SHAW COMMUNICATIONS INC
Form 6-K
January 18, 2005

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 6-K

REPORT OF FOREIGN PRIVATE ISSUER
PURSUANT TO RULE 13a-16 OR 15d-16 UNDER
THE SECURITIES EXCHANGE ACT OF 1934

For the month of January, 2005

Shaw Communications Inc.

(Translation of registrant s name into English)

Suite 900, 630 3rd Avenue S.W., Calgary, Alberta T2P 4L4 (403) 750-4500

(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F:

Form 20-F o Form 40-F þ

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1): o

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7): o

Indicate by check mark whether by furnishing the information contained in this Form, the registrant is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes o No þ

If Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-

SIGNATURE

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

Date: January 17, 2005
Shaw Communications Inc.

By:
/s/ Steve Wilson

Steve Wilson
Sr. V.P., Chief Financial Officer
Shaw Communications Inc.

NEWS RELEASE

Shaw Communications Inc. announces first quarter results

Calgary, Alberta, January 12, 2005 Shaw Communications Inc. today announced net income of $18.8 million or $0.04 per share for the quarter ended November 30, 2004 compared to net income of $20.0 million or $0.04 per share for the comparable period last year. Improvements from operating activities were more than offset by a fair value loss on a foreign currency forward contract. Total service revenue in the first quarter was $537.1 million, representing an increase of $34.7 million or 6.9% over the same quarter last year. Consolidated service operating income before amortization[1] for the quarter increased 4.0% to $234.0 million. Cash flow from operations of $180.8 million grew 8.8% over the same period last year.

Customer growth in cable and Internet continued in the first quarter. Basic cable subscribers increased by 17,109, digital customers grew by 21,501 and Internet customers were up 47,748 to 1.07 million. This represents growth in the quarter of 4.0% and 4.7% for digital and Internet, respectively. Due in part to typical seasonal disconnects, DTH customers declined 3,068 in the quarter. At the end of December 2004, year-to-date DTH customer growth stood at 2,554.

Commenting on the results, Jim Shaw, Chief Executive Officer of Shaw, noted: Overall customer growth in the quarter was better than expected and we are off to a strong start in fiscal 2005. The growth caused success-based capital expenditures to increase compared to last year. We have also accelerated certain capital expenditures to accommodate customer growth, and to advance the rollout of Digital Phone and other new products and services. As a result, we saw a temporary decline in free cash flow in the quarter largely due to the timing of these investments.

On a consolidated basis, the Company achieved positive free cash flow[1] of $26.9 million in the first quarter compared to $65.9 million last year. The decrease was primarily due to higher capital expenditures in both cable and Satellite.

Jim Shaw added, We remain committed to free cash flow growth. After almost tripling free cash flow in fiscal 2004 compared to fiscal 2003, we announced in December that we expect free cash flow for fiscal 2005 will be consistent with the previous year, ranging from $270 $285 million. This reflects our current focus on the customer, the capabilities of our network and the strength of product offerings, all of which are important immediate priorities that position us for enhanced growth in the future.

Cable service revenue for the quarter was up 6.3% to $386.0 million (2003 $363.2 million). This growth resulted from higher customer levels, rate increases and the impact of the Monarch

cable systems acquisition in the third quarter of fiscal 2004. Service operating income before amortization of $193.6 million (2003 $192.8 million) increased by 0.5% over the same period last year.

Satellite division quarterly service revenue of $151.1 million (2003 $139.1 million) grew by approximately 8.6% over the same period in 2004, and service operating income before amortization was $40.4 million (2003 $32.2 million). Both improvements were largely due to rate increases and customer growth in DTH in prior periods.

Jim Shaw commented, Both divisions reported solid revenue growth compared to last year. As expected, the cable division experienced pressure on margins as we continue to focus on customer acquisition and retention, and make necessary investments to support customer growth and prepare for the launch of Digital Phone. Customer service, value and reliability are key differentiators in the competitive triple-play market. We are investing in those areas now, with bundling promotions, enhanced product offerings and customer support initiatives such as same-day/next-day service.

During the quarter Shaw repurchased 915,400 of its Class B Non-Voting Shares for cancellation pursuant to the normal course issuer bid for $19.4 million ($21.17 per share). As announced in December, on February 1, 2005 Shaw will redeem its outstanding Series A US$142.5 million 8.45% Canadian Originated Preferred Securities (Series A Preferred Securities), listed on the New York Stock Exchange under the symbol SJR PrA. The redemption will result in a potential estimated economic benefit in excess of $25 million. This represents the foreign exchange benefit realized on the redemption of the unhedged par value of the Series A Preferred Securities, combined with the present value of the potential carrying charge savings over a ten-year term, net of breakage costs of $12.2 million. The breakage costs are in respect of a cross currency swap relating to certain Series A Preferred Security distributions. The redemption is being financed using Shaw s existing revolving bank facility.

Mr. Shaw concluded, We believe this will be another significant year in Shaw s history. We started out in the cable business over thirty-five years ago and now have more than two million cable customers. Seven years ago we entered the Internet market and today we have the highest penetration rate in North America, with 50% of basic customers now subscribing to our Internet service. In fiscal 2005 we will enter another exciting phase of Shaw s evolution as we launch our next growth opportunity Digital Phone .

This news release contains forward-looking statements, identified by words such as anticipate , believe , expect , plan intend and potential . These statements are based on current conditions and assumptions and are not a guarantee of future events. Actual events could differ materially as a result of changes to Shaw s plans and the impact of events, risks and uncertainties. For a discussion of these factors, refer to Shaw s current annual information form, annual and quarterly reports to shareholders and other documents filed with regulatory authorities.

Shaw Communications Inc. is a diversified Canadian communications company whose core business is providing broadband cable television, Internet and satellite direct-to-home (DTH) services to approximately 3.0 million customers. Shaw is traded on the Toronto and New York stock exchanges (Symbol: TSX SJR.NV.B, NYSE SJR).

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For further information, please contact:

Steve Wilson
Senior Vice President, Chief Financial Officer
Shaw Communications Inc.
403-750-4500

1 See definitions under Key Performance Drivers in Management s Discussion and Analysis

Shaw Communications Inc.

SHAREHOLDERS REPORT
FIRST QUARTER ENDING NOVEMBER 30, 2004

SELECTED FINANCIAL HIGHLIGHTS
CONSOLIDATED RESULTS OF OPERATIONS
FIRST QUARTER ENDING NOVEMBER 30, 2004

	Three months ended November 30,		
	2004	2003	Change %
($000 s Cdn, except per share amounts)			
Operations:			
Service revenue	**537,050**	502,372	6.9
Service operating income before amortization [1]	**234,024**	224,962	4.0
Cash flow from operations [2]	**180,766**	166,131	8.8
Net income	**18,815**	20,008	(6.0)
Per share data:			
Earnings per share basic and diluted [3]	**$ 0.04**	$ 0.04	
Weighted average participating shares outstanding during period (000 s)	**231,429**	231,810	

(1) See definition under Key Performance Drivers in Management s Discussion and Analysis.

(2) Cash flow from operations is before changes in non-cash working capital as presented in the unaudited interim Consolidated Financial Statements.

(3) After deducting entitlements on the equity instruments, net of income taxes, amounting to $9,350 or $0.04 per share [2003 $9,655 or $0.04 per share].

QUARTERLY HIGHLIGHTS

Net income was $18.8 million for the quarter compared to $20.0 million for the same quarter last year. Improvements from operating activities were more than offset by a fair value loss on a foreign currency forward contract.

Earnings per share were $0.04 for the quarter consistent with last year.

Service revenue improved from $502.4 million in the first quarter of last year to $537.1 million this year, which represents a 6.9% increase.

Service operating income before amortization was up 4.0% to $234.0 million (2003 $225.0 million).

Free cash flow[1] was $26.9 million for the quarter.

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1 See definitions under Key Performance Drivers in Management s Discussion and Analysis

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Shaw Communications Inc.

The Company s cable and Internet customer base continued to grow in the first quarter with increases of 17,109 for basic cable, 21,501 for digital, and 47,748 for Internet. Approximately 43.7% (2003 39.6%) of cable customers now subscribe to a bundled service.

Due in part to typical seasonal disconnects, Satellite customers declined 3,068 in the first quarter.

Quarterly dividends on the Class B Non-Voting Shares increased from $0.05 per share to $0.07 per share effective September 30, 2004. Going forward, we intend to pay dividends on a monthly basis.

Pursuant to the normal course issue bid, during the first quarter 915,400 Class B Non-Voting Shares were repurchased for $19.4 million ($21.17 per share).

First quarter subscriber growth was better than anticipated. The launch of Digital Phone will complete our triple-play bundle and give us a significant opportunity to further expand our customer base. In addition, we continue to enhance and strengthen our core product offerings and recently announced the addition of several new value-added services:

Shaw Secure, the Company s comprehensive security package, included as part of our Internet services for all existing and future customers. It offers a complete computer security suite with anti-virus, firewall, parental control, spam control, pop-up blocker, and anti-spyware combined into a single, easy-to-use product.

Shaw Messenger, a complete online messaging service for all Shaw Internet customers. Messenger includes secure instant messaging, PC to PC voice/video calling, chat rooms, and application sharing features such as file sharing for photos and web pages.

The recent nationwide debut of **Fox News** and **Bloomberg Television** on Shaw Digital Cable and Star Choice satellite.

The new **24 hour HD movie channel** from Movie Central available to Shaw Cable customers and Star Choice satellite Movie Central customers at no additional charge. Customers can enjoy a wide range of movies and the best selection of premium television programs and mini-series in full High Definition TV.

We also remain focused on the generation of free cash flow while still ensuring we invest in the future capabilities of our network. After almost tripling free cash flow in fiscal 2004 over fiscal 2003, we announced in December that free cash flow for fiscal 2005 will be consistent with the previous year, ranging from $270 $285 million. This will be a significant accomplishment considering this year s investments in Digital Phone, ongoing 860 Megahertz upgrades, increased success based activity and the purchase of Anik F2 transponders. Much of this capital activity will occur in the first half of the year reflected by this quarter s increase in capital expenditures over the same quarter last year.

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Finally, we are focused on the successful launch of our Digital Phone service. Key to this will be the delivery of a fully-featured, reliable telephone service coupled with outstanding customer support. In preparation for the Digital Phone launch, we are staffing-up and developing bundling promotions and service programs, such as same-day/next-day service. While investments such as these may result in near term pressure on margins, we believe that our focus on the customer, the capabilities of our network and the strength of our product offerings will position us for enhanced growth in the future.

JR Shaw	Jim Shaw
Executive Chair	Chief Executive Officer

Shaw Communications Inc.

MANAGEMENT S DISCUSSION AND ANALYSIS
NOVEMBER 30, 2004

January 6, 2005

Certain statements in this report may constitute forward-looking statements. Such forward-looking statements involve risks, uncertainties and other factors which may cause actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Included herein is a Caution Concerning Forward-Looking Statements section which should be read in conjunction with this report.

The following should also be read in conjunction with Management s Discussion and Analysis included in the Company s August 31, 2004 Annual Report and the Consolidated Financial Statements and the Notes thereto and the unaudited interim Consolidated Financial Statements of the current quarter.

Consolidated Overview

Consolidated service revenue increased by 6.9% to $537.1 million in the first quarter compared to $502.4 million last year. Improved service revenue resulted from growth in the customer base, rate increases and the acquisition of the Monarch cable systems effective March 31, 2004. First quarter consolidated service operating income before amortization[1] of $234.0 million increased by 4.0% over the same quarter last year due to revenue growth partly offset by increased costs in the cable division primarily incurred to support continued growth and in preparation for increased competition and the launch of Digital Phone. Accordingly the consolidated operating margin decreased to 43.6% from 44.8%.

Net income in the first quarter benefited from improved operating performance over the same quarter last year, reflected through increased service operating income before amortization of $9.1 million and decreased interest expense of $2.5 million. These improvements were more than offset by a fair value loss of $21.6 million on a certain foreign currency forward contract. As outlined in previous annual reports, the Company entered into a forward contract to purchase US dollars at 1.4078 Cdn. in respect of its US dollar denominated entitlements on equity instruments. Under Accounting Guideline 13, the forward contract does not qualify for hedge accounting. Accordingly, the entitlements are recorded through the deficit at spot rates while fair value adjustments on the related derivative are recorded in income. The impact of the foregoing and other changes to net income, which resulted in a decrease to net income of $1.2 million in the quarter, are outlined below:

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1 See definitions under Key Performance Drivers in Management s Discussion and Analysis

Shaw Communications Inc.

	Three months ended November 30, 2004
($millions Cdn)	
Increased service operating income before amortization	9.1
Increased amortization of deferred IRU revenue	0.5
Increased amortization of deferred net equipment cost	(3.9)
Decreased amortization of deferred charges and property, plant and equipment	2.9
Decreased interest expense	2.5
Change in net other costs and revenue[(1)]	(15.6)
Decrease in income taxes	3.3
	(1.2)

(1) Net other costs and revenue include: foreign exchange gain on long-term debt, fair value loss on a foreign currency forward contract, debt retirement costs, and other gains as detailed in the unaudited interim Consolidated Statements of Income and Deficit.

Earnings per share were $0.04 for the quarter, which is consistent with last year.

Cash flow from operations before changes in non-cash working capital was $180.8 million in the first quarter compared to $166.1 million in the same period last year. The growth over the comparative quarter was primarily due to increased service operating income before amortization of $9.1 million, reduced interest expense of $2.5 million and decreased current income tax expense of $1.6 million.

On a consolidated basis, the Company achieved positive free cash flow[1] of $26.9 million in the first quarter (2003 $65.9 million). The decline compared to last year is primarily due to increased capital expenditures, particularly in the upgrades and enhancement and success-based categories. The satellite division generated negative free cash flow of $5.1 million compared to negative free cash flow of $10.5 million in the same quarter last year. Cable generated $32.0 million of positive free cash flow for the quarter compared to $76.4 million last year.

Update to critical accounting policies

In Management s Discussion and Analysis (MD&A) included in the Company s August 31, 2004 Annual Report, the Company discussed critical accounting policies including key estimates and assumptions that management has made under these policies and how they affect the amounts reported in the Consolidated Financial Statements. The MD&A also describes significant accounting policies where alternatives exist. Also described therein were a number of new accounting policies Shaw was required to adopt in 2005 as a result of recent changes in Canadian Accounting pronouncements. For a description of the changes in accounting policies, readers should refer to Note 1 of the unaudited interim Consolidated Financial Statements. The ensuing discussion provides additional information as to the date that Shaw was required to adopt the new standards, the methods of adoption permitted by the standards and the method chosen by Shaw and the effect on the financial statements as a result of adopting the new policy.

1 See definitions under Key Performance Drivers in Management s Discussion and Analysis

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Adoption of recent Canadian accounting pronouncements

Asset Retirement Obligations

In the first quarter of 2005, the Company was required to retroactively adopt the new Canadian standard, Asset Retirement Obligations. The application of this standard had no significant impact on the financial position or results of operations of the Company.

GAAP Hierarchy and General Standards of Financial Statement Presentation

In the first quarter of 2005, the Company was required to adopt the new CICA Handbook Sections 1100, Generally Accepted Accounting Principles, and 1400, General Standards of Financial Statement Presentation . The effect of any change in accounting policy made in adopting these sections only applies to events and transactions occurring after August 31, 2004 and to any outstanding related balances existing at the date of the change.

The application of these recommendations had no significant impact on the Company s consolidated financial statements.

