

NEW PEOPLES BANKSHARES INC

Form 10-Q

August 08, 2011

[Table of Contents](#)

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-Q**

x **Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
For the quarterly period ended June 30, 2011

.. **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: 000-33411

**NEW PEOPLES BANKSHARES, INC.**

(Exact name of registrant as specified in its charter)

Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

**Virginia**  
(State or other jurisdiction of  
incorporation or organization)

**31-1804543**  
(I.R.S. Employer  
Identification No.)

**67 Commerce Drive**  
**Honaker, Virginia**  
(Address of principal executive offices)

**24260**  
(Zip Code)

**(276) 873-7000**

(Registrant's telephone number, including area code)

n/a

(Former name, former address and former fiscal year, 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  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every 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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer   
Non-accelerated filer  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

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

10,010,178 shares of common stock, par value \$2.00 per share, outstanding as of August 8, 2011.

**Table of Contents**

**NEW PEOPLES BANKSHARES, INC.**

INDEX

	Page
PART I <u>FINANCIAL INFORMATION</u>	2
Item 1. <u>Financial Statements</u>	2
<u>Consolidated Statements of Income - Six Months Ended June 30, 2011 and 2010 (Unaudited)</u>	2
<u>Consolidated Statements of Income - Three Months Ended June 30, 2011 and 2010 (Unaudited)</u>	3
<u>Consolidated Balance Sheets - June 30, 2011 (Unaudited) and December 31, 2010</u>	4
<u>Consolidated Statements of Changes in Stockholders' Equity Six Months Ended June 30, 2011 and 2010 (Unaudited)</u>	5
<u>Consolidated Statements Of Cash Flows - Six Months Ended June 30, 2011 and 2010 (Unaudited)</u>	6
<u>Notes to Consolidated Financial Statements</u>	7
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	18
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	24
Item 4. <u>Controls and Procedures</u>	24
PART II <u>OTHER INFORMATION</u>	25
Item 1. <u>Legal Proceedings</u>	25
Item 1A. <u>Risk Factors</u>	25
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	25
Item 3. <u>Defaults upon Senior Securities</u>	25
Item 4. <u>(Removed and Reserved)</u>	25
Item 5. <u>Other Information</u>	25
Item 6. <u>Exhibits</u>	25
<u>SIGNATURES</u>	26

**Table of Contents****Part I Financial Information****Item 1 Financial Statements****NEW PEOPLES BANKSHARES, INC.****CONSOLIDATED STATEMENTS OF INCOME****FOR THE SIX MONTHS ENDED JUNE 30, 2011 AND 2010**

(IN THOUSANDS EXCEPT SHARE AND PER SHARE DATA)

(UNAUDITED)

	2011	2010
<b>INTEREST AND DIVIDEND INCOME</b>		
Loans including fees	\$ 21,402	\$ 24,478
Federal funds sold	9	21
Interest-earning deposits with banks	80	
Investments	84	58
Dividends on equity securities (restricted)	50	42
<b>Total Interest and Dividend Income</b>	<b>21,625</b>	<b>24,599</b>
<b>INTEREST EXPENSE</b>		
Deposits		
Demand	89	150
Savings	324	393
Time deposits below \$100,000	2,630	3,792
Time deposits above \$100,000	1,574	2,337
FHLB Advances	444	524
Other borrowings	105	122
Trust Preferred Securities	200	219
<b>Total Interest Expense</b>	<b>5,366</b>	<b>7,537</b>
<b>NET INTEREST INCOME</b>	<b>16,259</b>	<b>17,062</b>
<b>PROVISION FOR LOAN LOSSES</b>	<b>3,457</b>	<b>3,940</b>
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES</b>	<b>12,802</b>	<b>13,122</b>
<b>NONINTEREST INCOME</b>		
Service charges	1,159	1,313
Fees, commissions and other income	1,019	989
Insurance and investment fees	191	279
Life insurance investment income	176	209
<b>Total Noninterest Income</b>	<b>2,545</b>	<b>2,790</b>
<b>NONINTEREST EXPENSES</b>		

Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

Salaries and employee benefits	7,859	7,520
Occupancy and equipment expense	2,144	2,334
Advertising and public relations	183	194
Data processing and telecommunications	798	814
FDIC insurance premiums	1,096	1,500
Other real estate owned and repossessed vehicles, net	2,490	302
Other operating expenses	2,660	2,358
<b>Total Noninterest Expenses</b>	<b>17,230</b>	<b>15,022</b>
<b>INCOME (LOSS) BEFORE INCOME TAXES</b>	<b>(1,883)</b>	<b>890</b>
<b>INCOME TAX EXPENSE (BENEFIT)</b>	<b>(757)</b>	<b>235</b>
<b>NET INCOME (LOSS)</b>	<b>\$ (1,126)</b>	<b>\$ 655</b>
<b>Earnings (Loss) Per Share</b>		
Basic	\$ (0.11)	\$ 0.07
Fully Diluted	\$ (0.11)	\$ 0.07
<b>Average Weighted Shares of Common Stock</b>		
Basic	10,010,178	10,009,039
Fully Diluted	10,010,178	10,009,039

The accompanying notes are an integral part of this statement.

**Table of Contents****NEW PEOPLES BANKSHARES, INC.****CONSOLIDATED STATEMENTS OF INCOME****FOR THE THREE MONTHS ENDED JUNE 30, 2011 AND 2010**

(IN THOUSANDS EXCEPT SHARE AND PER SHARE DATA)

(UNAUDITED)

	2011	2010
<b>INTEREST AND DIVIDEND INCOME</b>		
Loans including fees	\$ 10,514	\$ 12,283
Federal funds sold		11
Interest-earning deposits with banks	54	
Investments	45	35
Dividends on equity securities (restricted)	28	21
<b>Total Interest and Dividend Income</b>	<b>10,641</b>	<b>12,350</b>
<b>INTEREST EXPENSE</b>		
Deposits		
Demand	44	77
Savings	138	193
Time deposits below \$100,000	1,242	1,812
Time deposits above \$100,000	769	1,118
FHLB Advances	223	263
Other borrowings	44	59
Trust Preferred Securities	92	112
<b>Total Interest Expense</b>	<b>2,552</b>	<b>3,634</b>
<b>NET INTEREST INCOME</b>	<b>8,089</b>	<b>8,716</b>
<b>PROVISION FOR LOAN LOSSES</b>	<b>2,312</b>	<b>1,950</b>
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES</b>	<b>5,777</b>	<b>6,766</b>
<b>NONINTEREST INCOME</b>		
Service charges	607	703
Fees, commissions and other income	445	448
Insurance and investment fees	93	159
Life insurance investment income	89	103
<b>Total Noninterest Income</b>	<b>1,234</b>	<b>1,413</b>
<b>NONINTEREST EXPENSES</b>		
Salaries and employee benefits	3,946	4,019
Occupancy and equipment expense	1,119	1,130
Advertising and public relations	98	116
Data processing and telecommunications	392	399
FDIC insurance premiums	421	750

Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

Other real estate owned and repossessed vehicles, net	2,246	156
Other operating expenses	1,395	1,301
<b>Total Noninterest Expenses</b>	<b>9,617</b>	<b>7,871</b>
<b>INCOME (LOSS) BEFORE INCOME TAXES</b>	<b>(2,606)</b>	<b>308</b>
<b>INCOME TAX EXPENSE (BENEFIT)</b>	<b>(931)</b>	<b>66</b>
<b>NET INCOME (LOSS)</b>	<b>\$ (1,675)</b>	<b>\$ 242</b>
<b>Earnings (Loss) Per Share</b>		
Basic	\$ (0.17)	\$ 0.02
Fully Diluted	\$ (0.17)	\$ 0.02
<b>Average Weighted Shares of Common Stock</b>		
Basic	10,010,178	10,009,042
Fully Diluted	10,010,178	10,009,042

The accompanying notes are an integral part of this statement.

**Table of Contents****NEW PEOPLES BANKSHARES, INC.****CONSOLIDATED BALANCE SHEETS**

(IN THOUSANDS EXCEPT PER SHARE AND SHARE DATA)

	<b>June 30, 2011</b>	<b>December 31, 2010</b>
	(Unaudited)	(Audited)
<b>ASSETS</b>		
Cash and due from banks	\$ 18,818	\$ 14,369
Interest-bearing deposits with banks	69,082	42,549
Federal funds sold	1,010	25,611
<b>Total Cash and Cash Equivalents</b>	<b>88,910</b>	<b>82,529</b>
Investment securities		
Available-for-sale	4,383	4,658
Loans receivable	664,003	707,794
Allowance for loan losses	(18,697)	(25,014)
<b>Net Loans</b>	<b>645,306</b>	<b>682,780</b>
Bank premises and equipment, net	33,780	34,141
Equity securities (restricted)	3,733	3,878
Other real estate owned	11,137	12,346
Accrued interest receivable	3,368	3,700
Life insurance investments	11,187	11,011
Goodwill and other intangibles	4,288	4,346
Deferred taxes	7,362	8,037
Other assets	7,653	5,201
<b>Total Assets</b>	<b>\$ 821,107</b>	<b>\$ 852,627</b>
<b>LIABILITIES</b>		
Deposits:		
Demand deposits:		
Noninterest bearing	\$ 102,343	\$ 87,839
Interest-bearing	56,062	60,022
Savings deposits	99,992	108,119
Time deposits	482,756	510,100
<b>Total Deposits</b>	<b>741,153</b>	<b>766,080</b>
Federal Home Loan Bank advances	18,583	24,183
Accrued interest payable	1,795	1,720
Accrued expenses and other liabilities	1,150	1,475
Line of credit borrowing		4,900
Other borrowings	5,450	250
Trust preferred securities	16,496	16,496
<b>Total Liabilities</b>	<b>784,627</b>	<b>815,104</b>



**STOCKHOLDERS EQUITY**

Common stock - \$2.00 par value; 50,000,000 shares authorized; 10,010,178 shares issued and outstanding	20,020	20,020
Additional paid-in-capital	21,689	21,689
Retained earnings (deficit)	(5,301)	(4,175)
Accumulated other comprehensive income (loss)	72	(11)
 Total Stockholders Equity	 36,480	 37,523
 Total Liabilities and Stockholders Equity	 \$ 821,107	 \$ 852,627

The accompanying notes are an integral part of this statement.

