companies with assets in excess of \$1.0 billion. In April 2011, the FRB, along with other federal banking supervisors, issued a joint notice of proposed rulemaking implementing those requirements.

The Dodd-Frank Act created a new Bureau of Consumer Financial Protection ("CFPB") with wide-ranging powers to supervise and enforce consumer protection laws. The CFPB has broad rule-making authority for a wide range of consumer protection laws that apply to all banks and savings institutions, including the authority to prohibit "unfair, deceptive or abusive" acts and practices. The CFPB has examination and enforcement authority over all banks and savings institutions with more than \$10 billion in assets. The Dodd-Frank Act also weakened the federal preemption rules that have been applicable to national banks and federal savings associations, and gives state attorneys general certain powers to enforce federal consumer protection regulations.

It is difficult to predict at this time what specific impact certain provisions of the Dodd-Frank Act and its implementing rules and regulations, including those yet to be written, will have on the Corporation. The financial reform legislation and any additional implementing rules that are ultimately issued could have adverse implications on the financial industry, the competitive environment, and the Corporation's ability to conduct business. The Corporation will have to apply resources to ensure compliance with all applicable provisions of the Dodd-Frank Act and its implementing rules, which may further increase the Corporation's costs of operations and adversely impact its earnings.

Basel III Amendments to Capital Adequacy Requirements

In December 2010, the Basel Committee, a group of bank regulatory supervisors from around the world, released its final framework for strengthening international capital and liquidity regulation, now officially identified by the Basel Committee as "Basel III." Basel III, when implemented by the U.S. bank regulatory agencies and fully phased-in, will require bank holding companies and their bank subsidiaries to maintain substantially more capital, with a greater emphasis on common equity. The Basel III final capital framework, among other things:

- introduces as a new capital measure "Common Equity Tier 1", or "CET1", specifies that Tier 1 capital consists of CET1 and "Additional Tier 1 capital" instruments meeting specified requirements, defines CET1 narrowly by requiring that most adjustments to regulatory capital measures be made to CET1 and not to the other components of capital, and expands the scope of the adjustments as compared to existing regulations;
- when fully phased in on January 1, 2019, requires banks to maintain:
 - as a newly adopted international standard, a minimum ratio of CET1 to risk-weighted assets of at least 4.5 percent, plus a 2.5 percent "capital conservation buffer" (which is added to the 4.5 percent CET1 ratio as that buffer is phased in, effectively resulting in a minimum ratio of CET1 to risk-weighted assets of at least 7 percent);
- a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0 percent, plus the capital conservation buffer (which is added to the 6.0 percent Tier 1 capital ratio as that buffer is phased in, effectively resulting in a minimum Tier 1 capital ratio of 8.5 percent upon full implementation);
- a minimum ratio of Total (that is, Tier 1 plus Tier 2) capital to risk-weighted assets of at least 8.0

percent, plus the capital conservation buffer (which is added to the 8.0 percent total capital ratio as that buffer is phased in, effectively resulting in a minimum total capital ratio of 10.5 percent upon full implementation);

- as a newly adopted international standard, a minimum leverage ratio of 3.0 percent, calculated as the ratio of Tier 1 capital to balance sheet exposures plus certain off-balance sheet exposures (as the average for each quarter of the month-end ratios for the quarter); and
- provides for a “countercyclical capital buffer”, generally to be imposed when national regulators determine that excess aggregate credit growth becomes associated with a buildup of systemic risk, that would be a CET1 add-on to the capital conservation buffer in the range of 0 percent to 2.5 percent when fully implemented (potentially resulting in total buffers of between 2.5 percent and 5 percent).

The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of CET1 to risk-weighted assets above the minimum but below the conservation buffer (or below the combined capital conservation buffer and countercyclical capital buffer, when the latter is applied) will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall.