Key Performance Drivers

The Company s continuous disclosure documents may provide discussion and analysis of non-GAAP financial measures. These financial measures do not have standard definitions prescribed by Canadian GAAP or US GAAP and therefore may not be comparable to similar measures disclosed by other Companies. The Company utilizes these measures in making operating decisions and assessing its performance. Certain investors, analysts and others, utilize these measures in assessing the Company s financial performance and as an indicator of its ability to service debt. These non-GAAP financial measures have not been presented as an alternative to net income or any other measure of performance required by Canadian or US GAAP.

The following contains a listing of the Company s use of non-GAAP financial measures and provides a reconciliation to the nearest GAAP measurement or provides a reference to such reconciliation.

Service operating income before amortization

The Company utilizes this measurement as it is a widely accepted financial indicator of a company s ability to service and/or incur debt. In respect of the calculation of consolidated service operating income before amortization, it is presented as a sub-total line item in the Company s unaudited interim Consolidated Statements of Income and Deficit. It is calculated as service revenue less operating, general and administrative expenses.

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Free cash flow

The Company utilizes this measurement as it measures the Company s ability to repay debt and return cash to shareholders. Consolidated free cash flow is calculated as follows:

	Three months ended November 30,	
	2004	2003
($000 s Cdn)		
Cable free cash flow[1]	**31,979**	76,376
Combined satellite free cash flow[1]	**(5,129)**	(10,464)
Consolidated	**26,850**	65,912

(1) The reconciliation of free cash flow for both cable and satellite is provided in the following segmented analysis.

CABLE

FINANCIAL HIGHLIGHTS

	Three months ended November 30,		
	2004	2003	Change %
($000 s Cdn)			
Service revenue (third party)	**385,966**	363,238	6.3
Service operating income before amortization (1)	**193,646**	192,771	0.5
Less:			
Interest	**43,228**	44,001	(1.8)
Entitlements on equity instruments, net of current taxes	**9,350**	9,655	(3.2)
Cash taxes on net income	**6,718**	8,252	(18.6)
Cash flow before the following:	**134,350**	130,863	2.7
Capital expenditures and equipment costs (net):			
New housing development	**19,459**	17,998	8.1
Success based	**20,200**	12,611	60.2
Upgrades and enhancement	**45,138**	17,727	154.6
Replacement	**6,348**	3,904	62.6
Buildings/other	**11,226**	2,247	399.6
Total as per Note 2 to the unaudited interim Consolidated Financial Statements	**102,371**	54,487	87.9

Free cash flow (1)	**31,979**	76,376	(58.1)
Operating margin	**50.2%**	53.1%	(2.9)

(1) See definitions under Key Performance Drivers in Management s Discussion and Analysis.

OPERATING HIGHLIGHTS

Strong customer growth occurred during the first quarter with increases of 17,109 in basic, 21,501 in digital and 47,748 in Internet.

Effective November 26, 2004, Shaw introduced average rate increases of approximately $1 per month on most of its packages. The increases should generate additional revenue of approximately $2 million per month when fully implemented by February 2005.

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Cable service revenue increased by 6.3% over the same period last year primarily as a result of customer growth, rate increases of $1 to $2 per month implemented in February, 2004 and the Monarch cable systems acquired effective March 31, 2004, which generated revenue of $5.8 million in the first quarter of fiscal 2005. Despite these factors, service operating income before amortization grew by only 0.5% over last year because of increased costs primarily incurred to support continued growth and in preparation for increased competition and the launch of Digital Phone.

Although service revenue grew by 1.7% over the fourth quarter of fiscal 2004 as a result of the higher customer base, service operating income before amortization decreased by 1.1%. This occurred because of higher costs, principally salaries and benefits, network fees and premises costs. It is anticipated that the ongoing emphasis on enhancing customer service, the requirement to make up-front investments in advance of the rollout of Digital Phone, and competitive factors will continue to exert pressure on margins. These factors have been anticipated and are in-line with the Company s published guidance for fiscal 2005.

First quarter capital expenditures were $102.4 million, an increase of $47.9 million over the same period last year. Success-based expenditures grew by $7.6 million as a result of increased deployment of equipment, partially offset by lower costs which are in part due to the strengthening Canadian dollar. Upgrade and enhancement activity increased by $27.4 million due to upgrades to the distribution system, including $13.4 million directed towards the launch of Digital Phone. The majority of the $9.0 million increase in the buildings and other category was due to the completion of leasehold improvements at the new regional Vancouver office and the renewal of certain software licenses.

SUBSCRIBER STATISTICS

			Three months ended	
	November 30, 2004	August 31, 2004	Growth	Change %
CABLE:				
Basic service:				
Actual	**2,139,597**	2,122,488	17,109	0.8
Penetration as % of homes passed	**67.3%**	67.2%		
Digital terminals	**676,016**	640,975	35,041	5.5
Digital customers	**562,036**	540,535	21,501	4.0
INTERNET:				
Connected and scheduled installations	**1,068,686**	1,020,938	47,748	4.7
Penetration as % of basic	**49.9%**	48.1%		
Stand-alone Internet not included in basic cable	**124,597**	114,767	9,830	8.6

Shaw added 17,109 basic subscribers in the current quarter compared to 21,894 in the same quarter last year. In addition to the continued success of the basic and full cable service introductory offer to stand-alone Internet and other potential customers, customer growth has been enhanced as a result of strong economic activity in Alberta and British Columbia.

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During the quarter, Shaw added 21,501 digital customers, compared to 15,652 in the first quarter of fiscal 2004. Growth has increased due in part to increased customer awareness of the digital viewing experience through word-of-mouth, media and advertising. Also, the availability of advanced set-top boxes incorporating high definition televisions signals (HDTV) and/or a personal video recorder (PVR) has also enabled Shaw customers to enhance their television viewing, and gives Shaw a competitive advantage over its telephone company competitors.

Internet customers grew by 47,748 during the first quarter compared to 48,040 in the same period last year, enabling Shaw to improve its industry-leading penetration to 49.9% of basic, an improvement of almost 5% over last year (2003 45.1%). First quarter growth was achieved through Shaw s back to school marketing campaign as well as the continued migration of dial-up and other competitive services customers to Shaw s Internet service. To further increase the value of its Internet services, effective December 2004, Shaw Secure and Shaw Messenger will be included as part of Shaw s Internet services. Shaw Secure, the Company s comprehensive security package, offers a complete computer security suite with anti-virus, firewall, parental control, spam control, pop-up blocker, and anti-spyware combined into a single, easy-to-use product. Shaw Messenger is a complete online messaging service and includes secure instant messaging, PC to PC voice/video calling, chat rooms, and application sharing features such as file sharing for photos and web pages.

At the end of the first quarter, approximately 43.7% of Shaw customers subscribed to bundled services compared to 39.6% at November 30, 2003. The attractiveness of the bundled packages is enhanced by Shaw s ability to offer services such as VOD, HDTV and, in the near future, Digital Phone. Shaw s bundling strategy has proven to be an effective customer retention tool for its digital and Internet customers as shown by churn rates in the table below.

	Three months ended November 30,	
Churn (1)	**2004**	2003
Digital customers	**3.4%**	3.8%
Internet customers	**3.5%**	3.7%

(1) Calculated as the number of new customer activations less the net gain of customers during the period divided by the average of the opening and closing customers for the applicable period. It should be noted that seasonality and marketing programs could impact any comparison of quarterly churn on a sequential basis.

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SATELLITE (DTH and Satellite Services)

FINANCIAL HIGHLIGHTS

	Three months ended November 30,		
	2004	2003	Change %
($000s Cdn)			
Service revenue (third party)			
DTH (Star Choice)	**131,563**	119,150	10.4
Satellite Services	**19,521**	19,984	(2.3)
	151,084	139,134	8.6
Service operating income before amortization [(1)]			
DTH	**30,414**	22,203	37.0
Satellite Services	**9,964**	9,988	(0.2)
	40,378	32,191	25.4
Less:			
Interest [(2)]	**10,398**	12,136	(14.3)
Cash taxes on net income	**123**	175	(29.7)
Cash flow before the following:	**29,857**	19,880	50.2
Capital expenditures and equipment costs (net):			
Success based [(3)]	**25,568**	29,735	(14.0)
Transponders and other	**9,418**	609	1,446.5
Total as per Note 2 to the unaudited interim Consolidated Financial Statements	**34,986**	30,344	15.3
Free cash flow [(1)]	**(5,129)**	(10,464)	51.0

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(1) See definitions under Key Performance Drivers in Management s Discussion and Analysis.

(2) Interest is allocated to the Satellite division based on the actual cost of debt incurred by the Company to repay prior outstanding Satellite debt and to fund accumulated cash deficits of Cancom and Star Choice.

(3) Net of the profit on the sale of satellite equipment as it is viewed as a recovery of expenditures on customer premise equipment.

OPERATING HIGHLIGHTS

DTH customers declined by 3,068 in this quarter compared to a decrease of 956 in the same quarter last year. At the end of December 2004, fiscal year-to-date customer growth stood at 2,554 (December 2003 3,783).

Service revenue increased by 8.6% over the same quarter last year primarily as a result of the February 1, 2004 DTH monthly rate increase of $3.00 and subscriber growth. These factors enabled Satellite to improve service operating income before amortization by 25.4% over the comparable period last year.

Service revenue decreased marginally in comparison to the fourth quarter of 2004 as a result of certain rate reductions and customer losses in Satellite Services. This revenue reduction, along with higher network fees and marketing costs in DTH, were the main reasons for a decrease of 6.9% in service operating income before amortization from the fourth quarter of 2004.

Capital expenditures increased $4.6 million over the first quarter last year due to costs incurred on the launch of the Anik F2 satellite of $8.8 million which were partially offset by reduced success based capital of $4.2 million. Effective October 4, 2004 Star Choice began operating

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with additional capacity on Telesat s Anik F2 satellite, which has enabled the addition of three more HDTV channels to its service, bringing the total to nine. Star Choice has also introduced receivers which provide a more economical alternative for new customers or existing customers to expand Star Choice services in their homes. On-going development of the DTH service, combined with improvements in customer service implemented over the past two years, are anticipated to result in improved customer retention.

CUSTOMER STATISTICS

			Three months ended	
	November 30, 2004	August 31, 2004	Growth	Change %
Star Choice customers [1]	**824,835**	827,903	(3,068)	(0.4)

(1) Including seasonal customers who temporarily suspend their service.

	Three months ended November 30,	
Churn [2]	**2004**	2003
Star Choice customers	**5.3%**	6.0%

(2) Calculated as the number of new customer activations less the net gain of customers during the period divided by the average of the opening and closing customers for the applicable period.

Due in part to typical seasonal disconnects, DTH customers declined 3,068 in the first quarter. Customer churn has improved over last year, although it is higher than the fourth quarter of 2004, partially due to seasonal factors.

OTHER INCOME AND EXPENSE ITEMS:

Amortization

	Three months ended November 30,		
	2004	2003	Change %
($000s Cdn)			
Amortization revenue (expense) -			
Deferred IRU revenue	**3,636**	3,083	17.9
Deferred equipment revenue	**17,887**	23,861	(25.0)
Deferred equipment cost	**(56,405)**	(58,483)	(3.6)
Deferred charges	**(1,713)**	(2,648)	(35.3)

Property, plant and equipment	**(101,579)**	(103,548)	(1.9)

Commencing in fiscal 2004, Star Choice reduced the selling price of DTH equipment in lieu of giving programming credits to new customers. This is the principal reason for the decrease in amortization of deferred equipment revenue in the current quarter. Amortization of deferred charges declined as a result of the repayment of the $250.0 million Cancom Structured Note and deferred marketing costs becoming fully amortized during 2004.

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Interest

	Three months ended November 30,		
	2004	2003	Change %
($000s Cdn)			
Interest	**53,626**	56,137	(4.5)

Interest charges decreased over the same periods last year as a result of reduced consolidated debt levels.

Foreign exchange gain (loss) on unhedged and hedged long-term debt

Shaw records foreign exchange gains and losses on the translation of foreign denominated unhedged long-term debt, which at November 30, 2004 was comprised of US $47.2 million of bank loans. As a result of fluctuations of the Canadian dollar relative to the US dollar, the Company recorded a foreign exchange gain of $6.4 million in the quarter (2003 $4.8 million).

As required by generally accepted accounting principles, the Company is required to translate long-term debt at period-end foreign exchange rates. Because the Company follows hedge accounting, the resulting foreign exchange gains or losses on translating hedged long-term debt are included in deferred credits or deferred charges. As a result, the amount of hedged long-term debt that is reported under GAAP is often different than the amount at which the hedged debt would be settled under existing cross-currency interest rate agreements. As outlined in Note 3 to the unaudited interim Consolidated Financial Statements, if the rate of translation was adjusted to reflect the hedged rates of the Company s cross-currency interest rate agreements (which fix the liability for interest and principal) long-term debt would increase by $330.8 million (August 31, 2004 $208.3 million) which represents the corresponding hedged amounts included in deferred credits.

Debt retirement costs

In November 2003, the Company incurred $2.4 million of debt retirement costs in connection with the issuance of $350 million of Senior unsecured notes at 7.5% and used the net proceeds to repay its $350 million credit facility due February 10, 2006. There were no such costs in the current quarter.

Fair value adjustment on a foreign currency forward contract

The Company s extendible forward purchase contract which provides US funds required for the quarterly entitlement payments on the US denominated equity instruments, does not qualify for hedge accounting under Canadian GAAP. Accordingly, the carrying value of this financial instrument is adjusted to reflect the current market value which resulted in a pre-tax loss of $21.6 million in the quarter.

Shaw Communications Inc.

Other gains

This category consists mainly of realized and unrealized foreign exchange gains of $3.2 million (2003 $0.9 million) on US dollar denominated current assets and liabilities. The increase is due to the strengthening of the Canadian dollar relative to the US dollar in the past year.

RISKS AND UNCERTAINTIES

There have been no material changes in any risks or uncertainties facing the Company since August 31, 2004.

FINANCIAL POSITION

Following is a discussion of significant changes in the consolidated balance sheet since August 31, 2004.

Total assets at November 30, 2004 were $7.6 billion. This represents an increase of $11.7 million over August 31, 2004. Current assets increased by $2.9 million due to higher inventory levels of $4.5 million in preparation for the holiday season. Non-current assets grew by $8.7 million. This was partly attributable to the increase in investments and other assets due to the purchase of an additional 2.1 million shares of Canadian Hydro Developers, Inc. for $5.2 million.

Broadcast licenses decreased by $0.9 million due to the sale of the cable television advertising business, originally acquired as part of the purchase of the Monarch cable systems in 2004, to Corus Entertainment Inc., a company subject to common voting control, for cash during the first quarter. The transaction was reviewed by the Company s Corporate Governance Committee, comprised of independent directors.

Current liabilities (excluding current portion of long-term debt) decreased by $33.3 million since August 31, 2004, primarily reflecting payments of accrued interest during the first quarter.

Total long-term debt decreased by $79.0 million as a result of a decrease of $128.9 million relating to the translation of US denominated debt, offset by net new borrowings (including $5.9 million in respect of the Burrard Landing partnership) of $50.0 million.

Deferred credits increased by $118.1 million primarily due to the increase in deferred foreign exchange translation gains on the translation of hedged US dollar denominated senior notes of $122.6 million, offset by amortization of prepaid IRU rental of $3.6 million. Other liabilities increased by $30.2 million primarily due to a fair value adjustment in respect of a foreign currency forward contract which is not accounted for as a hedge.

Share capital decreased by $8.9 million due to the repurchase of 915,400 Class B Non-Voting Shares for cancellation for $19.4 million in the first quarter. The balance of the cost of the shares repurchased was charged to the deficit. As of the date of Management s Discussion and Analysis, there were no subsequent changes in share capital other than the repurchase of 19,200 Class B Non-Voting Shares for cancellation at an average price of $20.54.

Shaw Communications Inc.