**Table of Contents****NEW PEOPLES BANKSHARES, INC.****CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY****FOR THE SIX MONTHS ENDED JUNE 30, 2011 AND 2010**

(IN THOUSANDS INCLUDING SHARE DATA)

(UNAUDITED)

	Shares of Common Stock	Common Stock	Additional Paid in Capital	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income (Loss)	Total Shareholders Equity	Comprehensive Income (Loss)
Balance, December 31, 2009	10,009	\$ 20,018	\$ 21,683	\$ 4,890	\$ 28	\$ 46,619	
Net Income				655		655	\$ 655
Unrealized loss on available-for-sale securities, net of \$2 tax					4	4	4
Balance, June 30, 2010	10,009	\$ 20,018	\$ 21,683	\$ 5,545	\$ 32	\$ 47,278	\$ 659
Balance, December 31, 2010	10,010	\$ 20,020	\$ 21,689	\$ (4,175)	\$ (11)	\$ 37,523	
Net Income (Loss)				(1,126)		(1,126)	\$ (1,126)
Unrealized gain on available-for-sale securities, net of \$43 tax					83	83	83
Balance, June 30, 2011	10,010	\$ 20,020	\$ 21,689	\$ (5,301)	\$ 72	\$ 36,480	\$ (1,043)

The accompanying notes are an integral part of this statement.

**Table of Contents****NEW PEOPLES BANKSHARES, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****FOR THE SIX MONTHS ENDED JUNE 30, 2011 AND 2010**

(IN THOUSANDS)

(UNAUDITED)

	2011	2010
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income (loss)	\$ (1,126)	\$ 655
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation	1,245	1,383
Provision for loan losses	3,457	3,940
Income (less expenses) on life insurance	(176)	(209)
Loss on sale of fixed assets	152	
Loss on sale of foreclosed real estate	47	36
Adjustment of carrying value of foreclosed real estate	1,869	
Accretion of bond premiums/discounts	4	
Deferred tax expense	631	735
Amortization of core deposit intangible	58	109
Net change in:		
Interest receivable	332	(71)
Other assets	(2,452)	(1,811)
Accrued interest payable	75	(37)
Accrued expenses and other liabilities	(325)	314
Net Cash Provided by Operating Activities	3,791	5,044
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Net decrease in loans	30,655	11,478
Purchase of securities available-for-sale	(2,455)	(1,654)
Proceeds from sale and maturities of securities available-for-sale	2,853	613
Sale of Federal Home Loan Bank stock	145	
Purchase of Federal Reserve Bank stock		1
Payments for the purchase of property and equipment	(1,204)	(1,269)
Proceeds from sales of property and equipment	168	
Proceeds from sales of other real estate owned	2,655	1,559
Net Cash Provided by Investing Activities	32,817	10,728
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net decrease in line of credit borrowings	(4,900)	
Net increase in other borrowings	5,200	
Repayments to Federal Home Loan Bank	(5,600)	(600)
Net change in:		
Demand deposits	10,544	23,544
Savings deposits	(8,127)	(728)
Time deposits	(27,344)	(21,436)
Net Cash Provided by (Used in) Financing Activities	(30,227)	780

Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

Net increase in cash and cash equivalents	6,381	16,552
Cash and Cash Equivalents, Beginning of Period	82,529	39,560
Cash and Cash Equivalents, End of Period	\$ 88,910	\$ 56,112
Supplemental Disclosure of Cash Paid During the Period for:		
Interest	\$ 5,441	\$ 7,500
Taxes	\$	\$
Supplemental Disclosure of Non Cash Transactions:		
Other real estate acquired in settlement of foreclosed loans	\$ 3,362	\$ 5,897
Loans made to finance sale of foreclosed real estate	\$	\$ 175

The accompanying notes are an integral part of this statement.

---

**Table of Contents**

**NEW PEOPLES BANKSHARES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 NATURE OF OPERATIONS:**

New Peoples Bankshares, Inc. ( The Company ) is a bank holding company whose principal activity is the ownership and management of a community bank. New Peoples Bank, Inc. ( Bank ) was organized and incorporated under the laws of the Commonwealth of Virginia on December 9, 1997. The Bank commenced operations on October 28, 1998, after receiving regulatory approval. As a state chartered member bank, the Bank is subject to regulation by the Virginia Bureau of Financial Institutions, the Federal Deposit Insurance Corporation and the Federal Reserve Bank. The Bank provides general banking services to individuals, small and medium size businesses and the professional community of southwestern Virginia, southern West Virginia, and eastern Tennessee. On June 9, 2003, the Company formed two wholly owned subsidiaries, NPB Financial Services, Inc. and NPB Web Services, Inc. On July 7, 2004 the Company established NPB Capital Trust I for the purpose of issuing trust preferred securities. On September 27, 2006, the Company established NPB Capital Trust 2 for the purpose of issuing additional trust preferred securities. NPB Financial Services, Inc. was a subsidiary of the Company until January 1, 2009 when it became a subsidiary of the Bank.

**NOTE 2 ACCOUNTING PRINCIPLES:**

The financial statements conform to U. S. generally accepted accounting principles and to general industry practices. In the opinion of management, the accompanying unaudited financial statements contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly the financial position at June 30, 2011, and the results of operations for the three month and six month periods ended June 30, 2011 and 2010. The notes included herein should be read in conjunction with the notes to financial statements included in the Company s Annual Report on Form 10-K/A Amendment No. 2 for the year ended December 31, 2010. The results of operations for the three month and six month periods ended June 30, 2011 and 2010 are not necessarily indicative of the results to be expected for the full year.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, 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. Actual results could differ from those estimates. The determination of the adequacy of the allowance for loan losses is based on estimates that are particularly susceptible to significant changes in the economic environment and market conditions.

**NOTE 3 FORMAL WRITTEN AGREEMENT:**

Effective July 29, 2010, the Company and the Bank entered into a written agreement with the Federal Reserve Bank of Richmond ( Reserve Bank ) and the Virginia State Corporation Commission Bureau of Financial Institutions (the Bureau ) called (the Written Agreement ). We believe we have made good progress in our compliance efforts under the Written Agreement and all of the written plans required to date, as discussed in the following paragraphs, have been submitted on a timely basis.

Under the terms of the Written Agreement, the Bank has agreed to develop and submit for approval within specified time periods written plans to: (a) strengthen board oversight of management and the Bank s operation; (b) if appropriate after review, to strengthen the Bank s management and board governance; (c) strengthen credit risk management policies; (d) enhance lending and credit administration; (e) enhance the Bank s management of commercial real estate concentrations; (f) conduct ongoing review and grading of the Bank s loan portfolio; (g) improve the Bank s position with respect to loans, relationships, or other assets in excess of \$1 million which are now or in the future become past due more than 90 days, which are on the Bank s problem loan list, or which are adversely classified in any report of examination of the Bank; (h) review and revise, as appropriate, current policy and maintain sound processes for maintaining an adequate allowance for loan and lease losses; (i) enhance management of the Bank s liquidity position and funds management practices; (j) revise its contingency funding plan; (k) revise its strategic plan; and (l) enhance the Bank s anti-money laundering and related activities.

In addition, the Bank has agreed that it will: (a) not extend, renew, or restructure any credit that has been criticized by the Reserve Bank or the Bureau absent prior board of directors approval in accordance with the restrictions in the Written Agreement; (b) eliminate all assets or portions of assets classified as loss and thereafter charge off all assets classified as loss in a federal or state report of examination, unless otherwise approved by the Reserve Bank.

## Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

Under the terms of the Written Agreement, both the Company and the Bank have agreed to submit capital plans to maintain sufficient capital at the Company, on a consolidated basis, and the Bank, on a stand-alone basis, and to refrain from declaring or paying dividends without prior regulatory approval. The Company has agreed that it will not take any

**Table of Contents****NEW PEOPLES BANKSHARES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)****NOTE 3 FORMAL WRITTEN AGREEMENT (CONTINUED):**

other form of payment representing a reduction in the Bank's capital or make any distributions of interest, principal, or other sums on subordinated debentures or trust preferred securities without prior regulatory approval. The Company may not incur, increase or guarantee any debt without prior regulatory approval and has agreed not to purchase or redeem any shares of its stock without prior regulatory approval.