The implementation of the Basel III final framework will commence January 1, 2013. On that date, banking institutions will be required to meet the following minimum capital ratios:

- 3.5 percent CET1 to risk-weighted assets;
- 4.5 percent Tier 1 capital to risk-weighted assets; and
- 8.0 percent Total capital to risk-weighted assets.

The Basel III final framework provides for a number of new deductions from and adjustments to CET1. These include, for example, the requirement that mortgage servicing rights, deferred tax assets and significant investments in non-consolidated financial entities be deducted from CET1 to the extent that any one such category exceeds 10 percent of CET1 or all such categories in the aggregate exceed 15 percent of CET1.

Implementation of the deductions and other adjustments to CET1 will begin on January 1, 2014 and will be phased-in over a five-year period (20 percent per year). The implementation of the capital conservation buffer will begin on January 1, 2016 at 0.625 percent and be phased in over a four-year period (increasing by that amount on each subsequent January 1, until it reaches 2.5 percent on January 1, 2019).

The U.S. banking agencies have indicated informally that they expect to propose regulations implementing Basel III in early 2012.

The Dodd-Frank Act requires the Federal Reserve to adopt regulations imposing a continuing “floor” of the Basel I-based capital requirements in cases where the Basel II-based capital requirements and any changes in capital regulations resulting from Basel III otherwise would permit lower requirements. In June 2011, the Federal Reserve finalized regulations implementing this requirement.

Given that the Basel III rules are subject to implementation and change and the scope and content of capital regulations that U.S. federal banking agencies may adopt under the Dodd-Frank Act is uncertain, the Corporation cannot be certain of the impact new capital regulations will have on its capital ratios.

Other Regulatory and Legislative Actions

Transactions between the Bank and either the Corporation or CFS Group, Inc. are governed by sections 23A and 23B of the Federal Reserve Act ("FRA") and the Federal Reserve Board's implementing Regulation W. Generally, these provisions are intended to protect insured depository institutions from suffering losses arising from transactions with non-insured affiliates, by placing quantitative and qualitative limitations on covered transactions between a bank and any one affiliate as well as all affiliates of the bank in the aggregate, and requiring that such transactions be on terms that are consistent with safe and sound banking practices. Sections 22(g) and (h) of the FRA and their implementing Regulation O restrict the amounts and terms of loans to directors, executive officers and principal shareholders.

Under the privacy and data security provisions of the Financial Modernization Act of 1999, also known as the Gramm-Leach-Bliley Act ("GLB Act"), and rules promulgated thereunder, all financial institutions, including the Corporation, the Bank and CFS Group, Inc., are required to establish policies and procedures to restrict the sharing of nonpublic customer data with nonaffiliated parties at the customer's request and to protect customer data from unauthorized access. In addition, the Fair Credit Reporting Act ("FCRA"), as amended by the Fair and Accurate Credit Transactions Act of 2003 ("FACT Act"), includes many provisions affecting the Corporation, Bank, and/or CFS Group, Inc., including provisions concerning obtaining consumer reports, furnishing information to consumer reporting agencies, maintaining a program to prevent identity theft, sharing of certain information among affiliated companies, and other provisions. For instance, FCRA requires persons subject to FCRA to notify their customers if they report negative information about them to a credit bureau or if they are granted credit on terms less favorable than those generally available. The Federal Reserve Board and the Federal Trade Commission ("FTC") have extensive rulemaking authority under the FACT Act, and the Corporation and the Bank are subject to the rules that have been promulgated by the Federal Reserve Board and FTC thereunder, including recent rules regarding limitations on affiliate marketing and implementation of programs to identify, detect and mitigate the risk of identity theft through red flags. The Corporation has developed policies and procedures for itself and its subsidiaries to maintain compliance and believes it is in compliance with all privacy, information sharing and notification provisions of the GLB Act and FCRA.