LIQUIDITY AND CAPITAL RESOURCES

Shaw generated $26.9 million of free cash flow in the first quarter which, combined with the increase in bank loans and bank indebtedness of $63.5 million, was used to purchase $19.4 million of Class B Non-Voting Shares for cancellation, pay common share dividends of $16.2 million and finance the increase in working capital of $53.2 million and other items of $1.6 million.

Shaw received approval from the Toronto Stock Exchange (TSX) to renew its normal course issuer bid which authorizes Shaw to purchase up to 10,900,000 of its Class B Non-Voting Shares for the period November 6, 2004 to November 7, 2005, representing approximately 5% of the issued and outstanding Class B Non-Voting Shares. The purchase and cancellation of outstanding Class B Non-Voting Shares under the bid may represent an opportunity to provide capital appreciation and market stability for the benefit of Shaw s shareholders. Pursuant to the normal course issuer bid, during the quarter Shaw repurchased 915,400 of its Class B Non-Voting Shares for cancellation for $19.4 million.

On December 16, 2004 the Company announced the redemption of its outstanding Series A US $142.5 million 8.45% Canadian Originated Preferred Securities (Series A COPrS) on February 1, 2005. The Company believes that the redemption is prudent given the current interest and foreign exchange rate environments. The potential estimated economic benefit is approximately $25 million, representing the foreign exchange benefit realized on the redemption of the unhedged par value of the securities and the potential carrying charge savings over a term of ten years, net of a $12.2 million cost to break a cross-currency swap relating to the dividend payments on the securities. The redemption is to be financed using Shaw s existing revolving bank facility. Shaw has entered into a forward contract to purchase the US funds required at the redemption date at an exchange rate of $1.2091 Canadian.

At November 30, 2004, Shaw had access to $780 million of available credit facilities based on existing bank covenants. Based on available credit facilities and forecasted free cash flow, the Company expects to have sufficient liquidity to fund operations and obligations during the current fiscal year, including the redemption of the Series A COPrS and the repayment of the $275 million 7.05% Notes due April 11, 2005. On a longer-term basis, Shaw expects to generate adequate free cash flow and to have sufficient borrowing capacity to finance foreseeable future business plans and refinance maturing debt.

CASH FLOW

Operating Activities

	Three months ended November 30,		
	2004	2003	%
($000s Cdn)			
Cash flow from operations	**180,766**	166,131	8.8
Net decrease (increase) in non-cash working capital balances related to operations	**(53,198)**	(20,691)	(157.1)
	127,568	145,440	(12.3)

Shaw Communications Inc.

Cash flow from operations increased over comparative periods as a result of growth in service operating income before amortization and due to decreased interest and current income tax expenses. Over half of the quarter-over-quarter decrease in the net change in non-cash working capital balances of $32.5 million is due to the timing of bonus payments. The bonuses in respect of the 2004 fiscal year were paid in the first quarter of the current year whereas the bonuses for the 2003 fiscal year were paid in the fourth quarter of that same year. The remaining change is mainly in respect of timing in payments for prepaid interest and contract maintenance expenses.

Investing Activities

	Three months ended November 30,		
	2004	2003	Decrease
($000s Cdn)			
Cash flow used in investing activities	**(150,437)**	(107,560)	(42,877)

The cash used in investing activities was $42.9 million higher in the current quarter primarily due to higher capital expenditures.

Financing Activities

The changes in financing activities during the comparative periods were as follows:

	Three months ended November 30,	
	2004	2003
(In $millions Cdn)		
Repayment of $350 million credit facility		(350.0)
Proceeds on $350 million Senior notes		350.0
Bank loans and bank indebtedness net borrowings (repayments)	**63.6**	(4.3)
Purchase of Class B Non-Voting Shares for cancellation	**(19.4)**	(21.8)
Dividends and equity entitlements	**(27.2)**	(17.5)
Debt retirement costs		(1.0)
Proceeds on prepayment of IRU		2.9
Increase in Partnership bank loans	**5.9**	4.3
	22.9	(37.4)

CAUTION CONCERNING FORWARD LOOKING STATEMENTS

Certain statements included and incorporated by reference herein constitute forward-looking statements. When used, the words anticipate , believe , expect , plan , intend , target , guideline , goal , and similar expressions are inte identify forward-looking statements. These forward-looking statements include, but are not limited to, references to

future capital expenditures (including the amount and nature thereof), business strategies and measures to implement strategies, competitive strengths, goals, expansion and growth of Shaw s business and operations, plans and references to the future success of Shaw. These forward-looking statements are based on certain assumptions and analyses made by Shaw in light of its experience and its perception of historical trends, current conditions and expected future developments as well as other factors it believes are appropriate in the circumstances. However, whether actual results and developments will conform with the expectations and predictions of Shaw is subject to a number of risks and uncertainties, including, but not limited to, general economic, market or business conditions; the opportunities (or lack thereof) that may be presented to and pursued by Shaw; increased competition in the markets in which Shaw operates

Shaw Communications Inc.

and from the development of new markets for emerging technologies; changes in laws, regulations and decisions by regulators in Shaw s industries in both Canada and the United States; Shaw s status as a holding company with separate operating subsidiaries; changing conditions in the entertainment, information and communications industries; risks associated with the economic, political and regulatory policies of local governments and laws and policies of Canada and the United States; and other factors, many of which are beyond the control of Shaw. Should one or more of these risks materialize, or should assumptions underlying the forward-looking statements prove incorrect, our actual results may vary materially from those as described herein. Consequently, all of the forward-looking statements made in this report and the documents incorporated by reference herein are qualified by these cautionary statements, and there can be no assurance that the actual results or developments anticipated by Shaw will be realized or, even if substantially realized, that they will have the expected consequences to, or effects on, Shaw.

You should not place undue reliance on any such forward-looking statements. Further, any forward-looking statement (and such risks, uncertainties and other factors) speaks only as of the date on which it was originally made and the Company expressly disclaims any obligation or undertaking to disseminate any updates or revisions to any forward-looking statement contained in this document to reflect any change in our expectations with regard to those statements or any other change in events, conditions or circumstances on which any such statement is based, except as required by law. New factors emerge from time to time, and it is not possible for the Company to predict what factors will arise or when they may arise. In addition, the Company cannot assess the impact of each factor on its business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

Shaw Communications Inc.

CONSOLIDATED BALANCE SHEETS

(Unaudited)

[thousands of Canadian dollars]	**November 30, 2004**	August 31, 2004
ASSETS		
Current		
Accounts receivable	**117,073**	119,519
Inventories	**47,429**	42,973
Prepaids and other	**17,894**	16,975
	182,396	179,467
Investments and other assets	**49,160**	43,965
Property, plant and equipment	**2,295,336**	2,292,340
Deferred charges	**268,911**	267,439
Intangibles		
Broadcast licenses	**4,684,647**	4,685,582
Goodwill	**88,111**	88,111
	7,568,561	7,556,904
LIABILITIES AND SHAREHOLDERS EQUITY		
Current		
Bank indebtedness	**23,760**	4,317
Accounts payable and accrued liabilities	**361,074**	410,037
Income taxes payable	**4,938**	5,563
Unearned revenue	**92,944**	96,095
Current portion of long-term debt *[note 3]*	**358,094**	343,097
	840,810	859,109
Long-term debt *[note 3]*	**2,213,605**	2,307,583
Other long-term liabilities *[note 9]*	**47,153**	16,933
Deferred credits	**1,017,034**	898,980
Future income taxes	**984,958**	982,281
	5,103,560	5,064,886
Shareholders equity		
Share capital *[note 4]*	**2,851,486**	2,860,356
Contributed surplus	**665**	412
Deficit	**(387,522)**	(369,194)
Cumulative translation adjustment	**372**	444

	2,465,001	2,492,018
	7,568,561	7,556,904

See accompanying notes

Shaw Communications Inc.

CONSOLIDATED STATEMENTS OF INCOME AND DEFICIT

(Unaudited)

[thousands of Canadian dollars except per share amounts]	Three months ended November 30, **2004**	2003
		(Restated - note 1)
Service revenue *[note 2]*	**537,050**	502,372
Operating, general and administrative expenses	**303,026**	277,410
Service operating income before amortization *[note 2]*	**234,024**	224,962
Amortization:		
Deferred IRU revenue	**3,636**	3,083
Deferred equipment revenue	**17,887**	23,861
Deferred equipment cost	**(56,405)**	(58,483)
Deferred charges	**(1,713)**	(2,648)
Property, plant and equipment	**(101,579)**	(103,548)
Operating income	**95,850**	87,227
Interest on long-term debt	**(53,626)**	(56,137)
	42,224	31,090
Foreign exchange gain on long-term debt	**6,385**	4,832
Fair value loss on a foreign currency forward contract	**(21,600)**	
Debt retirement costs		(2,428)
Other gains	**3,608**	1,601
Income before income taxes	**30,617**	35,095
Income tax expense	**11,826**	15,168
Income before the following	**18,791**	19,927
Equity income on investees	**24**	81
Net income	**18,815**	20,008
Deficit beginning of period as previously reported	**(369,194)**	(340,294)
Adjustment for change in accounting policy for revenue recognition *[note 1]*		3,599
Deficit, beginning of period restated	**(369,194)**	(336,695)
Reduction on Class B Non-Voting Shares purchased for cancellation	**(10,504)**	(11,366)
Amortization of opening fair value loss on a foreign currency forward contract	**(1,100)**	
Dividends -		
Class A and Class B Non-Voting Shares	**(16,189)**	(6,956)
Equity instruments (net of income taxes)	**(9,350)**	(9,655)

Deficit, end of period	**(387,522)**	(344,664)
Earnings per share *[note 5]*		
Basic and diluted	**$ 0.04**	$ 0.04
[thousands of shares]		
Weighted average participating shares outstanding during period	**231,429**	231,810
Participating shares outstanding, end of period	**230,554**	230,763

See accompanying notes

Shaw Communications Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

[thousands of Canadian dollars]	Three months ended November 30, **2004**	2003
		(Restated - note 1)
OPERATING ACTIVITIES *[note 6]*		
Cash flow from operations	**180,766**	166,131
Net decrease (increase) in non-cash working capital balances related to operations	**(53,198)**	(20,691)
	127,568	145,440
INVESTING ACTIVITIES		
Additions to property, plant and equipment *[note 2]*	**(101,988)**	(58,238)
Additions to equipment costs (net) *[note 2]*	**(39,596)**	(34,862)
Net addition to inventories	**(4,456)**	(7,830)
Cable system acquisition		(145)
Proceeds on sale of investments and other assets	**1,051**	307
Cost to terminate IRU	**(283)**	
Acquisition of investments	**(5,165)**	
Additions to deferred charges		(6,792)
	(150,437)	(107,560)
FINANCING ACTIVITIES		
Increase in bank indebtedness	**19,443**	
Increase in long-term debt	**65,399**	402,260
Long-term debt repayments	**(15,440)**	(402,236)
Debt retirement costs		(969)
Proceeds on pre-payment of IRU		2,850
Purchase of Class B Non-Voting Shares for cancellation	**(19,374)**	(21,817)
Dividends paid -		
Class A and Class B Non-Voting Shares	**(16,189)**	(6,956)
Equity instruments, net of current taxes	**(10,963)**	(10,538)
	22,876	(37,406)
Effect of currency translation on cash balances and cash flows	**(7)**	(14)
Increase in cash		460
Cash, beginning of the period		20,753
Cash, end of the period		21,213

Cash includes cash and term deposits

See accompanying notes

Shaw Communications Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

November 30, 2004 and 2003
[all amounts in thousands of Canadian dollars, except per share amounts]

1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES

The unaudited interim Consolidated Financial Statements include the accounts of Shaw Communications Inc. and its subsidiaries (collectively the Company). The notes presented in these unaudited interim Consolidated Financial Statements include only significant events and transactions occurring since the Company s last fiscal year end and are not fully inclusive of all matters required to be disclosed in the Company s annual audited consolidated financial statements. As a result, these unaudited interim Consolidated Financial Statements should be read in conjunction with the Company s consolidated financial statements for the year ended August 31, 2004.

The unaudited interim Consolidated Financial Statements follow the same accounting policies and methods of application as the most recent annual consolidated financial statements except as noted below.

Adoption of recent Canadian accounting pronouncements

Asset Retirement Obligations

In the first quarter of 2005, the Company retroactively adopted the new Canadian standard, Asset Retirement Obligations, which establishes standards for the recognition, measurement and disclosure of asset retirement obligations and the related asset retirement costs. This new standard applies to obligations associated with the retirement of property, plant and equipment when those obligations result from the acquisition, construction, development or normal operation of the assets. The standard requires the recognition of all legal obligations associated with the retirement, whether by sale, abandonment, recycling or other disposal of an asset. The application of this standard had no significant impact on the unaudited interim Consolidated Financial Statements of the Company.

GAAP Hierarchy and General Standards of Financial Statement Presentation

In the first quarter of 2005 the Company adopted the new CICA Handbook Sections 1100, Generally Accepted Accounting Principles, and 1400, General Standards of Financial Statement Presentation . Section 1100 describes what constitutes Canadian Generally Accepted Accounting Principles (GAAP) and its sources and provides guidance on sources to consult when selecting accounting policies and determining appropriate disclosures when a matter is not dealt with explicitly in the primary sources of generally accepted accounting principles, thereby re-codifying the Canadian GAAP hierarchy. Section 1400 provides general guidance on financial statement presentation and further clarifies what constitutes fair presentation in accordance with GAAP. The application of these recommendations had no significant impact on the Company s unaudited interim Consolidated Financial Statements.

Restatement for change in accounting policy for revenue recognition

As previously disclosed, the Company retroactively adopted with restatement beginning March 1, 2004, the accounting pronouncement for Revenue Arrangements with Multiple Deliverables . Accordingly, the figures for the comparative quarter have been restated.

Shaw Communications Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

November 30, 2004 and 2003
[all amounts in thousands of Canadian dollars, except per share amounts]

2. BUSINESS SEGMENT INFORMATION

The Company provides cable television services, high-speed Internet access and Internet infrastructure services (Big Pipe) (Cable); DTH (Star Choice) satellite services; and, satellite distribution services (Satellite Services). All of these operations are located in Canada. Information on operations by segment is as follows:

Operating information

	Three months ended November 30,	
	2004	2003
	$	$
Service revenue		
Cable	**386,681**	363,842
DTH	**132,666**	120,362
Satellite Services	**21,876**	23,484
Inter segment -	**541,223**	507,688
Cable	**(715)**	(604)
DTH	**(1,103)**	(1,212)
Satellite Services	**(2,355)**	(3,500)
	537,050	502,372
Service operating income before amortization		
Cable	**193,646**	192,771
DTH	**30,414**	22,203
Satellite Services	**9,964**	9,988
	234,024	224,962
Interest on long-term debt [(1)]		
Cable	**43,228**	44,001
DTH and Satellite Services	**10,398**	12,136
	53,626	56,137
Cash taxes [(1)]		
Cable	**6,718**	8,252

DTH and Satellite Services	**123**	175
	6,841	8,427

(1) The Company reports interest and cash taxes on a segmented basis for Cable and combined Satellite only. It does not report interest and cash taxes on a segmented basis for DTH and Satellite Services.