Under the terms of the Written Agreement, the Company and the Bank have appointed a committee to monitor compliance with the Written Agreement. The directors of the Company and the Bank have recognized and unanimously agree with the common goal of financial soundness represented by the Written Agreement and have confirmed the intent of the directors and executive management to diligently seek to comply with all requirements of the Written Agreement.

**NOTE 4 CAPITAL REQUIREMENTS:**

The Company and the Bank are subject to various capital requirements administered by federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and, possibly, additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier 1 capital (as defined) to risk-weighted assets (as defined) and of Tier 1 capital (as defined) to average assets (as defined). Management believes that, as of June 30, 2011, the Company and the Bank meet all capital adequacy requirements to which they are subject.

As of June 30, 2011 the Bank was well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following tables. There are no conditions or events since the notification that management believes have changed the Bank's category.

The Company's and the Bank's actual capital amounts and ratios are presented in the table as of June 30, 2011 and December 31, 2010, respectively.

(Dollars are in thousands)	Actual		Minimum Capital Requirement		Minimum to Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
<b>June 30, 2011:</b>						
Total Capital to Risk Weighted Assets:						
The Company	\$ 51,988	9.35%	\$ 44,496	8%	\$ N/A	N/A
The Bank	56,651	10.21%	44,384	8%	55,480	10%
Tier 1 Capital Risk Weighted Assets:						
The Company	39,615	7.12%	22,248	4%	N/A	N/A
The Bank	49,571	8.93%	22,192	4%	33,288	6%
Tier 1 Capital to Average Assets:						

Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

The Company	39,615	4.74%	33,409	4%	N/A	N/A
The Bank	49,571	5.97%	33,194	4%	41,492	5%
<b>December 31, 2010:</b>						
Total Capital to Risk Weighted Assets:						
The Company	\$ 53,020	8.87%	\$ 47,825	8%	\$ N/A	N/A
The Bank	58,466	9.79%	47,786	8%	59,732	10%
Tier 1 Capital Risk Weighted Assets:						
The Company	39,108	6.54%	23,913	4%	N/A	N/A
The Bank	50,777	8.50%	23,893	4%	35,839	6%
Tier 1 Capital to Average Assets:						
The Company	39,108	4.62%	33,857	4%	N/A	N/A
The Bank	50,777	6.00%	33,857	4%	42,321	5%



**Table of Contents****NEW PEOPLES BANKSHARES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)****NOTE 5 INVESTMENT SECURITIES:**

The amortized cost and estimated fair value of securities are as follows:

(Dollars are in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Value
<b>June 30, 2011</b>				
<u>Available for Sale</u>				
U.S. Government Agencies	\$ 2,707	\$ 37	\$	\$ 2,744
Taxable municipals	893	52		945
US. Government Mortgage backed securities	674	20		694
<b>Total Securities AFS</b>	<b>\$ 4,274</b>	<b>\$ 109</b>	<b>\$</b>	<b>\$ 4,383</b>
<b>December 31, 2010</b>				
<u>Available for Sale</u>				
U.S. Government Agencies	\$ 3,001	\$	\$ 31	\$ 2,970
Taxable municipals	894	5		899
U.S. Government Mortgage backed securities	781	8		789
<b>Total Securities AFS</b>	<b>\$ 4,676</b>	<b>\$ 13</b>	<b>\$ 31</b>	<b>\$ 4,658</b>

The following table details unrealized losses and related fair values in the available for sale portfolio. This information is aggregated by the length of time that individual securities have been in a continuous unrealized loss position as of June 30, 2011 and December 31, 2010.

(Dollars are in thousands)	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<b>June 30, 2011</b>						
U.S. Government Agencies	\$	\$	\$	\$	\$	\$
<b>December 31, 2010</b>						
U.S. Government Agencies	\$ 2,970	\$ 31	\$	\$	\$ 2,970	\$ 31

At June 30, 2011, the available for sale portfolio had no investments for which the fair market value was less than amortized cost. At December 31, 2010, the available for sale portfolio included four investments for which the fair market value was less than amortized cost. No securities had an other than temporary impairment.

The amortized cost and fair value of investment securities at June 30, 2011, by contractual maturity, are shown in the following schedule. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

## Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

(Dollars are in thousands)

Securities Available for Sale	Amortized Cost	Fair Value	Weighted Average Yield
Due in one year or less	\$	\$	%
Due after one year through five years	231	236	3.14%
Due after five years through fifteen years	4,043	4,147	3.50%
 Total	 \$ 4,274	 \$ 4,383	 3.46%

Investment securities with a carrying value of \$1.2 million and \$892 thousand at June 30, 2011 and December 31, 2010, were pledged to secure public deposits and for other purposes required by law.

The Bank, as a member of the Federal Reserve Bank and the Federal Home Loan Bank, is required to hold stock in each. These equity securities are restricted from trading and are recorded at a cost of \$3.7 million and \$3.9 million as of June 30, 2011 and December 31, 2010, respectively.

**Table of Contents****NEW PEOPLES BANKSHARES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)****NOTE 6 LOANS:**

Loans receivable outstanding are summarized as follows:

(Dollars are in thousands)	June 30, 2011	December 31, 2010
Commercial, financial and agricultural	\$ 98,365	\$ 109,551
Real estate-construction	44,872	52,307
Real estate-mortgages	473,814	489,314
Installment loans to individuals	46,952	56,622
<b>Total loans</b>	<b>\$ 664,003</b>	<b>\$ 707,794</b>

The following table presents information concerning the Company's investment in loans considered impaired as of June 30, 2011 and December 31, 2010:

**As of June 30, 2011**

(Dollars are in thousands)	Average Recorded Investment	Interest Income Recognized	Recorded Investment	Unpaid Principal Balance	Related Allowance
<b>With no related allowance recorded:</b>					
Commercial, financial and agricultural	\$ 14,062	\$ 322	\$ 16,934	\$ 17,712	\$
Real estate-construction	13,672	128	14,768	23,735	
Real Estate-mortgages	34,413	857	40,827	44,103	
Installment loans to individuals	1		4	4	
<b>With an allowance recorded:</b>					
Commercial, financial and agricultural	6,104	90	3,650	3,824	1,256
Real estate-construction	7,275	50	3,963	4,306	1,632
Real Estate-mortgages	13,533	254	10,357	10,642	1,735
Installment loans to individuals	38	1	26	27	7
<b>Total</b>	<b>\$ 89,098</b>	<b>\$ 1,702</b>	<b>\$ 90,529</b>	<b>\$ 104,353</b>	<b>\$ 4,630</b>

**As of December 31, 2010**

(Dollars are in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance
<b>With no related allowance recorded:</b>			
Commercial, financial and agricultural	\$ 9,264	\$ 9,785	\$
Real estate-construction	8,585	12,594	
Real Estate-mortgages	27,138	27,997	
Installment loans to individuals			
<b>With an allowance recorded:</b>			
Commercial, financial and agricultural	11,729	11,729	4,042
Real estate-construction	14,913	16,253	3,926
Real Estate-mortgages	18,973	19,142	4,842

## Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

Installment loans to individuals	46	46	23
<b>Total</b>	<b>\$ 90,648</b>	<b>\$ 97,546</b>	<b>\$ 12,833</b>

The average recorded investment in impaired loans was \$63.4 million for the year ended December 31, 2010.

Loans receivable on nonaccrual status are summarized as follows:

	June 30, 2011	December 31, 2010
(Dollars are in thousands)		
<b>Commercial, financial and agricultural</b>	<b>\$ 11,544</b>	<b>\$ 5,970</b>
Real estate-construction	12,239	15,460
<b>Real estate-mortgages</b>	<b>18,889</b>	<b>22,986</b>
Installment loans to individuals	324	1,365
<b>Total loans receivable on nonaccrual status</b>	<b>\$ 42,996</b>	<b>\$ 45,781</b>

Total interest income not recognized on nonaccrual loans for six months ended June 30, 2011 and 2010 was \$1.1 million and \$309 thousand, respectively.

**Table of Contents****NEW PEOPLES BANKSHARES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)****NOTE 6 LOANS (CONTINUED):**

An age analysis of past due loans receivable was as follows:

	Loans					Accruing
	Loans	90 or	Total			Loans
	30-89	More	Past			90 or
	Days	Days	Past			More
	Past	Past	Due	Current	Total	Past
	Due	Due	Loans	Loans	Loans	Due
<b>As of June 30, 2011</b>						
(Dollars are in thousands)						
Commercial, financial and agricultural	\$ 4,257	\$ 9,855	\$ 14,112	\$ 84,253	\$ 98,365	\$ 446
Real estate-construction	3,628	9,394	13,022	31,850	44,872	
Real Estate-mortgages	19,305	11,355	30,660	443,154	473,814	1,598
Installment loans to individuals	1,276	533	1,809	45,143	46,952	309
<b>Total</b>	<b>\$ 28,466</b>	<b>\$ 31,137</b>	<b>\$ 59,603</b>	<b>\$ 604,400</b>	<b>\$ 664,003</b>	<b>\$ 2,353</b>

	Loans					Accruing
	Loans	90 or	Total			Loans
	30-89	More	Past			90 or
	Days	Days	Past			More
	Past	Past	Due	Current	Total	Past
	Due	Due	Loans	Loans	Loans	Due
<b>As of December 31, 2010</b>						
(Dollars are in thousands)						
Commercial, financial and agricultural	\$ 5,622	\$ 2,690	\$ 8,312	\$ 101,239	\$ 109,551	\$ 90
Real estate-construction	2,079	8,150	10,229	42,078	52,307	
Real Estate-mortgages	22,251	12,227	34,478	454,836	489,314	1,332
Installment loans to individuals	2,584	337	2,921	53,701	56,622	270
<b>Total</b>	<b>\$ 32,536</b>	<b>\$ 23,404</b>	<b>\$ 55,940</b>	<b>\$ 651,854</b>	<b>\$ 707,794</b>	<b>\$ 1,692</b>

The Company categorizes loans receivable 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, among other factors. The Company analyzes loans and leases individually by classifying the loans receivable as to credit risk. The Company uses the following definitions for risk ratings:

**Pass** - Loans in this category are considered to have a low likelihood of loss based on relevant information analyzed about the ability of the borrowers to service their debt and other factors.