The GLB Act and FCRA also impose requirements regarding data security and the safeguarding of customer information. The Bank is subject to the Interagency Guidelines Establishing Information Security Standards (Security Guidelines), which implement section 501(b) of the GLB Act and section 216 of the FACT Act. The Security Guidelines establish standards relating to administrative, technical, and physical safeguards to ensure the security, confidentiality, integrity and the proper disposal of customer information. The Bank believes it is in compliance with all such standards.

Under Title III of the USA PATRIOT Act, also known as the International Money Laundering Abatement and Anti-Terrorism Financing Act of 2001, all financial institutions are required in general to identify their customers, adopt formal and comprehensive anti-money laundering programs, scrutinize or prohibit altogether certain transactions of special concern, and be prepared to respond to inquiries from U.S. law enforcement agencies concerning their customers and their transactions. Additional information-sharing among financial institutions, regulators, and law enforcement authorities is encouraged by the presence of an exemption from the privacy provisions of the GLB Act for financial institutions that comply with this provision and the authorization of the Secretary of the Treasury to adopt rules to further encourage cooperation and information-sharing. The effectiveness of a financial institution in combating money laundering activities is a factor to be considered in any application submitted by the financial institution under the Bank Merger Act, which applies to the Bank, or the BHC Act, which applies to the Corporation.

The Bank has a responsibility under the Community Reinvestment Act of 1977 ("CRA") to help meet the credit needs of its communities, including low- and moderate-income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with the CRA. Regulators assess the Bank's record of compliance with the CRA. In addition, the Equal Credit Opportunity Act and the Fair Housing Act prohibit discrimination in lending practices on the basis of characteristics specified in those statutes. The Bank's failure to comply with the provisions of the CRA could, at a minimum, result in regulatory restrictions on its activities and the activities of the Corporation. The Bank's failure to comply with the Equal Credit Opportunity Act and the Fair Housing Act could result in enforcement actions against it by its regulators as well as other federal regulatory agencies including the CFPB and the Department of Justice. The Bank's latest CRA rating was "Outstanding".

The Sarbanes-Oxley Act of 2002 implemented a broad range of measures to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies, and protect investors by improving the accuracy and reliability of corporate disclosures for companies that have securities registered under the Exchange Act, including publicly-held financial holding companies such as the Corporation. Among other things, Sarbanes-Oxley and/or its implementing regulations have established new membership requirements and additional responsibilities for the Corporation's audit committee, imposed restrictions on the relationship between the Corporation and its outside auditors (including restrictions on the types of non-audit services its auditors may provide to it), imposed additional responsibilities for its external financial statements on its chief executive officer and chief financial officer, expanded the disclosure requirements for its corporate insiders, required its management to evaluate its disclosure controls and procedures and its internal control over financial reporting, and required its auditors to issue a report on its internal control over financial reporting.

Home mortgage lenders, including banks, are required under the Home Mortgage Disclosure Act to make available to the public information regarding the pricing of home mortgage loans, including the "rate spread" between the interest rate on loans and certain Treasury securities and other benchmarks. The availability of this information has led to increased scrutiny of higher-priced loans at all financial institutions to detect illegal discriminatory practices and to the initiation of a limited number of investigations by federal banking agencies and the U.S. Department of Justice. The Corporation has no information that it or its affiliates are the subject of any investigation.

In recent years, declining housing values have resulted in deteriorating economic conditions across the U.S., resulting in significant writedowns in the values of mortgage-backed securities and derivative securities by financial institutions, government sponsored entities, and major commercial and investment banks. This has led to decreased confidence in financial markets among borrowers, lenders, and depositors as well as extreme volatility in the capital and credit markets and the failure of some entities in the financial sector. The Corporation is fortunate that the markets it serves have been impacted to a lesser extent than many areas around the country.

Employees

As of December 31, 2011, the Corporation and its subsidiaries employed 349 persons on a full-time equivalent basis. None of the Corporation's employees are covered by collective bargaining agreements, and the Corporation believes that its relationship with its employees is good.