Shaw Communications Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

November 30, 2004 and 2003
[all amounts in thousands of Canadian dollars, except per share amounts]

Capital expenditures

	Three months ended November 30,	
	2004	2003
	$	$
Capital expenditures accrual basis		
Cable	**78,313**	39,260
Corporate	**10,429**	6,504
Sub-total Cable including corporate	**88,742**	45,764
Satellite	**9,019**	4,205
	97,761	49,969
Equipment costs (net of revenue received)		
Cable	**13,629**	8,723
Satellite	**25,967**	26,139
	39,596	34,862
Capital expenditures and equipment costs (net)		
Cable	**102,371**	54,487
Satellite	**34,986**	30,344
	137,357	84,831
Reconciliation to Consolidated Statements of Cash Flows		
Additions to property, plant and equipment	**101,988**	58,238
Additions to equipment costs (net)	**39,596**	34,862
Total of capital expenditures and equipment subsidies per Consolidated Statement of Cash Flows	**141,584**	93,100

Decrease (increase) in working capital related to capital expenditures	**2,857**	(3,034)
Less: Partnership capital expenditures [(1)]	**(5,899)**	(4,259)
Less: IRU prepayments [(2)]	**(366)**	(154)
Less: Satellite equipment profit [(3)]	**(819)**	(822)
Total capital expenditures and equipment subsidies reported by segments	**137,357**	84,831

(1) Consolidated capital expenditures include the Company s 38.3% proportionate share of the Burrard Landing Lot 2 Holdings Partnership (Partnership) capital expenditures which the Company is required to proportionately consolidate (see Note 1 to the Company s 2004 Consolidated Financial Statements). As the Partnership is financed by its own credit facility with limited recourse to the Company, the Partnership s capital expenditures are subtracted from the calculation of segmented capital expenditures and equipment subsidies.

(2) Prepayments on indefeasible rights to use (IRUs) certain specifically identified fibres in amounts not exceeding the costs to build the fiber subject to the IRUs are subtracted from the calculation of segmented capital expenditures and equipment subsidies.

(3) The profit from the sale of satellite equipment is subtracted from the calculation of segmented capital expenditures and equipment subsidies as the Company views the profit on sale as a recovery of expenditures on customer premise equipment.

Shaw Communications Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

November 30, 2004 and 2003
[all amounts in thousands of Canadian dollars, except per share amounts]

Assets

	November 30, 2004			
	Cable	**DTH**	**Satellite Services**	**Total**
	$	$	$	$
Segment assets	**5,840,071**	**916,180**	**558,825**	**7,315,076**
Corporate assets				**253,485**
Total assets				**7,568,561**

	August 31, 2004			
	Cable	**DTH**	**Satellite Services**	**Total**
	$	$	$	$
Segment assets	5,842,338	926,478	558,402	7,327,218
Corporate assets				229,686
Total assets				7,556,904

Shaw Communications Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

November 30, 2004 and 2003
[all amounts in thousands of Canadian dollars, except per share amounts]

3. LONG-TERM DEBT

		November 30, 2004			August 31, 2004		
	Effective interest rates %	**Translated at period end exchange rate**	**Adjustment for hedged debt[1]**	**Translated at hedged rate**	Translated at year end exchange rate	Adjustment for hedged debt[1]	Translated at hedged rate
		$	$	$	$	$	$
Corporate							
Bank loans [2]	Fixed and variable	**333,108**		**333,108**	295,433		295,433
Senior notes-							
Due April 11, 2005	7.05	**275,000**		**275,000**	275,000		275,000
Due October 17, 2007	7.40	**296,760**		**296,760**	296,760		296,760
US $440,000 due April 11, 2010	7.88	**521,840**	**120,780**	**642,620**	577,720	64,900	642,620
US $225,000 due April 6, 2011	7.68	**266,850**	**88,988**	**355,838**	295,425	60,413	355,838
US $300,000 due December 15, 2011	7.61	**355,800**	**121,050**	**476,850**	393,900	82,950	476,850
Due November 20, 2013	7.50	**350,000**		**350,000**	350,000		350,000
		2,399,358	**330,818**	**2,730,176**	2,484,238	208,263	2,692,501
Other subsidiaries and entities							
Videon CableSystems Inc. 8.15% Senior Debentures Series A due April 26, 2010	7.63	**130,000**		**130,000**	130,000		130,000

Burrard Landing Lot 2 Holdings Partnership [3]	variable	**42,341**		**42,341**	36,442		36,442
		172,341		**172,341**	166,442		166,442
Total consolidated debt		**2,571,699**	**330,818**	**2,902,517**	2,650,680	208,263	2,858,943
Less current portion [4]		**358,094**		**358,094**	343,097		343,097
		2,213,605	**330,818**	**2,544,423**	2,307,583	208,263	2,515,846

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(1) As required by GAAP, foreign denominated long-term debt is to be translated at the period-end foreign exchange rates. Because the Company follows hedge accounting, the resulting exchange gains and losses on translating hedged long-term debt are included in deferred charges or deferred credits. If the rate of translation was adjusted to reflect the hedged rates of the Company s cross-currency interest rate agreements (which fix the liability for interest and principal), long-term debt would increase by $330,818 (August 31, 2004 - $208,263) representing a corresponding amount in deferred credits. The hedged rates on the Senior notes of US $440,000, US $225,000 and US $300,000 are 1.4605, 1.5815 and 1.5895, respectively.

(2) Availabilities under banking facilities are as follows at November 30, 2004:

		Bank loans [a]			**Operating credit facilities [a]**
	Total	**Revolving [b]**	**Term [c]**	**Sub-total**	
	$	$	$	$	$
Total facilities	1,138,108	910,000	168,108	1,078,108	60,000
Amount drawn (excluding letters of credit of $1,231)	356,868	165,000	168,108	333,108	23,760
	781,240	745,000		745,000	36,240

(a) Bank loans represent liabilities classified as long-term debt. Operating credit facilities are for terms less than one year and accordingly are classified as bank indebtedness.

(b) The revolving credit facility is due April 30, 2009 and is unsecured and ranks pari passu with the senior secured notes.

(c) The term facilities are repayable in increasing semi-annual installments in April and October of each year until fully repaid on April 30, 2007.

Shaw Communications Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

November 30, 2004 and 2003
[all amounts in thousands of Canadian dollars, except per share amounts]

(3) The facilities have been extended until June 30, 2005.

(4) Current portion of long-term debt includes the current portion of the term facilities, the $275,000 Senior Notes and the Burrard Landing Lot 2 Holdings Partnership Loan.

4. SHARE CAPITAL

Issued and outstanding

Number of Securities			**November 30, 2004**	August 31, 2004
November 30, 2004	August 31,		$	$

(16)

(16)

Balance at December 31, 2012

5,180,000

95

51,800

57,366

5,330

114,591

Net income before dividends on preferred stock of subsidiary

9,892

9,892

Other comprehensive loss

(14,331)

(14,331)

Repurchase of common stock

(158,988)

(1,590)

(2,132)

(3,722)

Cash dividends declared, $0.74 per share

(3,741)

(3,741)

Cash dividends - preferred stock of subsidiary

(16)

(16)

Balance AT December 31, 2013

5,021,012

$

95

$

50,210

$

61,369

$

(9,001)

$

102,673

The accompanying notes are an integral part of the consolidated financial statements.

All dollar amounts are reported in thousands except share and per share data.

FIRST FARMERS AND MERCHANTS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

		Years Ended December 31,		
	(unaudited)	2013	2012	2011
OPERATING ACTIVITIES	Net income available for common shareholders	$ 9,876	$ 7,608	$ 6,996
	Adjustments to reconcile net income to net cash provided by (used in) operating activities			
	Provision for loan losses	-	1,120	3,125
	Provision for depreciation and amortization of premises and equipment	1,543	1,412	1,270
	Deferred tax benefit (expense)	1,950	(340)	(1,216)
	Net securities gains	(829)	(2,294)	(1,458)
	Gains on loans sold	(437)	(511)	(417)
	Proceeds from sale of mortgage loans held for sale	21,047	28,625	24,402
	Funding of mortgage loans held for sale	(18,481)	(28,065)	(23,985)
	Loss on other real estate owned	308	1,317	948
	Gain (loss) on sale of premises and equipment	38	(10)	-
	Amortization of investment security premiums, net of accretion of discounts	1,312	3,526	2,094
	Increase in cash surrender value of life insurance contracts	(497)	(705)	(717)
	(Increase) decrease in			
	Other assets	1,243	741	1,177
	Increase (decrease) in			
	Other liabilities	(287)	2,647	534
	Total adjustments	6,910	7,463	5,757
	Net cash provided by operating activities	16,786	15,071	12,753
INVESTING ACTIVITIES	Proceeds from sales of available-for-sale securities	137,150	421,346	140,580
	Proceeds from maturities and calls of available-for-sale securities	44,908	68,673	106,270
	Proceeds from maturities and calls of held-to-maturity securities	3,890	3,430	4,725
	Purchases of investment securities available-for-sale	(189,436)	(521,837)	(323,222)
	Net (increase) decrease in loans	(38,267)	(50,846)	38,031
	Proceeds from sale of other real estate owned	2,378	1,810	1,683
	Proceeds from sale of premises and equipment	799	-	-
	Purchases of premises and equipment	(831)	(786)	(263)
	Purchase of life insurance policies	(258)	(2,282)	(2,799)
	Net cash used in investing activities	(39,667)	(80,492)	(34,995)
FINANCING ACTIVITIES	Net increase in deposits	24,488	76,419	64,604
	Net increase in securities sold under agreements to repurchase	1,027	721	10,162
	Payments to FHLB borrowings	(10,100)	(7,000)	(7,000)
	Repurchase of common stock	(3,722)	(3,400)	(3,011)
	Cash dividends paid on common stock	(3,800)	(3,944)	(1,991)
	Net cash provided by financing activities	7,893	62,796	62,764
	Increase (decrease) in cash and cash equivalents	(14,988)	(2,625)	40,522
	Cash and cash equivalents at beginning of period	70,396	73,021	32,499
	Cash and cash equivalents at end of period	$ 55,408	$ 70,396	$ 73,021
	Supplemental disclosures of cash flow information			
	Cash paid during the period for expenses			
	Interest on deposits and borrowed funds	$ 2,816	$ 3,717	$ 5,235
	Income taxes	2,072	860	1,143
	Loans to facilitate sale of other real estate owned	1,905	1,774	-
	Real estate acquired in settlement of loans	312	1,355	1,375

The accompanying notes are an integral part of the consolidated financial statements.

All dollar amounts are reported in thousands except share and per share data.

NOTE 1 GENERAL AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Accounting Policies

The accounting principles followed and the methods of applying those principles conform with accounting principles generally accepted in the United States (GAAP) and to general practices in the banking industry. The significant accounting policies applicable to First Farmers and Merchants Corporation (the Corporation) are summarized as follows.

Nature of Operations

The Corporation is a bank holding company whose principal activity is the ownership and management of its wholly-owned subsidiary, First Farmers and Merchants Bank (the Bank). The Bank is primarily engaged in providing a full range of banking and financial services, including lending, investing of funds, obtaining deposits, trust and wealth management operations, and other financing activities to individual and corporate customers in the middle Tennessee area. The Bank is subject to competition from other financial institutions. The Corporation and Bank are subject to the regulation of certain federal and state agencies and undergo periodic examinations by those regulatory authorities.

Basis of Presentation

The accompanying consolidated financial statements present the accounts of the Corporation and its wholly-owned subsidiary, First Farmers and Merchants Bank. The Bank has the following direct and indirect subsidiaries: F & M West, Inc., Maury Tenn, Inc., and Maury Tenn Properties, Inc. Noncontrolling interests consist of preferred shares in Maury Tenn Properties, Inc. that are owned by third parties and Maury Tenn, Inc. The preferred shares in Maury Tenn Properties, Inc. receive dividends, which are included in the consolidated statements of income. Intercompany accounts and transactions have been eliminated in consolidation.

Certain items in prior financial statements have been reclassified to conform to the current presentation. These reclassifications had no effect on net income.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with GAAP requires management of the Corporation and the Bank to make estimates and assumptions that affect the reported amounts of assets and liabilities. Those estimates and assumptions also affect 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. Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan and lease losses, the fair value of financial instruments, the valuation of foreclosed real estate, valuation of goodwill, valuation of deferred tax assets and the liability related to post-retirement benefits.

Concentrations of Credit Risk

The Corporations banking activities include granting commercial, residential, and consumer loans to customers primarily located in central and south central Tennessee and Northern Alabama. The Corporation is continuing to manage all components of its portfolio mix in a manner to reduce risk from changes in economic conditions. Concentrations of credit, as defined for regulatory purposes, are reviewed quarterly by

management to ensure that internally established limits based on Tier 1 Capital plus allowance for loan losses and total capital are not exceeded. At December 31, 2013 our concentrations of commercial real estate, rental and leasing loans were 119.6% of Tier 1 Capital plus the allowance for loan and lease losses, respectively. Health care and social assistance loans were 46.3%. Manufacturing and construction loans were 25.4%. Wholesale trade credits were 25.2%. These percentages are within our internally established limits regarding concentrations of credit.

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Loans secured by non-farm, non-residential real estate comprised 29.0% of the loan portfolio at December 31, 2013. Management remains comfortable with the real estate exposure levels within the commercial loan portfolio. Management believes the commercial real estate portion remains well diversified across several different property types and several different geographic markets, stretching primarily from Davidson County, Tennessee to northern Alabama.

Cash and Due From Banks

Included in cash and due from banks are reserve amounts that are required to be maintained in the form of cash and balances due from the Federal Reserve Bank and other banks. At December 31, 2013, the Bank s required reserve was $2,560 at the Federal Reserve. From time to time throughout the year, the Bank s balances due from other financial institutions exceeded Federal Deposit Insurance Corporation (FDIC) insurance limits. The Bank had one account over the limit at December 31, 2013 and it was $261. Furthermore, federal funds sold are essentially uncollateralized loans to other financial institutions.

Cash Equivalents

The Corporation considers all liquid investments with original maturities of three months or less to be cash equivalents. Cash equivalents include cash on hand, cash due from banks and federal funds sold. Federal funds are sold for one-day periods.

Securities

Certain debt securities that management has the positive intent and ability to hold to maturity are classified as held to maturity and recorded at amortized cost. Securities not classified as held to maturity are classified as available for sale and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income, net of tax. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

For debt securities with fair value below amortized cost when the Corporation does not intend to sell a debt security, and it is more likely than not the Corporation will not have to sell the security before recovery of its cost basis, it recognizes the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income. For held-to-maturity debt securities, the amount of an other-than-temporary impairment recorded in other comprehensive income for the noncredit portion of a previous other-than-temporary impairment is amortized prospectively over the remaining life of the security on the basis of the timing of future estimated cash flows of the security.

If declines in fair value are other than temporary, the carrying value of the securities is written down to fair value as a realized loss with a charge to income for the portion attributable to credit losses and a charge to other comprehensive income for the portion that is not credit related. For available-for-sale and held-to-maturity debt securities that management has no intent to sell and believes that it more likely than not will not be required to sell prior to recovery, only the credit loss component of the impairment is recognized in earnings, while the noncredit loss is

recognized in accumulated other comprehensive income. The credit loss component recognized in earnings is identified as the amount of principal cash flows not expected to be received over the remaining term of the security based on cash flow projections.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoffs are reported at their outstanding principal balances adjusted for unearned income, charge-offs, the allowance for loan losses, any unamortized deferred fees or costs on originated loans and unamortized premiums or discounts on purchased loans.

For loans amortized at cost, interest income is accrued based on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, as well as premiums and discounts, are deferred and amortized as a level yield adjustment over the respective term of the loan.

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The accrual of interest on mortgage and commercial loans is discontinued at the time the loan is 90 days past due unless the credit is well-secured and in process of collection. Past-due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off are reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Discounts and premiums on purchased commercial loans are amortized to income using the interest method over the remaining period to contractual maturity and adjusted for anticipated prepayments.

Allowance for Loan and Lease Losses

The allowance for loan and lease losses is established through provisions for loan and lease losses charged against income. Loan losses are charged against the allowance when management determines that the uncollectibility of a loan has been confirmed. Subsequent recoveries, if any, are credited to the allowance account in the period received.