**Special Mention** - Loans in this category are currently protected but are potentially weak, including adverse trends in borrower's operations, credit quality or financial strength. Those loans constitute an undue and unwarranted credit risk but not to the point of justifying a substandard classification. The credit risk may be relatively minor yet constitute an unwarranted risk in light of the circumstances. Special mention loans

## Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

have potential weaknesses which may, if not checked or corrected, weaken the loan or inadequately protect the Company's credit position at some future date.

**Substandard** - A substandard loan is inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified as substandard must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt; they are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

**Doubtful** - Loans classified Doubtful have all the weaknesses inherent in loans classified Substandard, plus 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.

Based on the most recent analysis performed, the risk category of loans receivable was as follows:

### As of June 30, 2011

(Dollars are in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Commercial, financial and agricultural	\$ 68,631	\$ 8,906	\$ 18,304	\$ 2,524	\$ 98,365
Real estate-construction	25,638	4,158	15,076		44,872
Real Estate-mortgages	375,388	30,728	63,560	4,138	473,814
Installment loans to individuals	44,720	632	1,560	40	46,952
<b>Total</b>	<b>\$ 514,377</b>	<b>\$ 44,424</b>	<b>\$ 98,500</b>	<b>\$ 6,702</b>	<b>\$ 664,003</b>

**Table of Contents****NEW PEOPLES BANKSHARES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)****NOTE 6 LOANS (CONTINUED):****As of December 31, 2010**

(Dollars are in thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Commercial, financial and agricultural	\$ 83,482	\$ 5,561	\$ 18,619	\$ 1,889	\$ 109,551
Real estate-construction	28,802	4,095	19,410		52,307
Real Estate-mortgages	418,166	20,113	47,389	3,646	489,314
Installment loans to individuals	56,037	122	434	29	56,622
<b>Total</b>	<b>\$ 586,487</b>	<b>\$ 29,891</b>	<b>\$ 85,852</b>	<b>\$ 5,564</b>	<b>\$ 707,794</b>

At June 30, 2011 there were \$19.2 million in loans that are classified as troubled debt restructurings compared to \$13.9 million at December 31, 2010.

**NOTE 7 ALLOWANCE FOR LOAN LOSSES:**

A summary of transactions in the allowance for loan losses is as follows:

(Dollar are in thousands)	For the Six Months Ended	
	June 30, 2011	June 30, 2010
Balance, beginning of year	\$ 25,014	\$ 18,588
Provision for loan losses	3,457	3,940
Advances made on loans with off balance sheet provision	153	
Recoveries of loans charged off	1,059	66
Loans charged off	(10,986)	(6,167)
 Balance, End of period	 \$ 18,697	 \$ 16,427
 Percentage of Loans	 2.82%	 2.22%

The following table details activity in the allowance for loan losses by portfolio segment for the periods ended June 30, 2011 and December 31, 2010. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

**As of June 30, 2011**

(Dollars are in thousands)	Commercial, Financial and Agricultural	Real Estate Construction	Real Estate Mortgages	Installment Loans to Individuals	Unallocated	Total
Allowance for loan losses:						
Beginning balance	\$ 5,323	\$ 4,913	\$ 6,882	\$ 1,733	\$ 6,163	\$ 25,014
Charge offs	(2,208)	(3,965)	(3,480)	(1,333)		(10,986)
Recoveries	39	707	217	96		1,059
Advances		153				153
Provisions	190	1,011	2,261	492	(497)	3,457

Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

Ending balance	\$	3,344	\$	2,819	\$	5,880	\$	988	\$	5,666	\$	18,697
----------------	----	-------	----	-------	----	-------	----	-----	----	-------	----	--------

Ending balance allocated to:

Individually evaluated for impairment	\$	1,256	\$	1,632	\$	1,735	\$	7	\$		\$	4,630
---------------------------------------	----	-------	----	-------	----	-------	----	---	----	--	----	-------

Collectively evaluated for impairment		2,088		1,187		4,145		981		5,666		14,067
---------------------------------------	--	-------	--	-------	--	-------	--	-----	--	-------	--	--------

Ending balance	\$	3,344	\$	2,819	\$	5,880	\$	988	\$	5,666	\$	18,697
----------------	----	-------	----	-------	----	-------	----	-----	----	-------	----	--------

Loans ending balances:

Individually evaluated for impairment	\$	20,584	\$	18,731	\$	51,184	\$	30	\$		\$	90,529
---------------------------------------	----	--------	----	--------	----	--------	----	----	----	--	----	--------

Collectively evaluated for impairment		77,781		26,141		422,630		46,922				573,474
---------------------------------------	--	--------	--	--------	--	---------	--	--------	--	--	--	---------

Total	\$	98,365	\$	44,872	\$	473,814	\$	46,952	\$		\$	664,003
-------	----	--------	----	--------	----	---------	----	--------	----	--	----	---------



**Table of Contents****NEW PEOPLES BANKSHARES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)****NOTE 7 ALLOWANCE FOR LOAN LOSSES (CONTINUED):****As of December 31, 2010**

(Dollars are in thousands)	Commercial, Financial and Agricultural	Real Estate Construction	Real Estate Mortgages	Installment Loans to Individuals	Unallocated	Total
<b>Allowance for loan losses:</b>						
Beginning balance	\$ 1,710	\$ 8,036	\$ 3,525	\$ 1,501	\$ 3,816	\$ 18,588
Charge offs	(1,425)	(10,002)	(3,867)	(1,214)		(16,508)
Recoveries	509		7	90		606
Provisions	4,529	6,879	7,217	1,356	2,347	22,328
 Ending balance	 \$ 5,323	 \$ 4,913	 \$ 6,882	 \$ 1,733	 \$ 6,163	 \$ 25,014
<b>Ending balance allocated to:</b>						
Individually evaluated for impairment	\$ 4,042	\$ 3,926	\$ 4,842	\$ 23	\$	\$ 12,833
Collectively evaluated for impairment	1,281	987	2,040	1,710	6,163	12,181
 Ending balance	 \$ 5,323	 \$ 4,913	 \$ 6,882	 \$ 1,733	 \$ 6,163	 \$ 25,014
<b>Loans ending balances:</b>						
Individually evaluated for impairment	\$ 20,993	\$ 23,497	\$ 46,112	\$ 46	\$	\$ 90,648
Collectively evaluated for impairment	88,558	28,810	443,202	56,576		617,146
 Total	 \$ 109,551	 \$ 52,307	 \$ 489,314	 \$ 56,622	 \$	 \$ 707,794

In determining the amount of our allowance, we rely on an analysis of our loan portfolio, our experience and our evaluation of general economic conditions, as well as the requirements of the written agreement and other regulatory input. If our assumptions prove to be incorrect, our current allowance may not be sufficient to cover future loan losses and we may experience significant increases to our provision.

**NOTE 8 EARNINGS PER SHARE:**

Basic earnings per share computations are based on the weighted average number of shares outstanding during each year. Dilutive earnings per share reflect the additional common shares that would have been outstanding if dilutive potential common shares had been issued. Potential common shares that may be issued relate to outstanding options and are determined by the Treasury method. For the three and six month periods ended June 30, 2011 and 2010, potential common shares were anti-dilutive and were not included in the calculation. Basic and diluted net income per common share calculations follows:

(Amounts in Thousands, Except Share and Per Share Data)	For the three months ended June 30,		For the six months ended June 30,	
	2011	2010	2011	2010
Net income (loss)	\$ (1,675)	\$ 242	\$ (1,126)	\$ 655
Weighted average shares outstanding	10,010,178	10,009,042	10,010,178	10,009,039
Dilutive shares for stock options				

Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

Weighted average dilutive shares outstanding	10,010,178	10,009,042	10,010,178	10,009,039
Basic earnings (loss) per share	\$ (0.17)	\$ 0.02	\$ (0.11)	\$ 0.07
Diluted earnings (loss) per share	\$ (0.17)	\$ 0.02	\$ (0.11)	\$ 0.07

---

**Table of Contents**

**NEW PEOPLES BANKSHARES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**

**NOTE 9 FAIR VALUES:**

ASC 820, Fair Value Measurements and Disclosures provides a framework for measuring fair value under generally accepted accounting principles and requires disclosures about the fair value of assets and liabilities recognized in the balance sheet in periods subsequent to initial recognition, whether the measurements are made on a recurring basis (for example, available for sale investment securities) or on a nonrecurring basis (for example, impaired loans and other real estate acquired through foreclosure).