Recent Developments

On March 19, 2012, the Corporation received a letter from a law firm on behalf of its client, Automated Transactions, LLC, which asserts claims against the Corporation for patent infringement based upon the Corporation's ATM operations. The letter includes a copy of a proposed complaint seeking injunctive relief and damages for the alleged

infringement and also suggests the possibility of an amicable resolution of these claims. The Corporation is reviewing the allegations of the proposed complaint and plans to engage counsel to represent it in this matter.

Financial Information about Foreign and Domestic Operations and Export Sales

Neither the Corporation nor its subsidiaries relies on foreign sources of funds or income.

Statistical Disclosure by Bank Holding Companies

The following disclosures present certain summarized statistical data covering the Corporation and its subsidiaries. See also Management's Discussion and Analysis of Financial Condition and Results of Operations in Part II, Item 7, of this report for other required statistical data.

Investment Portfolio

The following table sets forth the carrying amount of available for sale and held to maturity investment securities at the dates indicated (in thousands of dollars):

	December 31,		
	2011	2010	2009
Obligations of U.S. Government and U.S. Government sponsored enterprises	\$ 152,080	\$ 102,132	\$ 84,621
Mortgage-backed securities, residential	50,766	62,762	93,945
Collateralized mortgage obligations	7,537	-	-
Obligations of states and political subdivisions	54,825	46,480	44,284
Corporate bonds and notes	13,684	11,694	12,185
SBA loan pools	1,950	-	-
Trust preferred securities	2,310	2,344	2,261
Corporate stocks	6,030	5,848	5,847
Total	\$ 289,182	\$ 231,260	\$ 243,143

Included in the above table are \$280,870, \$223,545 and \$230,984 (in thousands of dollars) of securities available for sale at December 31, 2011, 2010 and 2009, respectively. Also included in the above table are \$8,312, \$7,715 and \$12,160 (in thousands of dollars) of securities held to maturity at December 31, 2011, 2010 and 2009, respectively.

The following table sets forth the carrying amounts and maturities of debt securities at December 31, 2011 and the weighted average yields of such securities (all yields are calculated on the basis of the amortized cost and weighted for the scheduled maturity of each security, except mortgage-backed securities which are based on the average life at the projected prepayment speed of each security). Federal tax equivalent adjustments have not been made in calculating yields on municipal obligations:

Maturing			
Dollars in thousands			
Within One Year		After One, But Within Five Years	
Amount	Yield	Amount	Yield
\$25,858	1.79%	\$123,670	1.64%

Obligations of U.S. Government and U.S. Government sponsored enterprises				
Mortgage-backed securities, residential	2,244	3.59%	44,632	3.85%
Collateralized mortgage obligations	3,131	2.08%	4,406	3.33%
Obligations of states and political subdivisions	10,611	2.42%	30,977	2.34%
Corporate bonds and notes	2,084	2.82%	11,356	4.76%
SBA loan pools	508	2.52%	-	-
Trust preferred securities	1,025	8.99%	-	-
Total	\$45,461	2.25%	\$215,041	2.39%

	Maturing			
	Dollars in thousands			
	After Five, But Within Ten Years		After Ten Years	
	Amount	Yield	Amount	Yield
Obligations of U.S. Government and U.S. Government sponsored enterprises	\$ 2,552	3.24%	\$ -	-%
Mortgage-backed securities, residential	1,900	3.84%	1,990	2.23%
Collateralized mortgage obligations	-	-%	-	-
Obligations of states and political subdivisions	13,237	3.50%	-	-
Corporate bonds and notes	244	3.25	-	-
SBA loan pools	1,442	1.85%	-	-
Trust preferred securities	-	-	1,285	69.10%
Total	\$ 19,375	3.37%	\$ 3,275	32.52%

Loan Portfolio

The following table shows the Corporation's loan distribution by segment at the end of each of the last five years, net of deferred origination fees and costs, and unearned income (in thousands of dollars):

	December 31,				
	2011	2010	2009	2008	2007
Commercial, financial and agricultural	\$ 142,743				