The adequacy of the allowance for loan and lease losses is evaluated quarterly in conjunction with loan review reports and evaluations that are discussed in meetings with loan officers, credit administration and the Corporation s Board of Directors. The Bank s past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect a borrower s ability to repay (including the timing of future payments), the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors are considered in this evaluation. This process is inherently subjective as it requires material estimates that are susceptible to significant change, including the amounts and timing of future cash flows expected to be received on impaired loans. The allowance for loan and lease losses is maintained at a level believed adequate by management to absorb estimated losses inherent in the loan portfolio.

A loan is considered impaired when it is probable that the Bank will be unable to collect all amounts due (principal and interest) according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower s prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan s effective interest rate, the loan s obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Groups of loans with similar risk characteristics are collectively evaluated for impairment based on the group s historical loss experience adjusted for changes in trends, conditions and other relevant factors that affect repayment of the loans. Accordingly, the Bank does not separately identify individual consumer and residential loans for impairment measurements, unless such loans are the subject of a restructuring agreement due to financial difficulties of the borrower.

When any secured commercial loan is considered uncollectable, whether past due or not, a current assessment of the value of the underlying collateral is made. If the balance of the loan exceeds the fair value of the collateral, the loan is placed on nonaccrual and the loan is charged down to the value of the collateral less estimated cost to sell or a specific reserve equal to the difference between book value of the loan and the fair value assigned to the collateral is created until such time as the loan is foreclosed. When the foreclosed collateral has been legally assigned to the Corporation, a charge off is taken, if necessary, in order that the remaining balance reflects the fair value estimated less costs to sell the collateral then transferred to other real estate owned or other repossessed assets. When any unsecured commercial loan is considered uncollectable the loan is charged off no later than at 90 days past due.

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All closed-end consumer loans (excluding conventional 1-4 family residential loans and installment and revolving loans secured by real estate) are charged off no later than 120 days (4 monthly payments) delinquent. If a loan is considered uncollectable, it is charged off earlier than 120 days delinquent. For conventional 1-4 family residential loans and installment and revolving loans secured by real estate, when a loan is 90 days past due, a current assessment of the value of the real estate is made. If the balance of the loan exceeds the fair value of the property, the loan is placed on nonaccrual and foreclosure proceedings are initiated. When the foreclosed property has been legally assigned to the Corporation, a charge-off is taken with the remaining balance, reflecting the fair value less estimated costs to sell, transferred to other real estate owned.

Loans Held for Sale

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to noninterest income. Gains and losses on loan sales are recorded in noninterest income. The Corporation does not retain servicing rights on loans sold. Loans held for sale at December 31, 2013 and 2012 totaled $327 and $2,456, respectively.

Other Real Estate

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value less cost to sell at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net income or expense from foreclosed assets.

When foreclosed properties are acquired current appraisals are obtained on the properties. Additionally, periodic updated appraisals are obtained on unsold foreclosed properties. When an updated appraisal reflects a market value below the current book value, a charge is booked to current earnings to reduce the property to its new market value less expected selling costs. Our policy for determining the frequency of periodic reviews is based upon consideration of the specific properties and the known or perceived market fluctuations in a particular market and is typically between 12 and 24 months.

Premises and Equipment

Premises and equipment are stated at cost, less accumulated depreciation and amortization. The provision for depreciation is computed principally on an accelerated method over the estimated useful life of an asset, which ranges from 15 to 39 years for buildings and from three to 25 years for equipment. Costs of major additions and improvements are capitalized. Expenditures for maintenance and repairs are charged to operations as incurred. Gains or losses from the disposition of property are reflected in operations, and the asset accounts and related allowances for depreciation are reduced.

Federal Reserve and Federal Home Loan Bank Stock

Federal Reserve and Federal Home Loan Bank stock are required investments for institutions that are members of the Federal Reserve and Federal Home Loan Bank systems. The required investment in the common stock is based on a predetermined formula, carried at cost and evaluated for impairment. At December 31, 2013 and 2012 Federal Reserve and Federal Home Loan Bank stock totaled $3,879.

Goodwill

Goodwill is evaluated annually for impairment. Quantitative and qualitative assessments are performed to determine whether the existence of events or circumstances leads to a determination that it is more likely than not the fair value is less than the carrying amount, including goodwill. If, based on the evaluation, it is determined to be more likely than not that the fair value is less than the carrying value, then goodwill is tested further for impairment. If the implied fair value of goodwill is lower than its carrying amount, a goodwill impairment is indicated and goodwill is written down to its implied fair value. Subsequent increases in goodwill value are not recognized in the financial statements.

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Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Corporation put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and (3) the Corporation does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

Income Taxes

The Corporation files consolidated income tax returns with its subsidiaries. The Corporation accounts for income taxes in accordance with income tax accounting guidance (ASC 740, *Income Taxes*). The income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Corporation determines deferred income taxes using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur. Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are reduced by a valuation allowance if, based on the weight of evidence available, it is more likely than not that some portion or all of a deferred tax asset will not be realized.

Tax positions are recognized if it is more likely than not, based on the technical merits, that the tax position will be realized or sustained upon examination. The term more likely than not means a likelihood of more than 50 percent; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any. A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances and information available at the reporting date and is subject to management s judgment. With a few exceptions, the Corporation is no longer subject to U.S. federal tax examinations for years before 2010, and state and local tax examinations by tax authorities for years before 2010.

The Corporation recognizes interest and penalties on income taxes as a component of income tax expense.

Securities Sold Under Agreements to Repurchase

Securities sold under agreements to repurchase, which are classified as secured borrowings, generally mature within one to four days from the transaction date. Securities sold under agreements to repurchase are reflected at the amount of cash received in connection with the transaction

Fair Value Measurements

FASB ASC Topic 820, Fair Value Measurements and Disclosures , defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and requires certain disclosures about fair value measurements. See Note 13 Fair Value Measurement. In general, fair values of financial instruments are based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as input, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality and the Corporation s creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time.

All dollar amounts are reported in thousands except share and per share data.

Shareholders Equity and Earnings Per Share

Basic earnings per share represent income available to shareholders divided by the weighted average number of shares of Corporation common stock outstanding during the period. Diluted earnings per share reflect additional shares of common stock that would have been outstanding if potentially dilutive shares of common stock had been issued, as well as any adjustment to income that would result from the assumed conversion. For the years ended December 31, 2013, 2012 and 2011, there were no potentially dilutive shares of common stock issuable.

In 2013, the Corporation adopted a plan to repurchase shares of its common stock. The plan allowed the purchase of up to 200,000 shares. The Corporation purchased 158,988 shares in 2013. In 2012, the Corporation adopted a plan to repurchase up to 150,000 shares of common stock . The Corporation repurchased 150,000 shares in 2012. For 2011, the Corporation adopted a similar plan allowing it to repurchase up to 100,000 shares of common stock. The Corporation repurchased 100,000 shares in 2011.

Comprehensive Income (Loss)

Comprehensive income (loss) consists of net income and other comprehensive income (loss), net of applicable income tax expenses or benefits. Other comprehensive (loss) income includes unrealized appreciation or depreciation on available-for-sale securities and changes in the net actuarial gain or loss of the postretirement benefit obligation.

The components of accumulated other comprehensive income (loss), included in shareholder s equity, are as follows as of December 31, 2013, 2012 and 2011:

	Years Ended December 31,		
	2013	2012	2011
Net unrealized gains (losses) on available-for-sale securities	$ (17,178)	$ 5,747	$ 4,914
Net actuarial gain on unfunded portion of postretirement benefit obligation	2,542	2,920	302
	(14,636)	8,667	5,216
Tax effect - (expense) benefit	5,635	(3,337)	(2,008)
Other comprehensive income (loss)	$ (9,001)	$ 5,330	$ 3,208

Transfers Between Fair Value Hierarchy Levels

Transfers in and out of Level 1 (quoted market prices), Level 2 (other significant observable inputs) and Level 3 (significant unobservable inputs) are recognized on the period end date.

Segment Reporting

Management analyzes the operations of the Corporation assuming one operating segment, community lending services.

Recent Accounting Pronouncements

ASU 2013-02, *Comprehensive Income (Topic 220) Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income.* ASU 2013-02 amends recent guidance related to the reporting of comprehensive income to enhance the reporting of reclassifications out of accumulated other comprehensive income. ASU 2013-02 became effective for the Corporation on January 1, 2013 and did not have a significant impact on the Corporation s financial statements. See Note 2 Other Comprehensive Income (Loss).

All dollar amounts are reported in thousands except share and per share data.

ASU 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax loss, or a Tax Credit Carryforward Exists (Topic 740-10) a consensus of the FASB Emerging Issues Task Force.* ASU 2013-11 provides guidance on financial statement presentation of an unrecognized tax benefit when a net operating loss (NOL) carryforward, a similar tax loss, or a tax credit carryforward exists. The objective is to eliminate diversity in practice resulting from a lack of guidance on this topic. ASU 2013-11 will be effective for the Corporation after December 15, 2013 and is not expected to have a significant impact on the Corporation s financial statements.

ASU 2013-12, Definition of a Public Business Entity An Addition to the Master Glossary amends the Master Glossary of the FASB Accounting Standards Codification to include one definition of public business entity for future use in U.S. GAAP. The definition of a public business entity will be used in considering the scope of new financial guidance and will identify whether the guidance does or does not apply to business entities. The amendment does not affect existing requirements, but instead improves U.S. GAAP by providing a single definition of public business entity for use in future financial accounting and reporting guidance. There is no actual effective date for the amendment in this Update. However, the term public business entity will be used beginning with ASU 2014-01. ASU 2013-12 is not expected to have a significant impact on the Corporation s financial statements.

ASU 2014-04, Receivables Troubled Debt Restructurings by Creditors (Subtopic 310-40) clarifies when an in substance repossession or foreclosure occurs that is, when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan such that the loan receivable should be derecognized and the real estate property recognized. The new update requires a creditor to reclassify a collateralized consumer mortgage loan to real estate property upon obtaining legal title to the real estate collateral, or the borrower voluntarily conveying all interest in the real estate property to the lender to satisfy the loan through a deed in lieu of foreclosure or similar legal agreement. The update is effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014 and is not expected to have a significant impact on the Corporation s financial statements.

NOTE 2 ACCUMULATED OTHER COMPREHENSIVE INCOME (AOCI) BY COMPONENT

Amounts reclassified from AOCI and the affected line items in the statements of income during the periods ended December 31, 2013, 2012 and 2011, were as follows:

Amounts Reclassified from AOCI Years Ended	Affected Line Item in the Statements of Income

	December 31, 2013	December 31, 2012	December 31, 2011	
Unrealized gains (losses) on available-for-sale securities	$ 829	$ 2,294	$ 1,458	Realized gain (loss) on sale of securities
	(319)	(883)	(561)	Tax (expense) benefit
	$ 510	$ 1,411	$ 897	Net reclassified amount
Amortization of defined benefit pension items				
Actuarial gains (losses)	$ (190)	$ -	$ 205	
	73	-	(79)	Tax (expense) benefit
	$ (117)	$ -	$ 126	Net reclassified amount
Total reclassifications out of AOCI	$ 393	$ 1,411	$ 1,023	

All dollar amounts are reported in thousands except share and per share data.

NOTE 3 SECURITIES

The amortized cost and fair value of securities available-for-sale and held-to-maturity at December 31, 2013 and 2012 are summarized as follows:

December 31, 2013	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale securities				
U.S. Government agencies	$ 112,863	$ -	$ 7,791	$ 105,072
U.S. Government sponsored agency mortgage backed securities	168,045	27	10,649	157,423
States and political subdivisions	45,237	1,240	140	46,337
Corporate bonds	20,747	280	145	20,882
	$ 346,892	$ 1,547	$ 18,725	$ 329,714
Held-to-maturity securities				
States and political subdivisions	$ 27,839	$ 756	$ -	$ 28,595

December 31, 2012	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale securities				
U.S. Government agencies	$ 143,897	$ 400	$ 280	$ 144,017
U.S. Government sponsored agency mortgage backed securities	131,917	1,856	55	133,718
States and political subdivisions	47,273	3,306	-	50,579
Corporate bonds	16,884	529	9	17,404
	$ 339,971	$ 6,091	$ 344	$ 345,718
Held-to-maturity securities				
States and political subdivisions	$ 31,755	$ 1,665	$ -	$ 33,420

Certain investments in debt securities are reported in the financial statements at an amount less than their historical cost. Total fair value of these investments at December 31, 2013 and 2012 was approximately $269,691 and $83,579, which was approximately 75% and 22%, respectively, of the Corporation s available-for-sale and held-to-maturity investment portfolio. The Corporation evaluates its investment portfolio on a quarterly basis for impairment. The analysis performed as of December 31, 2013 and December 31, 2012 indicated that all impairment was considered temporary, market driven due primarily to fluctuations in market interest rates and not credit-related.

The following table shows the Corporation s investments gross unrealized losses and fair value of the Corporation s investments with unrealized losses that were not deemed to be other-than-temporarily impaired, aggregated by investment class and length of time that individual securities had been in a continuous unrealized loss position at December 31, 2013 and 2012:

December 31, 2013	Less than 12 months		12 months or Greater		Total	
Type of Security	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
US Government agencies	$ 100,533	$ 7,330	$ 4,539	$ 461	$ 105,072	$ 7,791
US Government sponsored agency mortgage backed securities	144,134	10,073	8,698	576	152,832	10,649
States and political subdivisions	2,615	140	-	-	2,615	140
Corporate bonds	8,590	121	582	24	9,172	145

	$ 255,872	$ 17,664	$ 13,819	$ 1,061	$ 269,691	$ 18,725

	Less than 12 months		12 months or Greater		Total	
December 31, 2012 Type of Security	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
US Government agencies	$ 68,979	$ 280	$ -	$ -	$ 68,979	$ 280
US Government sponsored agency mortgage backed securities	12,881	55	-	-	12,881	55
Corporate bonds	1,719	9	-	-	1,719	9
	$ 83,579	$ 344	$ -	$ -	$ 83,579	$ 344

All dollar amounts are reported in thousands except share and per share data.

The unrealized losses on the Corporation s investments in direct obligation of U.S. government agencies and U.S. government sponsored agency mortgage backed securities were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. Because the Corporation does not intend to sell the investments and it is not more likely than not the Corporation will be required to sell the investments before recovery of their amortized basis, which may be maturity, the Corporation does not consider those investments to be other-than-temporarily impaired at December 31, 2013.

The amortized cost and fair value of available-for-sale securities and held-to-maturity securities at December 31, 2013, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-Sale		**Held-to-Maturity**	
December 31, 2013	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Within one year	$ 5,841	$ 5,920	$ 3,135	$ 3,208
One to five years	26,404	26,489	7,043	7,305
Five to ten years	131,468	124,308	16,554	16,953
After ten years	15,134	15,574	1,107	1,129
Mortgage-backed securities	168,045	157,423	-	-
Total	$ 346,892	$ 329,714	$ 27,839	$ 28,595

The carrying value of securities pledged as collateral to secure public deposits and for other purposes was $210,494 at December 31, 2013 and $210,800 at December 31, 2012.

The book value of securities sold under agreements to repurchase amounted to $34,978 and $26,500 at December 31, 2013 and 2012, respectively.

Gross gains of $1,026, $2,455and $1,509 resulting from sales of available-for-sale securities were realized for at December 31, 2013, 2012 and 2011, respectively. A loss of $197 was included in the net gain of $829 for December 31, 2013. A loss of $161 was included in the net gain of $2,294 for December 31, 2012. Losses of $51 were included in the net gain of $1,458 for December 31, 2011.