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Fair Value Measurements and Disclosures also establishes 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. The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include debt and equity securities and derivative contracts that are traded in an exchange market, as well as U. S. Treasury, other U. S. Government and agency mortgage-backed debt securities that are highly liquid and are actively traded in over-the-counter markets.

Level 2: 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 for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include debt securities with quoted prices that are traded less frequently than exchange-traded instruments and derivative contracts whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. For example, this category generally includes certain private equity investments, retained residual interests in securitizations, residential mortgage servicing rights, and highly structured or long-term derivative contracts.

*Investment Securities Available for Sale* - Investment securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices. The Company's available for sale securities, totaling \$4.4 million and \$4.7 million at June 30, 2011 and December 31, 2010, respectively, are the only assets whose fair values are measured on a recurring basis using Level 2 inputs from an independent pricing service.

*Loans* - The Company does not record loans at fair value on a recurring basis. The Company is predominantly an asset based lender with real estate serving as collateral on a substantial majority of loans. From time to time a loan is considered impaired and an allowance for loan losses is established. Loans which are deemed to be impaired are primarily valued on a non-recurring basis at the fair values of the underlying real estate collateral. Such fair values are obtained using independent appraisals, which management used to determine the current value of the collateral. If further impairment below the appraised value is warranted based on changes in market conditions and there is no observable market price, or an appraised value does not include estimated costs of disposition, then management must make an estimate of these costs. In that case, the Company records the impaired loan as nonrecurring Level 3. The aggregate carrying amounts of impaired loans were \$90.5 million and \$90.6 million at June 30, 2011 and December 31, 2010, respectively.

*Foreclosed Assets* - Foreclosed assets are adjusted to fair value upon transfer of the loans to foreclosed assets. Foreclosed assets are carried at the lower of the carrying value or fair value. Fair value is based upon independent observable market prices or appraised values of the collateral with a third party estimate of disposition costs, which the Company considers to be level 2 inputs. When the appraised value is not available, management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, or an appraised value does not include estimated costs of disposition and management must make an estimate, the Company records the foreclosed asset as nonrecurring Level 3.



**Table of Contents****NEW PEOPLES BANKSHARES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)****NOTE 9 FAIR VALUES (CONTINUED):**

Assets and liabilities measured at fair value are as follows as of June 30, 2011:

(Dollars are in thousands) (On a recurring basis)	Quoted market price in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Available for sale investments			
U.S. Government Agencies	\$	\$ 2,744	\$
Taxable municipals		945	
Mortgage backed securities (On a non-recurring basis)		694	
Other real estate owned			11,137
Impaired loans			
Commercial, financial and agricultural			20,584
Real estate-construction			18,731
Real estate-mortgages			51,184
Installment loans to individuals			30
<b>Total</b>	<b>\$</b>	<b>\$ 4,383</b>	<b>\$ 101,666</b>

Assets and liabilities measured at fair value are as follows as of December 31, 2010:

(Dollars are in thousands) (On a recurring basis)	Quoted market price in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Available for sale investments			
U.S. Government Agencies	\$	\$ 2,970	\$
Taxable municipals		899	
Mortgage backed securities (On a non-recurring basis)		789	
Other real estate owned			12,346
Impaired loans			
Commercial, financial and agricultural			20,993

Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

Real estate-construction				23,497
Real estate-mortgages				46,112
Installment loans to individuals				46
<b>Total</b>	<b>\$</b>	<b>\$</b>	<b>4,658</b>	<b>\$ 102,994</b>

For the six months ended June 30, 2011 and 2010, the changes in other real estate owned Level 3 assets measured at fair value on a nonrecurring basis are summarized as follows (dollars in thousands):

(Dollars are in thousands)	June 30, 2011 Other Real Estate Owned	June 30, 2010 Other Real Estate Owned
Balance, January 1	\$ 12,346	\$ 3,675
Acquired in settlement of loans	3,362	5,861
Proceeds from sale of other real estate owned	(2,655)	(1,559)
Gain (Loss) on sale of other real estate owned	(47)	(36)
Adjustments to carrying value	(1,869)	
 Balance, June 30	 \$ 11,137	 \$ 7,941

**Table of Contents****NEW PEOPLES BANKSHARES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)****NOTE 9 FAIR VALUES (CONTINUED):****Fair Value of Financial Instruments**

Fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practical to estimate the value is based upon the characteristics of the instruments and relevant market information. Financial instruments include cash, evidence of ownership in an entity, or contracts that convey or impose on an entity that contractual right or obligation to either receive or deliver cash for another financial instrument.

The following summary presents the methodologies and assumptions used to estimate the fair value of the Company's financial instruments presented below. The information used to determine fair value is highly subjective and judgmental in nature and, therefore, the results may not be precise. Subjective factors include, among other things, estimates of cash flows, risk characteristics, credit quality, and interest rates, all of which are subject to change. Since the fair value is estimated as of the balance sheet date, the amounts that will actually be realized or paid upon settlement or maturity on these various instruments could be significantly different.

The carrying value of cash and due from banks, federal funds sold, interest-bearing deposits, deposits with no stated maturities, trust preferred securities and accrued interest approximates fair value. The estimated fair value of investment securities was based on closing market prices. The remaining financial instruments were valued based on the present value of estimated future cash flows, discounted at various rates in effect for similar instruments during the months of June 2011 and December 2010.

(Dollars are in thousands)	June 30, 2011		December 31, 2010	
	Estimated Fair Value	Carrying Value	Estimated Fair Value	Carrying Value
<b><u>Financial Assets</u></b>				
Cash and due from bank	\$ 18,818	\$ 18,818	\$ 14,369	\$ 14,369
Interest bearing deposits with banks	69,082	69,082	42,549	42,549
Federal funds sold	1,010	1,010	25,611	25,611
Investment securities	4,383	4,383	4,658	4,658
Equity securities (restricted)	3,733	3,733	3,878	3,878
Net Loans	648,980	645,306	700,420	682,780
Accrued Interest receivable	3,368	3,368	3,700	3,700
Life insurance investments	11,187	11,187	11,011	11,011
<b><u>Financial Liabilities</u></b>				
<b><u>Demand Deposits</u></b>				
Non-interest bearing	102,343	102,343	87,839	87,839
Interest-bearing	56,062	56,062	60,022	60,022
Savings deposits	99,992	99,992	108,119	108,119
Time deposits	485,889	482,756	513,090	510,100
FHLB advances	18,156	18,583	23,611	24,183
Accrued interest payable	1,795	1,795	1,720	1,720
Line of credit borrowing			4,900	4,900
Other borrowings	5,450	5,450	250	250
Trust preferred securities	16,496	16,496	16,496	16,496

**NOTE 10 RECENT ACCOUNTING DEVELOPMENTS:**

## Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

The following is a summary of recent authoritative announcements:

In July 2010, the Receivables topic of the Accounting Standards Codification ( ASC ) was amended by Accounting Standards Update ( ASU ) 2010-20 to require expanded disclosures related to a company s allowance for credit losses and the credit quality of its financing receivables. The amendments require the allowance disclosures to be provided on a disaggregated basis. The Company is required to include these disclosures in their interim and annual financial statements. See Notes 6 and 7 to the consolidated financial statements for the required disclosures.



**Table of Contents**

**NEW PEOPLES BANKSHARES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**

**NOTE 10 RECENT ACCOUNTING DEVELOPMENTS (CONTINUED):**

Disclosures about Troubled Debt Restructurings ( TDRs ) required by ASU 2010-20 were deferred by the Financial Accounting Standards Board ( FASB ) in ASU 2011-01 issued in January 2011. In April 2011 FASB issued ASU 2011-02 to assist creditors with their determination of when a restructuring is a TDR. The determination is based on whether the restructuring constitutes a concession and whether the debtor is experiencing financial difficulties as both events must be present.

Disclosures related to TDRs under ASU 2010-20 will be effective for reporting periods beginning after June 15, 2011, but are not expected to have a material effect on the financial statements.

In December 2010, the Intangibles topic of the ASC was amended to modify Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. Any resulting goodwill impairment should be recorded as a cumulative-effect adjustment to beginning retained earnings upon adoption. Impairments occurring subsequent to adoption should be included in earnings. The amendment is effective for the Company beginning January 1, 2011, but is not expected to have a material effect on the financial statements. Early adoption is not permitted.

In April 2011, the criteria used to determine effective control of transferred assets in the Transfers and Servicing topic of the ASC was amended by ASU 2011-03. The requirement for the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms and the collateral maintenance implementation guidance related to that criterion were removed from the assessment of effective control. The other criteria to assess effective control were not changed. The amendments are effective for the Company beginning January 1, 2012 but are not expected to have a material effect on the financial statements.

ASU 2011-04 was issued in May 2011 to amend the Fair Value Measurement topic of the ASC by clarifying the application of existing fair value measurement and disclosure requirements and by changing particular principles or requirements for measuring fair value or for disclosing information about fair value measurements. The amendments will be effective for the Company beginning January 1, 2012 but are not expected to have a material effect on the financial statements.

The Comprehensive Income topic of the ASC was amended in June 2011. The amendment eliminates the option to present other comprehensive income as a part of the statement of changes in stockholders' equity. The amendment requires consecutive presentation of the statement of net income and other comprehensive income and requires an entity to present reclassification adjustments from other comprehensive income to net income on the face of the financial statements. The amendments will be applicable to the Company on January 1, 2012 and will be applied retrospectively.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company's financial position, results of operations or cash flows.