NOTE 4 LOANS

The following table presents the Bank s loans by category as of December 31, 2013 and 2012:

	December 31, 2013	December 31, 2012
Commercial		

Commercial and industrial	$ 94,702	$ 83,631
Non-farm, nonresidential real estate	176,213	167,565
Construction and development	29,938	36,323
Commercial loans secured by real estate	26,940	23,983
Other commercial	26,582	24,423
Total commercial	**354,375**	**335,925**
Residential		
Consumer loans	10,957	11,621
Single family residential	213,763	196,349
Other retail	27,671	23,264
Total residential and consumer	**252,391**	**231,234**
	$ 606,766	**$ 567,159**
Less:		
Allowance for possible loan losses	(8,595)	(8,809)
Total net loans	**$ 598,171**	**$ 558,350**

All dollar amounts are reported in thousands except share and per share data.

Loan Origination/Risk Management. The Corporation has certain lending policies and procedures in place that are designed to maximize loan income within an acceptable level of risk. Management reviews and approves these policies and procedures on a regular basis. A reporting system supplements the review process by providing management with frequent reports related to loan production, loan quality, concentrations of credit, loan delinquencies and non-performing and potential problem loans. Diversification in the loan portfolio is a means of managing risk associated with fluctuations in economic conditions.

Commercial and industrial loans are underwritten after evaluating and understanding the borrower s ability to operate profitably and prudently expand its business. Underwriting standards are designed to promote relationship banking rather than transactional banking. Once it is determined that the borrower s management possesses sound ethics and solid business acumen, the Corporation s management examines current and projected cash flows to determine the ability of the borrower to repay their obligations as agreed. Commercial and industrial loans are primarily made based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial and industrial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory and may incorporate a personal guarantee; however, some short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

Commercial real estate loans are subject to underwriting standards and processes similar to commercial and industrial loans, in addition to those of real estate loans. These loans are viewed primarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is largely dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. Management monitors and evaluates commercial real estate loans based on collateral, geography and risk grade criteria. As a general rule, the Corporation avoids financing single-purpose projects unless other underwriting factors are present to help mitigate risk. The Corporation also utilizes third-party experts to provide insight and guidance about economic conditions and trends affecting market areas it serves. In addition, management tracks the level of owner-occupied commercial real estate loans versus non-owner occupied loans. At December 31, 2013, approximately seventy percent of the outstanding principal balance of the Corporation s commercial real estate loans was secured by owner-occupied properties, compared to eighty percent at December 31, 2012.

With respect to loans to developers and builders that are secured by non-owner occupied properties that the Corporation may originate from time to time, the Corporation generally requires the borrower to have had an existing relationship with the Corporation and have a proven record of success. Construction loans are underwritten utilizing feasibility studies, independent appraisal reviews, sensitivity analysis of absorption and lease rates and financial analysis of the developers and property owners. Construction loans are generally based upon estimates of costs and value associated with the complete project. These estimates may be inaccurate. Construction loans often involve the disbursement of substantial funds with repayment substantially dependent on the success of the ultimate project. Sources of repayment for these types of loans may be pre-committed permanent loans from approved long-term lenders, sales of developed property or an interim loan commitment from the Corporation until permanent financing is obtained. These loans are closely monitored by on-site inspections and are considered to have higher risks than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, governmental regulation of real property, general economic conditions and the availability of long-term financing.

The Corporation originates residential and consumer loans utilizing a computer-based credit scoring analysis to supplement the underwriting process. To monitor and manage consumer loan risk, policies and procedures are developed and modified, as needed, jointly by line and staff personnel. This activity, coupled with relatively small loan amounts that are spread across many individual borrowers, minimizes risk. Additionally, trend and outlook reports are reviewed by management on a regular basis. Underwriting standards for home equity loans are heavily influenced by statutory requirements, which include, but are not limited to, a maximum loan-to-value percentage of 80%, collection remedies, the number of such loans a borrower can have at one time and documentation requirements.

All dollar amounts are reported in thousands except share and per share data.

The Corporation contracts with a third party vendor to perform loan reviews. The Corporation reviews and validates the credit risk program on an annual basis. Results of these reviews are presented to management. The loan review process complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel, as well as the Corporation s policies and procedures.

The goal of the bank is to diversify loans to avoid a concentration of credit in a specific industry, person, entity, product, service, or any area vulnerable to a tax law change or an economic event. A concentration of credit occurs when obligations, direct or indirect, of the same or affiliated interests represent 15 percent or more of the Bank s capital structure. Commercial real estate rental and leasing represented the highest concentration at 120% of tier 1 capital. The Board of Directors recognizes that the Bank s geographic trade area imposes some limitations regarding loan diversification if the bank is to perform the function for which it has been chartered. Specifically, lending to qualified borrowers within the bank s trade area will naturally cause concentrations of real estate loans in the primary communities served by the bank and loans to employees of major employers in the area.

The following table provides details regarding the aging of the Bank s loan portfolio:

December 31, 2013	30 - 89 Days Past Due	90 Days and Greater Past Due	Total Past Due	Current	Total Loans
Retail					
Consumer	$ 182	$ 3	$ 185	$ 10,772	$ 10,957
Single family residential	3,805	83	3,876	209,887	213,763
Other retail	319	28	359	27,312	27,671
Retail total	$ 4,306	$ 114	$ 4,420	$ 247,971	$ 252,391
Commercial					
Commercial and industrial	$ 428	$ 1,328	$ 1,756	$ 92,946	$ 94,702
Non-farm, non-residential real estate	393	-	393	175,820	176,213
Construction and development	-	28	28	29,910	29,938
Commercial loans secured by real estate	38	178	216	26,724	26,940
All other commercial	-	1,249	1,249	25,333	26,582
Commercial total	$ 859	$ 2,783	$ 3,642	$ 350,733	$ 354,375
Total	$ 5,165	$ 2,897	$ 8,062	$ 598,704	$ 606,766
December 31, 2012	30 - 89 Days Past Due	90 Days and Greater Past Due	90 Days and Greater Past Due	Current	Total Loans
Retail					
Consumer	$ 112	$ 7	$ 119	$ 11,502	$ 11,621
Single family residential	3,543	387	3,930	192,419	196,349
Other retail	193	-	193	23,071	23,264
Retail total	$ 3,848	$ 394	$ 4,242	$ 226,992	$ 231,234
Commercial					
Commercial and industrial	$ 618	$ 1,457	$ 2,075	$ 81,556	$ 83,631
Non-farm, non-residential real estate	666	448	1,114	166,451	167,565
Construction and development	160	-	160	36,163	36,323
Commercial loans secured by real estate	22	193	215	23,768	23,983

All other commercial	741	1,379	2,120	22,303	24,423
Commercial total	$ 2,207	$ 3,477	$ 5,684	$ 330,241	$ 335,925
Total	$ 6,055	$ 3,871	$ 9,926	$ 557,233	$ 567,159

All dollar amounts are reported in thousands except share and per share data.

A loan is considered impaired, in accordance with the impairment accounting guidance (ASC 310-10-35-16), when based on current information and events, it is probable the Corporation will be unable to collect all amounts due from the borrower in accordance with the contractual terms of the loan. Impaired loans include nonperforming commercial loans but also include loans modified in troubled debt restructurings.

The following table summarizes the impaired loans by loan type as of December 31, 2013 and 2012:

December 31, 2013	Unpaid Contractual Principal Balance	Recorded investment with no allowance	Recorded Investment with allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment Year To Date	Interest Received	Interest A ccrued
Commercial								
Commercial and industrial	$ 2,190	$ 1,338	$ 234	$ 1,572	$ 16	$ 1,620	$ 23	$ 134
Non-farm, non-residential real estate	3,236	1,155	1,551	2,706	282	2,819	157	168
Construction and development	461	461	-	461	44	556	30	30
Other commercial	3,834	3,310	178	3,488	-	3,704	225	241
Commercial total	9,721	6,264	1,963	8,227	342	8,699	435	573
Retail								
Single family residential	1,121	568	419	987	118	1044	52	55
Other retail	11	-	11	11	11	11		
Retail total	1,132	568	430	998	129	1,097	52	55
Total	$ 10,853	$ 6,382	$ 2,393	$ 9,225	$ 471	$ 9,796	$ 487	$ 628

December 31, 2012	Unpaid Contractual Principal Balance	Recorded investment with no allowance	Recorded Investment with allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment Year To Date	Interest Received	Interest Accrued
Commercial								
Commercial and industrial	$ 2,036	$ 1,076	$ 328	$ 1,404	$ 103	$ 3,483	$ 74	$ 259
Non-farm, non-residential real estate	3,613	2,417	-	2,417	-	1,606	83	78
Construction and development	682	-	682	682	118	682	35	40
Other commercial	3,124	3,124	-	3,124		3,520	126	279
Commercial total	9,455	6,617	1,010	7,627	221	9,291	318	656
Retail								
Single family residential	1,237	402	613	1,015	82	638	39	64
Retail total	1,237	402	613	1,015	82		39	64
Total	$ 10,692	$ 7,019	$ 1,623	$ 8,642	$ 303	$ 9,291	$ 357	$ 720

December 31, 2011	Unpaid Contractual Principal Balance	Recorded investment with no allowance	Recorded Investment with allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment Year To Date	Interest Received	Interest Accrued
Commercial								
Commercial and industrial	$ 5,839	$ 738	$ 5,678	$ 5,446	$ 601	$ 5,069	$ 193	$ 337
Non-farm, non-residential real estate	4,378	2,986	2,115	4,573	307	5,232	35	70
Construction and development	870	-	870	870	203	941	39	45
Other commercial	3,238	-	-	1,498	-	1,527	190	310
Commercial total	14,325	3,724	8,663	12,387	1,111	12,769	457	762

Retail								
Single family residential	1,388	142	1,075	1,217	131	1,269	44	68
Retail total	1,388	142	1,075	1,217	131	1,269	44	68
Total	$ 15,713	$ 3,866	$ 9,738	$ 13,604	$ 1,242	$ 14,038	$ 501	$ 830

* Interest income received is recognized interest income and approximates cash basis.

All dollar amounts are reported in thousands except share and per share data.

Non-accrual loans, segregated by class of loans, were as follows at December 31, 2013 and 2012:

	2013		2012	
Commercial and industrial	$	1,649	$	1,595
Nonfarm, nonresidential real estate	737		1,372	
Construction and development	68		50	
Commercial real estate	6		126	
Other commercial	1,248		1,379	
Consumer	21		11	
Single family residential	1,667		3,541	
Total	$	5,396	$	8,074

Included in certain loan categories of impaired loans are certain loans that have been modified in a troubled debt restructuring where economic concessions have been granted to borrowers who have experienced financial difficulties. These concessions typically result from our loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Modifications of terms for our loans and their inclusion as troubled debt restructurings are based on individual facts and circumstances. Loan modifications that are included as troubled debt restructurings may involve either an increase or reduction of the interest rate, extension of the term of the loan, or deferral of principal and/or interest payments, regardless of the period of the modification. All of the loans identified as troubled debt restructuring were modified due to financial stress of the borrower. In order to determine if a borrower is experiencing financial difficulty, an evaluation is performed to determine the probability that the borrower will be in payment default on any of its debt in the foreseeable future with the modification. This evaluation is performed under the Corporation s internal underwriting policy.

When the Corporation modifies loans in a troubled debt restructuring, the Corporation evaluates any possible impairment similar to other impaired loans based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan or lease agreement, or use the current fair value of the collateral, less selling costs for collateral dependent loans. If the corporation determined that the value of the modified loan is less than the recorded investment in the loan, impairment is recognized through an allowance estimate or a charge-off to the allowance. In periods subsequent to modification, the Corporation evaluates all troubled debt restructuring, including those that have payment defaults, for possible impairment and recognize impairment through the allowance.

As of December 31, 2013, the Corporation did not have any commitments to extend additional funds to borrowers with loans modified and included as a troubled debt restructuring.

During 2013, certain loans were modified in troubled debt restructurings, where economic concessions were granted to borrowers consisting of reductions in the interest rates, payment extensions, forgiveness of principal, and forbearances. Presented below, segregated by class of loans, are troubled debt restructurings that occurred during the year ended December 31, 2013 and 2012:

(dollars in thousands)	2013 Number of Loans	Post - Modification Outstanding Balance	Net Charge-offs Resulting from Modifications	2012 Number of Loans	Post -Modification Outstanding Balance	Net Charge-offs Resulting from Modifications
Commercial:						
Commercial and industrial	-	$ -	$ -	1	$ 8	$ -
Nonfarm nonresidential	-	-	-	1	361	-
Retail:						
Consumer	3	8	-	1	3	-
Single family residential	3	167	6	3	237	-
Total trouble debt restructurings	6	$ 175	$ 6	6	$ 609	$ -

All dollar amounts are reported in thousands except share and per share data.

Loans retain their accrual status at the time of their modification. As a result, if a loan is on nonaccrual status at the time it is modified, it stays as no-accrual status, and if a loan is on accrual status at the time of the modification, it generally stays on accrual status. Commercial and consumer loans modified in a troubled debt restructuring are closely monitored for delinquency as an early indicator of possible future default. If loans modified in a troubled debt restructuring subsequently default, the Corporation evaluates the loan for possible further impairment. The allowance for loan losses may be increased, adjustments may be made in the allocation of the allowance, or partial charge-offs may be taken to further write-down the carrying value of the loan. The Corporation considers a loan in default when it is 90 days or more past due or transferred to nonaccrual.

As of December 31, 2013 and 2012, the Corporation did not have any loans that were modified in troubled debt restructurings during the past twelve months that have subsequently defaulted.

Credit Quality Indicators. As part of the on-going monitoring of the credit quality of the Corporation s loan portfolio, management tracks certain credit quality indicators including trends related to (i) the weighted-average risk grade of commercial loans, (ii) the level of classified commercial loans, (iii) net charge-offs, (iv) non-performing loans and (v) the general economic conditions in the State of Tennessee.

The Corporation uses a risk grading matrix to assign a risk grade to each of its commercials loans. Loans are graded on a scale of 1 8. A description of the general characteristics of the 8 risk grades is as follows:

Risk Rating 1: Minimal Risk

General Characteristics:

- Substantially risk free.
- Federal, state, or municipal subdivisions with acceptable investment grade credit rating.
- Large national, regional, or local entity with proven access to capital markets.
- Diversity in its line of business with stable and diversified sales base.
- Borrower is considered to be an industry leader with many consecutive years of strong profits and exhibits a financial condition, equity position, liquidity, and debt service capacity far exceeding industry norms.
- Borrower has an abundance of unpledged financeable assets coupled with superior cash generation capabilities.
- Industry conditions and trends are positive and strong.
- Borrower has strong management with evidence of management succession.
- Credit rating by Moody s, Standard & Poor, or other qualified rating agency that is grade A or higher.
- A cash secured loan with the cash on deposit in our bank or a guaranty from the Federal government also warrants this risk rating.

Risk Rating 2: Modest Risk

General Characteristics:

- Borrower shows strong profitability, liquidity, and capitalization better than industry norms and a strong market position in the region.
- Borrower may have limited access to public markets for short-term needs or capital requirements, but has ready access to alternative financing.
- Loans may be unsecured based on the financial strength of the borrower or secured by collateral that is considered liquid and marketable.
- Borrower has a proven history of profitability and financial stability.
- Borrower has a strong market position in its industry and has an abundance of financeable assets available to protect the bank s position.
- Proven and steady management with good management succession.
- Borrower can withstand major market instabilities of short duration.
- Credit rating by Moody s, Standard & Poor, or other qualified rating agency that is grade BAA or higher.

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Risk Rating 3: Average Risk

General Characteristics:

- Borrower shows a stable earnings history and financial condition in line with industry norms with indications that these trends will continue.
- The credit extension is considered sound, however elements may be present which suggest the borrower may not be free from temporary impairments in the future.
- Liquidity and leverage is in line with industry norms.
- Good management with acceptable management succession.
- Under most economic and business conditions has access to alternative financing but limited or no access to capital markets for short-term or capital needs.
- Borrower may be an individual with a sound financial condition and liquidity with proven historical income to repay the debt as scheduled.
- Credit extensions are generally secured by acceptable collateral.

Risk Rating 4: Acceptable Risk

General Characteristics:

- Credit is to a borrower with smaller margins of debt service coverage and with some elements of reduced financial strength.
- Borrower is generally in a lower average market position in its industry.
- Borrower shows satisfactory asset quality and liquidity, good debt capacity and coverage, and good management in critical positions.
- Management is of unquestioned character but management succession may be questionable.
- Borrower can obtain similar financing from other financial institutions.
- Interim losses or moderately declining earnings trends may occur, but the borrower has sufficient strength and financial flexibility to offset these issues.
- Credit may be to individuals with a moderately leveraged financial condition, but with satisfactory liquidity and income to cover debt repayment requirements.
- Business borrowers may have moderate leverage, but must have historically consistent cash flow to cover debt service and other operating needs.
- Business borrowers may also have erratic or cyclical operating performances but should demonstrate strong equity positions to support these profitability swings.
- Asset-based loans that have stabilized and proven performance with the financial capacity to provide for annual clean up may qualify for this rating.
- Borrower has no access to capital markets, but would be financeable by another financial institution or finance company.
- Credit extensions are generally secured by acceptable collateral.

Risk Rating 5: Pass / Watch

General Characteristics:

Loans considered for this risk rating require a heightened level of supervision.

A) Transitional, Event Driven This category of risk rated 5 loans captures responses to **early warning signals from a relationship and, therefore, signifies a specific, event-driven, transitional credit grade.** The event is generally something unplanned or unexpected such as a death, a disaster, the loss of a major client, product line, or key employee; divorce, or health condition of the owner or key management person. The Risk Rating 5 category may be used in transitional upgrades as well as transitional downgrades of credit relationships. Under these criteria, the risk rating 5 necessitates a plan of action to either upgrade the credit to a Pass rating (Risk Rating 1-4), downgrade the credit to a criticized asset, or exit the relationship within six months.

All dollar amounts are reported in thousands except share and per share data.

B) **Ongoing Supervision Warranted -** This risk rating may also be utilized to identify loans having inherent characteristics which warrant more than the normal level of supervision. Loans meeting these criteria may include larger, more complex loans with unusual structures. Loans, which, due to structure or nature of the collateral require above average servicing, may also be considered for this risk rating. Unlike other criteria listed previously for the Pass / Watch risk rating, these particular characteristics tend not to be one-time or transitional in nature; therefore, these loans may be expected to remain in this risk rating category longer than six months. A loan might remain in this risk rating category for its life or until the characteristic warranting the Pass / Watch rating can be eliminated or effectively mitigated.

- Borrowers may exhibit declining earnings, strained cash flow, increasing leverage, or weakening market positions that indicate a trend toward an unacceptable risk.
- Borrower s liquidity, leverage, and earnings performance is below or trending below industry norms.
- Interim losses and other adverse trends may occur, but not to the level that would impair the bank s position.
- Borrower may be a newly formed company or in a new line of business or may be an established business with new or unproven management. Borrower should be adequately capitalized, but may not yet have achieved stabilized cash flow.
- Borrower generally has a small market position in its industry.
- Borrower may be engaged in an industry that is experiencing an economic downturn or is particularly susceptible to uncontrollable external factors.
- Management is of good character although some management weakness may exist, including lack of depth or succession.
- Borrowers generally have limited additional debt capacity and modest coverage, and average or below-average asset quality, margins, and market share.
- Borrower s ability to obtain financing from other financial institutions may be impaired.
- Credit to individuals with marginal financial condition and liquidity, but with income still sufficient to service the debt.

Risk Rating 6: Special Mention

A special mention asset has potential weaknesses that deserve management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution s credit position at some future date. Special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

General Characteristics:

- Cash flow may not be sufficient to fund anticipated cash needs.
- Sufficiently or modestly sufficiently financeable assets are available to protect the bank s position.
- Adverse trends in operations/profits or unbalanced position in the balance sheet, but not to the point where repayment is in jeopardy.
- Borrower generally shows limited liquidity or high leverage.
- Borrower s financial position is in the lower quartile of industry norms.
- Business exhibits a deteriorating market position in the industry.
- Management lacks depth and succession.
- Business is unable to withstand temporary setbacks without affecting repayment capability.
- Borrower is not financeable by another bank but possibly by a finance company or specialized lender.

Risk Rating 7: Substandard

A substandard asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness, or weaknesses, that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected.

All dollar amounts are reported in thousands except share and per share data.

General Characteristics:

- The primary source of repayment no longer provides satisfactory support and repayment is dependent on secondary sources.
- A substandard loan is inadequately protected by the current sound worth and paying capacity of the obligor or by the collateral pledged, if any.
- Normal repayment from the borrower is impaired although no loss of principal is envisioned.
- A partial loss of interest or principal will occur if the deficiencies are not corrected.
- Cash flow is generally not sufficient to fund anticipated cash needs.
- Financeable assets may not be sufficient to protect the bank s position.
- Adverse trends in operations that jeopardized debt repayment may require the borrower to undertake a significant reorganization of financing or the business.
- Borrower shows poor liquidity and high leverage impairing the repayment of the debt in accordance with agreed upon terms.
- Management lacks depth and succession; may be inexperienced or of questionable character.
- Borrower s market position in the industry is deteriorating.
- Borrower is not financeable by another bank or finance company.

Risk Rating 8: Doubtful

An asset classified doubtful has all the weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

General Characteristics:

- **Inadequate primary source of repayment**. **Assumes a less than satisfactory secondary source of repayment on a most-likely case basis.** There may be **an adequate secondary source of repayment on a best-case basis.**
- Borrowers have the same weaknesses found in **Substandard** borrowers.
- Loss probability is extremely high but because of certain important and reasonably specific factors that may work to strengthen the loan, its classification as an estimated loss is deferred until a more exact status may be determined.
- Pending factors may include proposed merger or acquisition; liquidation procedures; capital injections; perfecting liens on additional collateral; and refinancing plans.
- Cash flow is insufficient to fund cash needs.
- Financeable assets are insufficient to protect the bank s position.
- Source of debt repayment is dependent on liquidation of assets with a probable loss.
- Borrower may no longer be a going concern, or may not exist as a going concern for the foreseeable future.
- No alternative financing sources exist.

The following table presents risk grades and classified loans by class for year ending December 31, 2013 and 2012:

December 31, 2013

Commercial Loan Portfolio: Credit	Commercial and Industrial	Non-Farm, Non-Residential Real	Construction and	Commercial Loans	All Other Commercial	Commercial Loan Totals

Risk Rating 7: Substandard

risk profile by internally assigned grade		Estate Loans	Development	Secured by Residential R/E	Loans	
Pass	$ 92,155	$ 170,585	$ 29,463	$ 26,516	$ 24,131	$ 342,850
Special Mention	836	3,883	-	-	179	4,898
Substandard	635	1,745	475	424	1,023	4,302
Doubtful	1,076	-	-	-	1,249	2,325
TOTALS	$ 94,702	$ 176,213	$ 29,938	$ 26,940	$ 26,582	$ 354,375

All dollar amounts are reported in thousands except share and per share data.

Retail Loan Portfolio: Credit risk profiles based on delinquency status classification	Consumer Loans	Single-Family Residential**	All Other Retail Loans	Retail Loan Totals
Performing	$ 10,9366	$ 212,096	$ 27,643	$ 250,675
Nonperforming*	21	1,667	28	1,716
TOTALS	$ 10,957	$ 213,763	$ 27,671	$ 252,391

December 31, 2012

Commercial Loan Portfolio: Credit risk profile by internally assigned grade	Commercial and Industrial	Non-Farm, Non-Residential Real Estate Loans	Construction and Development	Commercial Loans Secured by Residential R/E	All Other Commercial Loans	Commercial Loan Totals
Pass	$ 81,560	$ 164,290	$ 35,543	$ 21,660	$ 22,857	$ 325,910
Special Mention	269	815	98	398	-	1,580
Substandard	726	2,460	682	1,925	187	5,980
Doubtful	1,076	-	-	-	1,379	2,455
TOTALS	$ 83,631	$ 167,565	$ 36,323	$ 23,983	$ 24,423	$ 335,925

Retail Loan Portfolio: Credit risk profiles based on delinquency status classification	Consumer Loans	Single-Family Residential**	All Other Retail Loans	Retail Loan Totals
Performing	$ 11,610	$ 192,808	$ 23,131	$ 227,549
Nonperforming*	11	3,541	133	3,685
TOTALS	$ 11,621	$ 196,349	$ 23,264	$ 231,234

*Loans are classified as nonperforming loans and are automatically placed on nonaccrual status once they reach 90 days past due. For purposes of this table all loans graded substandard or below are including in nonperforming.

**Single-family residential loans includes primary liens, closed-end secondary liens, residential construction loans, and home equity lines of credit.

NOTE 5 ALLOWANCE FOR LOAN AND LEASE LOSSES

Allowance for Possible Loan Losses. The allowance for possible loan losses is a reserve established through a provision for possible loan losses charged to expense, which represents management s best estimate of probable losses that have been incurred within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated loan losses and risks inherent in the loan portfolio. The Corporation s allowance for possible loan loss methodology includes allowance allocations calculated in accordance with ASC Topic 310, Receivables and allowance allocations calculated in accordance with ASC Topic 450, Contingencies. Accordingly, the methodology is based on historical loss experience by type of credit and internal risk grade, specific homogeneous risk pools and specific loss allocations, with adjustments for current events and conditions. The Corporation s process for determining the appropriate level of the allowance for possible loan losses is designed to account for credit deterioration as it occurs. The provision for possible loan losses reflects loan quality trends, including the levels of and trends related to nonaccrual loans, past due loans, potential problem loans, criticized loans and net charge-offs or recoveries, among other factors. The provision for possible loan losses also reflects the totality of actions taken on all loans for a particular period. In other words, the amount of the provision reflects not only the necessary increases in the allowance for possible loan losses related to newly identified criticized loans, but it also reflects actions taken related to other loans including, among other things, any necessary increases or decreases in required allowances for specific loans or loan pools.

All dollar amounts are reported in thousands except share and per share data.

The level of the allowance reflects management s continuing evaluation of industry concentrations, specific credit risks, loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions and unidentified losses inherent in the current loan portfolio. Portions of the allowance may be allocated for specific credits; however, the entire allowance is available for any credit that, in management s judgment, should be charged off. While management utilizes its best judgment and information available, the ultimate adequacy of the allowance is dependent upon a variety of factors beyond the Corporation s control, including, among other things, the performance of the Corporation s loan portfolio, the economy, changes in interest rates and the view of the regulatory authorities toward loan classifications.

The Corporation s allowance for possible loan losses consists of three elements: (i) specific valuation allowances determined in accordance with ASC Topic 310 based on probable losses on specific loans; (ii) historical valuation allowances determined in accordance with ASC Topic 450 based on historical loan loss experience for similar loans with similar characteristics and trends, adjusted, as necessary, to reflect the impact of current conditions; and (iii) general valuation allowances determined in accordance with ASC Topic 450 based on general economic conditions and other qualitative risk factors both internal and external to the Corporation.

The allowances established for probable losses on specific loans are based on a regular analysis and evaluation of problem loans. Commercial loans are classified based on an internal credit risk grading process that evaluates, among other things: (i) the obligor s ability to repay; (ii) the underlying collateral, if any; and (iii) the economic environment and industry in which the borrower operates. This analysis is performed at the relationship manager level for all commercial loans. When a loan has a calculated grade of 7 or higher, a special assets officer analyzes the loan to determine whether the loan is impaired and, if impaired, the need to specifically allocate a portion of the allowance for possible loan losses to the loan. Specific valuation allowances are determined by analyzing the borrower s ability to repay amounts owed, collateral deficiencies, the relative risk grade of the loan and economic conditions affecting the borrower s industry, among other things.

Historical valuation allowances are calculated based on the historical loss experience of specific types of loans and the internal risk grade of such loans at the time they were charged-off. The Corporation calculates historical loss ratios for pools of similar loans with similar characteristics based on the proportion of actual charge-offs experienced to the total population of loans in the pool. The historical loss ratios are periodically updated based on actual charge-off experience. A historical valuation allowance is established for each pool of similar loans based upon the product of the historical loss ratio and the total dollar amount of the loans in the pool. The Corporation s pools of similar loans include similarly risk-graded groups of commercial and industrial loans, commercial real estate loans, consumer real estate loans and consumer and other loans.

The components of the general valuation allowance include (i) the additional reserves allocated to specific loan portfolio segments as a result of applying an environmental risk adjustment factor to the base historical loss allocation and (ii) the additional reserves that are not allocated to specific loan portfolio segments including allocations for groups of similar loans with risk characteristics that exceed certain concentration limits established by management.

There is an inherent imprecision in calculating the specific portion of the allowance for loan and lease losses (ALLL). Therefore, a factor has been added to the allocation of each of the identified segments of the loan portfolio to account for the imprecision.

Risk Rating 7: Substandard

Included in the general valuation allowances are allocations for groups of similar loans with risk characteristics that exceed certain concentration limits established by management. Concentration risk limits have been established, among other things, for certain industry concentrations, large balance and highly leveraged credit relationships that exceed specified risk grades, and loans originated with policy exceptions that exceed specified risk grades.

The allowance for loan losses is maintained at a level considered adequate to provide for the losses that can be reasonably anticipated. Management s periodic evaluation of the adequacy of the allowance is based on the Corporation s past loan loss experience, know and inherent risks in the portfolio, adverse situations that may affect the borrower s ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to change. The Corporation uses a rolling eight quarters historic loss period for all segments when estimating the historic charge off rates calculated in accordance with ASC Topic 450 and incorporates environmental factors for various components such as economic conditions, trends in delinquencies, loan review assessments, credit concentrations and level of underperforming ratios.

All dollar amounts are reported in thousands except share and per share data.

General valuation allowances are based on general economic conditions and other qualitative risk factors both internal and external to the Corporation. In general, such valuation allowances are determined by evaluating, among other things: (i) the experience, ability and effectiveness of the bank s lending management and staff; (ii) the effectiveness of the Corporation s loan policies, procedures and internal controls; (iii) changes in asset quality; (iv) changes in loan portfolio volume; (v) the composition and concentrations of credit; (vi) the impact of competition on loan structuring and pricing; (vii) the effectiveness of the internal loan review function; (viii) the impact of environmental risks on portfolio risks; and (ix) the impact of changes to interest rates on portfolio risk. Management evaluates the degree of risk that each one of these components has on the quality of the loan portfolio on a quarterly basis. Each component is determined to have either a high, moderate or low degree of risk. The results are then input into a general allocation matrix to determine an appropriate general valuation allowance.

Included in the general valuation allowances are allocations for groups of similar loans with risk characteristics that exceed certain concentration limits established by management. Concentration risk limits have been established, among other things, for certain industry concentrations, large balance and highly leveraged credit relationships that exceed specified risk grades, and loans originated with policy exceptions that exceed specified risk grades.

Loans identified as losses by management and internal loan review are charged-off. Furthermore, consumer loan accounts are charged-off automatically based on regulatory requirements.