---

## **Table of Contents**

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

#### **Caution About Forward Looking Statements**

We make forward looking statements in this quarterly report that are subject to risks and uncertainties. These forward looking statements include statements regarding our profitability, liquidity, allowance for loan losses, interest rate sensitivity, market risk, business strategy, and financial and other goals. The words believes, expects, may, will, should, projects, contemplates, anticipates, forecasts, intends, or other terms are intended to identify forward looking statements.

Certain information contained in this discussion may include forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements contain the Company's expectations, plans, future financial performance, and other statements that are not historical facts. These forward-looking statements are generally identified by phrases such as the Company expects, the Company believes or words of similar importance. Such forward-looking statements involve known and unknown risks including, but not limited to, changes in general economic and business conditions, interest rate fluctuations, competition within and from outside the banking industry, new products and services in the banking industry, risk inherent in making loans such as repayment risks and fluctuating collateral values, problems with technology utilized by the Company, changing trends in customer profiles and changes in laws and regulations applicable to the Company. Although the Company believes that its expectations with respect to the forward-looking statements are based upon reasonable assumptions within the bounds of its knowledge of its business and operations, there can be no assurance that actual results, performance or achievements of the Company will not differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements.

Because of these uncertainties, our actual future results may be materially different from the results indicated by these forward looking statements. In addition, our past results of operations do not necessarily indicate our future results.

#### **Overview**

The Company had a net loss for the quarter ended June 30, 2011 of \$1.7 million as compared to net income of \$242 thousand for the quarter ended June 30, 2010. Year-to-date June 30, 2011, the Company had a net loss of \$1.1 million as compared to net income of \$655 thousand for the same period in 2011. Basic net loss per share was \$0.17 for the quarter ended June 30, 2011 as compared to basic net income of \$0.02 for the quarter ended June 30, 2010. Basic net loss per share was \$0.11 for the six months ended June 30, 2011 as compared to net income per share of \$0.07 for the six months ended June 30, 2010. The net loss is primarily the result of other real estate owned property write-downs in the second quarter 2011 totaling \$1.9 million of which \$1.8 million of this amount is related to a single property market value depreciation in a development property in the coastal Carolina area. In addition, we made additional provisions for loan losses totaling \$2.3 million in the second quarter of 2011 as a result of additional impairments on troubled credits, one totaling \$1.4 million in the Coastal Carolina area, and net charge-offs realized in the quarter.

Total assets decreased to \$821.1 million, or 3.70%, from \$852.6 million at December 31, 2010. We intentionally are reducing our asset size in an attempt to manage our net interest margin by reducing higher cost funding and to improve our capital position. We foresee total assets to remain around the current level in the near future; however, future reductions may occur to maintain a well-capitalized status under regulatory guidelines.

In the second quarter of 2011, we experienced a decrease in our net interest margin to 4.28%, as compared to 4.45% for the same period in 2010. This is reflected in the \$627 thousand decrease in net interest income during the second quarter of 2011 as compared to the same period in 2010 primarily related to increased nonaccrual loans in 2011 and less earning assets.

The provision for loan losses increased \$362 thousand, or 18.56%, to \$2.3 million for the second quarter of 2011 as compared to \$2.0 million in the same period for 2010. At June 30, 2011 our allowance for loan losses totaled \$18.7 million, or 2.82% of total loans, as compared to \$25.0 million, or 3.53% of total loans at December 31, 2010. At June 30, 2010 our allowance for loan losses totaled \$16.4 million, or 2.22% of total loans. The allowance for loan losses are being maintained at a level that management deems appropriate to absorb any potential future losses and known impairments within the loan portfolio whether or not the losses are actually ever realized.

Total loans decreased to \$664.0 million at June 30, 2011 from \$707.8 million at year end 2010. This is the result of charge offs of \$11.0 million for the first six months of 2011, resolution of problem loans, and the intentional shrinking of the loan portfolio to increase regulatory capital ratios. We continue to serve our customers, and although the total loan portfolio has shrunk, we have renewed existing credits and have made new loans to qualified borrowers as well. We plan to decrease the loan portfolio in the near future as we reduce our exposure to certain risks and decrease nonperforming loans. Total deposits decreased \$24.9 million from \$766.1 million at December 31, 2010 to \$741.2 million at June 30,

## Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

2011 as two larger depositors and interest rate sensitive customers withdrew deposits to seek other investment opportunities. However, we continue to experience growth in core deposits through attractive consumer and commercial deposit products.

---

## **Table of Contents**

The deterioration of the residential and commercial real estate markets, as well as the extended recessionary period, have resulted in increases to our nonperforming assets. However, we are identifying potential problems early in an effort to minimize losses. The ratio of nonperforming assets to total assets is 6.88% at June 30, 2011 in comparison to 7.02% at December 31, 2010. Nonperforming assets, which include nonaccrual loans, other real estate owned and past due loans greater than 90 days still accruing interest, decreased to \$56.5 million at June 30, 2011 from \$59.8 million at December 31, 2010; however, as total assets have decreased during 2011, the June 30, 2011 ratio is higher than December 31, 2010. The majority of these assets are real estate development projects and commercial real estate secured loans. We are working aggressively to reduce these totals primarily by working with the customer for additional collateral, or restructuring the debt. However, we also may have to foreclose, repossess collateral or take other prudent measures. We are uncertain how long these processes will take. In the first six months of 2011, net charge offs were \$9.9 million as compared to \$6.1 million in the same period of 2010. The majority of the charge offs in the first six months of 2011 were related to real estate construction loans and commercial loans with collateral values that are dependent upon current market and economic conditions when these are ascertainable.

The Bank was well capitalized for regulatory purposes at June 30, 2011 as compared to adequately capitalized at December 31, 2010. The following ratios existed at June 30, 2011: Tier 1 leverage ratio of 5.97%, Tier 1 risk based capital ratio of 8.93%, and Total risk based capital ratio of 10.21%. The ratios were as follows at December 31, 2010: Tier 1 leverage ratio of 6.00%, Tier 1 risk based capital ratio of 8.50%, and Total risk based capital ratio of 9.79%.

### **Critical Accounting Policies**

Certain critical accounting policies affect the more significant judgments and estimates used in the preparation of our financial statements. The most critical accounting policy relates to our provision for loan losses, which reflects the estimated losses resulting from the inability of our customers to make required payments. If the financial condition of our borrowers were to further deteriorate, resulting in an impairment of their ability to make payments, our estimates would be updated, and additional provisions could be required. For further discussion of the estimates used in determining the allowance for loan losses, we refer you to the section on Provision for Loan Losses below. For discussion of our significant accounting policies see our Annual Report on Form 10-K/A Amendment No. 2 for the year ended December 31, 2010.

### **Balance Sheet Changes**

At June 30, 2011, total assets were \$821.1 million, a decrease of \$31.5 million, or 3.70%, from December 31, 2010. Total deposits decreased \$24.9 million, or 3.25%, for the first six months of 2011 to \$741.2 million from \$766.1 million at December 31, 2010. Total loans decreased \$43.8 million, or 6.19%, to \$664.0 million at June 30, 2011 from \$707.8 million at December 31, 2010.

We continue to experience an increase in core deposits as noninterest bearing deposits increased 16.51%, or \$14.5 million, from \$87.8 million at December 31, 2010 to \$102.3 million at June 30, 2011. This was partially offset by a \$4.0 million decrease in interest bearing demand deposits. Overall, we continue to experience growth in core deposits through attractive consumer and commercial deposit products.

We experienced a decrease in savings deposits of \$8.1 million and a decrease in time deposits of \$27.3 million. The decreases in savings and time deposits are due to customer desires to be more liquid in the current rate environment. During 2011, some larger liquid and rate sensitive deposits have withdrawn to seek other investment opportunities. We expect to continue to lose higher cost and rate sensitive deposits in the near future. However, we monitor deposits to ensure that we maintain adequate liquidity levels. We believe despite the deposit decrease, we have adequate liquidity.

Total loans decreased to \$664.0 million at June 30, 2011 from \$707.8 million at year end 2010. This is the result of charge offs of \$11.0 million for the first half of 2011 and resolution of problem loans. We plan to decrease the loan portfolio as we manage our capital levels to maintain a well-capitalized status, reduce certain risks to various industry sectors that have posed higher risks in recent times, and resolve nonperforming loans. Even as we decrease our loan portfolio, we still are committed to serving our customers. We have hired commercial lending personnel, continue to train our loan officers to meet the needs of our customers, and are developing new business with qualified borrowers that will ensure a stronger loan portfolio in the future.

## **Table of Contents**

### **Net Interest Income and Net Interest Margin**

Net interest income decreased \$627 thousand, or 7.19%, to \$8.1 million for the second quarter of 2011 from \$8.7 million for the same period in 2010. Our net interest margin decreased to 4.28% in the second quarter of 2011 as compared to 4.45% for the same period in 2010. This is the result of nonaccrual loans of \$43.0 million at June 30, 2011 which negatively affects the net interest margin as these loans are nonearning assets. If non-accruing loans increase, it may reduce our net interest margin further. We continue to manage our yields on assets and our costs of funds to improve the net interest margin.

### **Noninterest Income**

Noninterest income decreased \$179 thousand, or 12.67%, to \$1.2 million in the second quarter of 2011 from \$1.4 million in the same period in 2010. The decrease is the result of a \$96 thousand decrease in services charges on deposit accounts and a \$66 thousand decrease in insurance and investment fees. We expect noninterest income to remain flat throughout 2011 as a result of regulatory changes. During the third quarter 2011, we are increasing overdraft fees and some service charges. We continue to seek opportunities to improve noninterest income.

### **Noninterest Expense**

Noninterest expense totaled \$9.6 million for the second quarter of 2011 as compared to \$7.9 million for the second quarter of 2010. The primary contributors to the increase in noninterest expenses for the quarter are the increase in other real estate owned expenses of \$2.1 million, the increase in other operating expenses of \$94 thousand, offset by a decrease in FDIC insurance premiums of \$329 thousand. Other operating expenses increased mainly due to the result of complying with the terms of the Written Agreement entered into during 2010 and problem loan resolution expenses.

Salaries and benefits decreased \$73 thousand in the quarter-to-quarter comparison. We have decreased staffing during the first half of 2011 and in the subsequent period to improve earnings. In the future, we should continue to see improvements in salary and benefits expenses.

Our efficiency ratio, which is defined as noninterest expense divided by the sum of net interest income plus noninterest income, was 103.15% for the second quarter of 2011 as compared to 77.71% for the same period in 2010. This increase in the ratio is due primarily to the \$1.7 million increase in noninterest expenses for the quarter.

### **Provision for Loan Losses**

The calculation of the allowance for loan losses is considered a critical accounting policy. The adequacy of the allowance for loan losses is based upon management's judgment and analysis. The following factors are included in our evaluation of determining the adequacy of the allowance: risk characteristics of the loan portfolio, current and historical loss experience, concentrations and internal and external factors such as general economic conditions.

The allowance for loan losses decreased to \$18.7 million at June 30, 2011 as compared to \$25.0 million at December 31, 2010. The allowance for loan losses at June 30, 2011 was approximately 2.82% of total loans as compared to 3.53% at December 31, 2010 and 2.22% at June 30, 2010. Net loans charged off for the first six months of 2011 were \$9.9 million compared to \$6.1 million for the first six months of 2010. The provision for loan losses was \$2.3 million for the second quarter of 2011 as compared with \$2.0 million in the same period for 2010.

Certain risks exist in the Bank's loan portfolio. Historically, we have experienced significant annual loan growth until the past couple of years. However, there might be loans that have single pay maturities or demand loans that may be too new to have exhibited signs of weakness. Also, past expansions into new markets increase potential credit risk. A majority of our loans are collateralized by real estate located in our market area. It is our policy to sufficiently collateralize loans to help minimize loss exposures in case of default. The recent negative trends in the national real estate market and economy pose threats to our portfolio. With the exception of real estate development type properties which have experienced more deterioration in market values, the local residential and commercial real estate market values have shown some deterioration but remain relatively stable. National real estate markets have experienced a more significant downturn and this has impacted our portfolio for certain out-of-market loans in the Coastal Carolina, northeastern Tennessee, and eastern West Virginia markets. Prior to 2008, we had purchased participation construction loans in the Coastal Carolina area. The totals of these credits were \$5.9 million at June 30, 2011 and \$7.6 million at December 31, 2010. At June 30, 2011 \$1.3 million of the allowance for loan losses was allocated to these credits compared to \$1.2 million at December 31, 2010. The \$1.7 million decrease in these credits was the result of charge offs of \$1.6 million during the first six months of 2011. This market area poses higher risk to potential future writedowns if the real estate market conditions do not show improvements. It is uncertain as to when or if local real estate values will be more significantly impacted. We do not believe that there will be a severely negative effect in our market area, but because of the uncertainty we deem it prudent to assign more of



---

**Table of Contents**

the allowance to these types of loans. Our market area is somewhat diverse, but certain areas are more reliant upon agriculture, coal mining and natural gas. As a result, increased risk of loan impairments is possible if these industries experience a significant downturn, although we do not believe this to be likely at least in the near future. We consider these factors to be the primary higher risk characteristics of the loan portfolio.

An evaluation of individual loans is performed by the loan review function. Loans are initially risk rated by the originating loan officer. If deteriorations in the financial condition of the borrower and the capacity to repay the debt occur, along with other factors, the loan may be downgraded. This is typically determined by either the loan officer or loan reviewers. Guidance for the evaluation is established by the regulatory authorities who periodically review the Bank's loan portfolio for compliance. Classifications used by the Bank are exceptional, very good, standard, acceptable, transitory risk, other assets especially mentioned, substandard, doubtful and loss. For the year 2010 and 2011, we have engaged a third party loan review firm to conduct quarterly loan reviews.

All loans classified as special mention, substandard, doubtful and loss are individually reviewed for impairment. In determining impairment, collateral for loans classified as substandard, doubtful and loss is reviewed to determine if the collateral is sufficient for each of these credits. If an appraisal is older than one year, a new external certified appraisal is obtained in most cases and used to determine impairment. If an exposure exists, a specific allowance is directly made for the amount of the potential loss in addition to estimated liquidation and disposal costs. The evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. Impaired loans decreased to \$90.5 million with a valuation allowance of \$4.6 million at June 30, 2011 as compared to \$90.6 million with a valuation allowance of \$12.8 million at December 31, 2010. Of the \$90.5 million recorded as impaired loans, \$35.7 million were nonperforming loans, which includes nonaccrual loans and past due 90 days or more and still accruing. We determined we had \$18.0 million in loans that required a valuation allowance of \$4.6 million at June 30, 2011. At December 31, 2010 we had \$45.7 million in loans that required a valuation allowance of \$12.8 million. The \$27.7 million decrease in loans requiring a valuation allowance was the result of \$8.1 million decrease in commercial loans, \$8.6 million decrease in real estate loans, and a decrease of \$11.0 million in real estate construction loans that required a valuation allowance. Management is aggressively working to reduce the impaired credits at minimal loss.

Loans delinquent greater than 90 days still accruing interest and loans in non-accrual status present higher risks. At June 30, 2011, there were 132 loans in non-accrual status totaling \$43.0 million, or 6.48% of total loans. At December 31, 2010, there were 113 loans in non-accrual status totaling \$45.8 million, or 6.47% of total loans. It is our policy to stop accruing interest on a loan, and to classify that loan as non-accrual, under the following circumstances: (a) whenever we are advised by the borrower that scheduled payment or interest payments cannot be met, (b) when our best judgment indicates that payment in full of principal and interest can no longer be expected, or (c) when any such loan or obligation becomes delinquent for 90 days unless it is both well secured and in the process of collection. At June 30, 2011 there were \$19.2 million in loans that are classified as troubled debt restructurings compared to \$13.9 million at December 31, 2010. There are also no loans identified as potential problem loans. We do not have any commitments to lend additional funds to non-performing debtors.

**Liquidity**

We closely monitor our liquidity and have increased liquid assets in the form of cash, due from banks, federal funds sold, and unpledged available for sale investments from \$86.3 million at December 31, 2010 to \$92.1 million at June 30, 2011. We plan to maintain surplus short-term assets at levels adequate to meet potential liquidity needs during 2011.

At June 30, 2011, all of our investments are classified as available-for-sale, providing an additional source of liquidity in the amount of \$3.2 million, which is net of those securities pledged as collateral. We anticipate developing an investment portfolio in the near future as we shrink our loan portfolio and increase deposits. This will primarily serve as a source of liquidity while yielding a higher return than other short term investment options, such as federal funds sold and overnight deposits with the Federal Reserve Bank. In the third quarter of 2011, we are required to pledge approximately \$13.0 million in securities or loans for our payment processing with the Federal Reserve Bank. We anticipate purchasing securities and reducing our overnight funds at the Federal Reserve Bank to meet this requirement.

Our loan to deposit ratio was 89.59% at June 30, 2011 and 92.39% at year end 2010. We anticipate this ratio to remain below 90% as we continue to decrease our loan portfolio throughout 2011. We can further lower the ratio as management deems appropriate by managing the rate of growth in our loan portfolio and by offering special promotions to entice new deposits. This can be done by changing interest rates charged or limiting the amount of new loans approved.

Available third party sources of liquidity remain intact at June 30, 2011 which includes the following: our line of credit with the Federal Home Loan Bank of Atlanta, the brokered certificates of deposit markets, internet certificates of deposit, and the discount window at the Federal Reserve Bank of Richmond.





## **Table of Contents**

At June 30, 2011, we had borrowings from the Federal Home Loan Bank totaling \$18.6 million as compared to \$24.2 million at December 31, 2010. The \$5.6 million decrease was due to a \$5.0 million term note which matured in January 2011 and we paid off this note with liquid funds and the remaining \$600 thousand decrease was due to regular monthly principal payments. Of these borrowings at June 30, 2011, none are overnight and subject to daily interest rate changes. Term notes of \$10.2 million mature in the year 2012 and we anticipate paying these off as liquidity is available to do so. Two additional borrowings totaling \$8.4 million have a maturity date in the year 2018, but reduce in principal amounts monthly. We also used our line of credit with the Federal Home Loan Bank to issue a letter of credit for \$7.0 million in 2008 and \$3.0 million in 2010 to the Treasury Board of Virginia for collateral on public funds. An additional \$39.5 million was available on June 30, 2011 on the \$68.1 million line of credit which is secured by a blanket lien on our residential real estate loans. Recently, the Federal Home Loan Bank conducted a collateral review indicating fewer exceptions and our available line of credit increased slightly to \$68.1 million at the end of the second quarter of 2011.

We have access to the brokered deposits market. Currently we have \$2.7 million in 10 year term time deposits comprised of \$3 thousand incremental deposits which yield an interest rate of 4.10%. We utilized this low cost source of funds to match funding for a 10 year balloon mortgage product. With the exception of CDARS time deposits, we have no other brokered deposits. Though this has not been a strategy in the past, we may utilize this source in the future as a lower cost source of funds.

We are a member of an internet certificate of deposit network whereby we may obtain funds from other financial institutions at auction. We may invest funds through this network as well. Currently, we only intend to use this source of liquidity in a liquidity crisis event.

In September 2009, the Bank obtained approval for the Federal Reserve Bank discount window for overnight funding needs. We may collateralize this line with investment securities and loans at our discretion and in July 2011 we pledged an investment security with a fair value of \$359 thousand at July 31, 2011 as collateral. We did not request funding as a result of this pledge and do not anticipate using this funding source except as a last resort.

Additional liquidity is expected to be provided by loan repayments and core deposit growth that will result from an increase in market share in our targeted trade area.

With the increased asset liquidity and other external sources of funding, we believe at the Bank level we have adequate liquidity and capital resources to meet our requirements and needs for the foreseeable future. However, liquidity can be further affected by a number of factors such as counterparty willingness or ability to extend credit, regulatory actions and customer preferences, some of which are beyond our control.

Concerning the Company's liquidity, we borrowed \$500 thousand from two directors at \$250 thousand each. One borrowing occurred at the end of 2010 and the other in January 2011. The use of these funds is to meet current liquidity needs of the Company. At December 31, 2010, there was a \$4.9 million Silverton line of credit that management was diligently working to eliminate and to increase liquidity at the Company level. As reported in the Subsequent Event Section in Item 1. Business of the December 31, 2010 10-K, on March 16, 2011 we received additional borrowings from two directors totaling \$4.95 million and were able to retire the Silverton line of credit that was to mature in June 2011 and we continue to work on enhancing the Company's liquidity.

## **Capital Resources**

Total capital at the end of the second quarter of 2011 was \$36.5 million as compared to \$37.5 million at the end of December 31, 2010. The decrease was due to the net loss of \$1.1 million for the first half of 2011. The Bank remains well capitalized at June 30, 2011, as defined by the capital guidelines of bank regulations. The Company's capital as a percentage of total assets was 4.44% at June 30, 2011 compared to 4.40% at December 31, 2010.

Our primary source of additional capital comes from retained earnings. We continue to implement and follow our strategic plan and capital plan. Under current economic conditions, we believe it is prudent to increase capital to absorb potential losses that may occur if asset quality deteriorates further. We are aware that capital needs and requirements are affected by the level of problem assets, growth, earnings and other factors. Retained earnings are not alone sufficient to provide for this economic cycle and we believe we will need access to additional sources of capital. As part of our initiative to improve regulatory capital ratios, we are reducing our higher risk assets, which results in a shrinking loan portfolio. Deposit growth is primarily focused on growing core deposits, which are mainly transaction accounts, commercial relationships and savings products. We are focused on improving earnings by maintaining a strong net interest margin and decreasing overhead expenses. These options we are fully implementing to increase capital. However, these efforts alone may not provide us adequate capital if further loan losses are realized. We are exploring a common stock offering.



**Table of Contents**

No cash dividends have been paid historically and none are anticipated in the foreseeable future. Earnings will continue to be retained to build capital.

**Off Balance Sheet Items and Contractual Obligations**

There have been no material changes during the quarter ended June 30, 2011 to the off-balance sheet items and the contractual obligations disclosed in our annual report on Form 10-K/A Amendment No. 2 for the fiscal year ended December 31, 2010.

---

## **Table of Contents**

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

There have been no material changes in market risks faced by the Company during the quarter ended June 30, 2011. For information regarding the Company's market risk, refer to the Company's Annual Report on Form 10-K/A Amendment No. 2 for the year ended December 31, 2010.

### **Item 4. Controls and Procedures**

We have carried out an evaluation, under the supervision and with the participation of our management, including our President and Chief Executive Officer (our CEO) and our Executive Vice President and Chief Financial Officer (our CFO), of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the period covered by this report. Based upon that evaluation, our CEO and CFO concluded that our disclosure controls and procedures were not operating effectively in providing reasonable assurance that (a) the information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and (b) such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure. Our CEO and CFO based this conclusion on the fact that the Company identified a material weakness in New Peoples' internal control over financial reporting relating to the system of monitoring the real estate collateral values of impaired loans and other real estate owned properties at the Bank and while internal control procedures have been implemented to remediate this material weakness, no testing has been performed to determine the effectiveness of the new procedures. Additional information with respect to this issue is included in the discussion below.

#### **Changes in Internal Control Over Financial Reporting**

During May 2011, after management discovered the material weakness in its internal control over financial reporting described above, management implemented the following internal control procedures to ensure timely reporting of changes in collateral values on impaired loans and other real estate owned properties at the Bank to management responsible for financial reporting of the Company:

1. A Disclosure Control Committee has been established consisting of the following officers: Chief Executive Officer, Chief Financial Officer, Chief Credit Officer, Chief Operating Officer, Senior Lending Officer, Controller, In-house Legal Counsel, and Director of Internal Audit. This Committee will meet quarterly to discuss loan portfolio and problem asset quality issues, operation risks, legal issues, subsequent events, suspicious activities, and reported disclosures.
2. The Chief Credit Officer (CCO) of the Bank is assigned the responsibility for monitoring all assets classified as impaired. The CCO will also be responsible for determining when appraisals or evaluations will be needed on impaired loans and other real estate owned properties, and for reporting any reductions in collateral values to the Chief Financial Officer (CFO) on a quarterly basis prior to the filing of the quarterly and annual reports with the SEC.
3. When appraisals are received from the third party appraisal firm, a copy of the appraisal will promptly be logged on a register designating the date of receipt and provided to the Loan Officer and the Loan Operations Department, with the Loan Officer responsible to promptly place the appraisal in the customer file, update valuations on the Bank's database and forward a copy to the CCO.
4. The independent appraisal review department of the Bank will immediately notify the CCO and the Loan Officer of the results of an appraisal on an impaired or suspected impaired loan or other real estate owned property. After the CCO and Loan Officer review the appraisal, a determination will be made as to the reasonableness of the appraisal. The final determination as to reasonableness will be the responsibility of the CCO. Upon a determination of reasonableness, then the CCO will notify the CFO, Controller and Allowance for Loan Loss model coordinator of any deterioration in the appraised value. A new impairment test will be performed and reviewed by the CCO and CFO to determine if an additional allowance reserve is needed for this credit relationship, which will be provided to the Controller to make general ledger adjustments and financial statement revisions prior to issuance.

Edgar Filing: NEW PEOPLES BANKSHARES INC - Form 10-Q

5. Prior to release of financial information, the CFO will contact the CCO to insure no appraisals have been received or are being reviewed, the result of which might be material to the financial statement of the Company.

---

**Table of Contents**

**Part II Other Information**

**Item 1. Legal Proceedings**

In the course of operations, we may become a party to legal proceedings. We became aware of a lawsuit against the Bank in April 2010. This case involves a claim against the Bank by a joint venture between bank customers, some of whom are former members of senior management, and three investors. The allegation is that the joint venture, VFI, should have priority over the Bank's deed of trust in order for VFI's unrecorded and unrecordable ground lease to be enforceable for its full ten year term. There are also additional claims for damages resulting from allegations that the Bank's representatives imputed liability to the Bank based upon breach of fiduciary duty, fraud, and collaboration. The parties agreed to litigate the ground lease issue first and are now in negotiations to resolve all pending issues due to the fact that the business associated with the building has ceased and the building is vacant. Management and Bank's counsel believe VFI's position is not supported by law or the facts presented.

**Item 1A. Risk Factors**

There have been no other material changes in the risk factors faced by the Company from those disclosed in the Company's Amendment No. 2 on Form 10-K/A for the year ended December 31, 2010 except for the following:

Prior lending practices regarding demand and single pay loans can inhibit our ability to analyze the risk of these credits and timing of potential impairment due to the nature of their payment terms.

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

Not Applicable

**Item 3. Defaults Upon Senior Securities**

Not Applicable

**Item 4. (Removed and Reserved).**

**Item 5. Other Information**

Not Applicable

**Item 6. Exhibits**

The following exhibits are filed as part of this Form 10-Q, and this list includes the exhibit index:

No.	Description
31.1	Certification by Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act.
31.2	Certification by Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act.
32	Certification by Chief Executive Officer and Chief Financial Officer, as required by Section 906 of the Sarbanes-Oxley Act of 2002.



**Table of Contents**

**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.

**NEW PEOPLES BANKSHARES, INC.**  
**(Registrant)**

By: /s/ JONATHAN H. MULLINS  
Jonathan H. Mullins  
President and Chief Executive Officer

Date: August 8, 2011

By: /s/ C. TODD ASBURY  
C. Todd Asbury  
Executive Vice President and Chief Financial  
Officer

Date: August 8, 2011