The following table summarizes the allocation in the allowance for loan losses by loan segment for the years ended December 31, 2013, 2012 and 2011:

December 31, 2013	Commercial	Residential Real Estate	Consumer and Other Retail	Totals
Beginning Balance	$ 7,528	$ 1,109	$ 172	$ 8,809
Less: Charge-offs	222	27	49	298
Add: Recoveries	53	2	29	84
Add: Provisions	-	-	-	-
Ending Balance	$ 7,359	$ 1,084	$ 152	$ 8,595

December 31, 2012	Commercial	Residential Real Estate	Consumer and Other Retail	Totals
Beginning Balance	$ 6,895	$ 2,113	$ 192	$ 9,200
Less: Charge-offs	1,690	176	19	1,885
Add: Recoveries	364	2	8	374
Add: Provisions	1,959	(830)	(9)	1,120

Ending Balance	$	7,528	$	1,109	$	172	$	8,809

December 31, 2011	Commercial		Residential Real Estate		Consumer and Other Retail		Totals	
Beginning Balance	$	7,011	$	2,001	$	408	$	9,420
Less: Charge-offs		3,353		52		147		3,552
Add: Recoveries		103		-		104		207
Add: Provisions		3,134		164		(173)		3,125
Ending Balance	$	6,895	$	2,113	$	192	$	9,200

The following tables detail the amount of the ALLL allocated to each portfolio segment as of December 31, 2013, 2012 and 2011, disaggregated on the basis of the Corporation s impairment methodology:

All dollar amounts are reported in thousands except share and per share data.

December 31, 2013	Commercial	Residential Real Estate	Consumer and Other Retail	Totals
Loans individually evaluated for impairment	$ 342	$ 118	$ 11	$ 471
Loans collectively evaluated for impairment	7,017	966	141	8,124
Ending Balance	$ 7,359	$ 1,084	$ 152	$ 8,595

December 31, 2012	Commercial	Residential Real Estate	Consumer and Other Retail	Totals
Loans individually evaluated for impairment	$ 221	$ 82	$ -	$ 303
Loans collectively evaluated for impairment	7,307	1,027	172	8,506
Ending Balance	$ 7,528	$ 1,109	$ 172	$ 8,809

December 31, 2011	Commercial	Residential Real Estate	Consumer and Other Retail	Totals
Loans individually evaluated for impairment	$ 1,111	$ 131	$ -	$ 1,242
Loans collectively evaluated for impairment	5,784	1,982	192	7,958
Ending Balance	$ 6,895	$ 2,113	$ 192	$ 9,200

The following table shows loans as of December 31, 2013, 2012 and 2011 related to each balance in the allowance for possible loan losses by portfolio segment and disaggregated on the basis of the Bank s impairment methodology:

December 31, 2013	Commercial	Residential Real Estate	Consumer & Other Retail	Totals
Loans individually evaluated for impairment	$ 8,227	$ 987	$ 11	$ 9,225
Loans collectively evaluated for impairment	346,148	212,776	38,617	597,541
Ending Balance	$ 354,375	$ 213,763	$ 38,628	$ 606,766

December 31, 2012	Commercial	Residential Real Estate	Consumer & Other Retail	Totals
Loans individually evaluated for impairment	$ 7,627	$ 1,015	$ -	$ 8,642
Loans collectively evaluated for impairment	328,298	195,334	34,885	558,517
Ending Balance	$ 335,925	$ 196,349	$ 34,885	$ 567,159

December 31, 2011	Commercial	Residential Real Estate	Consumer & Other Retail	Totals
Loans individually evaluated for impairment	$ 12,387	$ 1,217	$ -	$ 13,604
Loans collectively evaluated for impairment	268,536	221,365	14,297	504,198
Ending Balance	$ 280,923	$ 222,582	$ 14,297	$ 517,802

NOTE 6 PREMISES AND EQUIPMENT

The following table presents the Corporation s assets by category at December 31, 2013 and 2012:

	2013	2012
Land	$ 8,223	$ 9,003
Premises	22,765	22,717
Furniture and equipment	9,367	9,401
Leasehold improvements	1,095	1,319
	41,450	42,440
Less allowance for depreciation and amortization	(16,582)	(16,023)
	$ 24,868	$ 26,417

All dollar amounts are reported in thousands except share and per share data.

NOTE 7 RELATED PARTY TRANSACTIONS

Certain related parties (primarily directors and senior officers of the Corporation or the Bank, including their affiliates, families and companies in which they hold 10% or more ownership) were customers of, and had loans and other transactions with, the Bank in the ordinary course of business. An analysis of the activity with respect to such loans for the years ended December 31, 2013 and 2012 is shown in the table below (dollars in thousands). These totals exclude loans made in the ordinary course of business to other companies with which neither the Corporation nor the Bank had a relationship other than the association of one of its directors in the capacity of officer or director. These loan transactions were made on substantially the same terms as those prevailing at the time for comparable loans to other persons. They did not involve more than the normal risk of collectability or present other unfavorable features. No related party loans were charged off in 2013 or 2012.

Activity for related party transactions during 2013 and 2012 is as follows (dollars in thousands):

	2013	2012
Related party extensions of credit, beginning of period	$ 3,831	$ 3,829
New loans	1,116	745
Repayments	(1,125)	(743)
Related party extension of credit, end of period	$ 3,822	$ 3,831

The aggregate balances of related party deposits at December 31, 2013 and 2012 were $15,724 and $15,984, respectively.

The aggregate balances of related party repurchase agreements at December 31, 2013 and 2012 were $9,079 and $8,694, respectively.

The Corporation and Bank utilize various services and purchased good provided by certain related parties. Significant services provided by a director during 2013 totaled $38, which was for consulting services. For 2012, these services totaled $1,105, which was for building contractor services.

NOTE 8 LEASES

Real property for four of the Bank s office locations and certain equipment are leased under noncancelable operating leases expiring at various times through 2028. In most cases, the leases provide for one or more renewal options of five to ten years under the same or similar terms. In addition, various items of office equipment are leased under cancelable operating leases. Total rental expense incurred under all operating leases, including short-term leases with terms of less than one month, amounted to approximately $18, $12 and $13 for equipment leases and approximately $264, $283 and $236 for building leases in 2013, 2012 and 2011, respectively. Future minimum lease commitments as of December 31, 2013 under all noncancelable operating leases with initial terms of one year or more are shown in the following table:

Year	Lease Payments	
2014	$	336
2015		347
2016		320
2017		290
2018		290
Thereafter		3,942
Total	$	5,525

All dollar amounts are reported in thousands except share and per share data.

NOTE 9 FEDERAL AND STATE INCOME TAXES

The following table presents components of income tax expense attributable to continuing operations for the years ended December 31, 2013, 2012 and 2011:

	2013	2012	2011
Current	$ 915	$ 2,256	$ 1,960
Deferred	1,950	(340)	(1,216)
Total provision for income taxes	2,865	1,916	744

Deferred Tax Effects of Principal Temporary Differences	2013	2012	2011
Allowance for possible loan losses	$ 3,309	$ 3,392	$ 3,519
Deferred compensation	2,516	2,420	2,234
Write down of other real estate	314	1,152	1,621
Deferred gain on OREO sale	188	202	-
Amortization of core deposit intangible	(272)	423	575
Recognition of nonaccrual loan income	111	152	66
Unrealized gains (losses) on available-for-sale securities	6,613	(2,212)	(1,892)
Post retirement benefit obligation	1,849	1,733	1,643
Accelerated depreciation	(822)	(630)	(562)
Amortization of goodwill	(2,591)	(2,376)	(2,152)
Alternative Minimum Tax	-	402	422
Dividend Income - F&M West	(372)	(219)	(241)
Prepaid Expenses	(178)	(185)	-
Other	(304)	(368)	(360)
Net deferred tax asset	$ 10,905	$ 3,884	$ 4,872

Reconciliation of Total Income Taxes Reported with the Amount of Income Taxes Computed at the Federal Statutory Rate (34% Each Year)	2013	2012	2011
Tax expense at statutory rate	$ 4,332	$ 3,238	$ 2,632
Increase (decrease) in taxes resulting from:			
Tax exempt interest	(1,144)	(1,275)	(1,533)
Nondeductible interest expense	18	29	45
Employee benefits	(196)	(240)	(244)
Other nondeductible expenses (nontaxable income) - net	11	32	55
State income taxes net of federal tax benefit	-	41	(40)
Dividend income exclusion	-	(1)	(52)
Other	(156)	92	(119)

Total provision for income taxes	$ 2,865	$ 1,916	$ 745
Effective tax rate	22.4%	20.1%	9.6%

The Corporation and one of its subsidiaries file consolidated income tax returns with the Internal Revenue Service and State of Tennessee. The Corporation is not subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2010. There was no valuation allowance for deferred tax assets at December 31, 2013 and 2012. Management believes it is more-likely-than-not that all of the deferred tax assets will be realized because they were supported by recoverable taxes paid in prior years.

All dollar amounts are reported in thousands except share and per share data.

NOTE 10 BORROWED FUNDS

The Bank is a party to the Blanket Agreement for Advances and Security Agreement (the Blanket Agreement) with the Federal Home Loan Bank of Cincinnati (the FHLB). Advances made to the Bank under the Blanket Agreement are collateralized by the FHLB stock and qualifying residential mortgage loans totaling 150% of the outstanding amount borrowed. These collateralization matters are outlined in the Blanket Agreement dated June 20, 2006 between the Bank and the FHLB. Outstanding advances at December 31, 2013 and 2012 were $0 and $10,100, respectively.

Stock held in the FHLB totaling $3,009 at December 31, 2013 is carried at cost. The stock is restricted and can only be sold back to the FHLB at par.

The Bank has a Cash Management Advance Line of Credit Agreement (the CMA) dated June 21, 2010, with the Federal Home Loan Bank. The CMA is a component of the Blanket Agreement. The purpose of the CMA is to assist with short-term liquidity management. Under the terms of the CMA, the Bank may borrow a maximum of $40 million selecting a variable rate of interest for up to 90 days or a fixed rate for a maximum of 30 days. There were no borrowings outstanding under the CMA as of December 31, 2013.

Short-term borrowings included the following at December 31:

	2013	2012
Securities sold under repurchase agreements	$ 18,095	$ 17,068

Securities sold under agreements to repurchase consist of obligations of the Bank to other parties. The obligations are secured by investment securities and such collateral is held by in safekeeping by a third party. The maximum amount of outstanding agreements at any month end during 2013 and 2012 totaled $22,359 and $22,598, respectively, and the monthly average of such agreements totaled $19,052 and $18,657 for 2013 and 2012, respectively. The agreements at December 31, 2013, mature January 2, 2014.

NOTE 11 SIGNIFICANT ESTIMATES, COMMITMENTS AND CONTINGENCIES

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Estimates related to the allowance for loan losses are reflected in the footnote regarding loans. Other significant estimates and concentrations not discussed in those footnotes include:

General Litigation

The Corporation is subject to claims and lawsuits that arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the consolidated financial position, results of operations and cash flows of the Corporation.

Pension and Other Postretirement Benefit Obligations

The Corporation has a noncontributory defined benefit postretirement health care plan whereby it agrees to provide certain postretirement benefits to eligible employees. The benefit obligation is the actuarial present value of all benefits attributed to service rendered prior to the valuation date based on the projected unit credit cost method. It is reasonably possible that events could occur that would change the estimated amount of this liability materially in the near term.

All dollar amounts are reported in thousands except share and per share data.

Current Economic Conditions

The current protracted economic decline continues to present financial institutions with circumstances and challenges, which in some cases have resulted in large and unanticipated declines in the fair values of investments and other assets, constraints on liquidity and capital and significant credit quality problems, including severe volatility in the valuation of real estate and other collateral supporting loans.

The accompanying financial statements have been prepared using values and information currently available to the Corporation.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments in asset values, the allowance for loan losses and capital that could negatively impact the Corporation s ability to meet regulatory capital requirements and maintain sufficient liquidity. Furthermore, the Corporation s regulators could require material adjustments to asset values or the allowance for loan losses for regulatory capital purposes that could affect the Corporation s measurement of regulatory capital and compliance with the capital adequacy guidelines under the regulatory framework for prompt corrective action.

Commitments and Credit Risk

The Corporation grants agribusiness, commercial and residential loans to customers throughout the state. The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheet. The contract or notional amounts of those instruments reflect the extent of involvement the Bank has in those particular financial instruments.

Commitments to Originate Loans

Commitments to originate loans are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since a portion of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Each customer s creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained, if deemed necessary, is based on management s credit evaluation of the counterparty. Collateral held varies, but may include accounts receivable, inventory, property, plant and equipment, commercial real estate and residential real estate.

Mortgage loans in the process of origination represent amounts that the Corporation plans to fund within a normal period of 30 to 90 days, and which are intended for sale to investors in the secondary market. Total mortgage loans in process of origination were $407 and $9,488, at December 31, 2013 and 2012, respectively. Total mortgage loans held for sale amounted to $327 and $2,456, at December 31, 2013 and 2012, respectively.

Standby Letters of Credit

Standby letters of credit are irrevocable conditional commitments issued by the Corporation to guarantee the performance of a customer to a third party. Financial standby letters of credit are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing and similar transactions. Performance standby letters of credit are issued to guarantee performance of certain customers under nonfinancial contractual obligations. The credit risk involved in issuing standby letters of credit is essentially the same as that involved in extending loans to customers. Should the Corporation be obligated to perform under the standby letters of credit, the Corporation may seek recourse from the customer for reimbursement of amounts paid.

The Corporation had total outstanding standby letters of credit amounting to $11,384 and $9,070, at December 31, 2013 and 2012, respectively, with terms ranging from seven days to 23 years.

All dollar amounts are reported in thousands except share and per share data.

Lines of Credit

Lines of credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Lines of credit generally have fixed expiration dates. Since a portion of the line may expire without being drawn upon, the total unused lines do not necessarily represent future cash requirements. Each customer s creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained, if deemed necessary, is based on management s credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, commercial real estate and residential real estate. Management uses the same credit policies in granting lines of credit as it does for on-balance-sheet instruments.

At December 31, 2013, the Corporation had granted unused lines of credit to borrowers aggregating approximately $79,150 and $44,318 for commercial lines and open-end consumer lines, respectively. At December 31, 2012, unused lines of credit to borrowers aggregated approximately $64,455 for commercial lines and $45,302 for open-end consumer lines.

NOTE 12 REGULATORY MATTERS

The Corporation and the Bank are subject to federal regulatory risk-adjusted capital adequacy standards. Failure to meet capital adequacy requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that could have a material adverse effect on the operating results and financial condition of the Corporation and the Bank. The applicable regulations require the Bank to meet specific capital adequacy guidelines that involve quantitative measures of assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital classification is also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Corporation and the Bank to maintain minimum amounts and ratios of Total Capital and Tier I Capital to risk-weighted assets and of Tier I Capital to average assets. Actual capital amounts and ratios are presented in the table below (dollars in thousands). Management believes, as of December 31, 2013, that the Corporation and the Bank met all capital adequacy requirements to which they were subject.

(Dollars in Thousands)	Actual		For Minimum Capital Adequacy Purposes		For Minimum Regulatory Compliance Purposes	
As of December 31, 2013	Amount	Ratio	Amount	Ratio > or =	Amount	Ratio > or =
Total Capital (to Risk Weighted						
Assets) Consolidated	$ 110,276	15.3 %	$ 57,632	8.0 %	$ -	-
Bank	107,392	15.0 %	57,248	8.0 %	71,560	10.0%
Tier I Capital (to Risk Weighted						
Assets) Consolidated	101,681	14.1 %	28,816	4.0 %	-	-
Bank	98,797	13.8 %	28,624	4.0 %	42,936	6.0%
Tier I Capital (to Average						
Assets) Consolidated	101,681	9.4 %	43,358	4.0 %	-	-
Bank	98,797	9.1 %	43,358	4.0 %	54,198	5.0%
As of December 31, 2012						
Total Capital (to Risk Weighted						
Assets) Consolidated	$ 109,011	15.8 %	$ 55,265	8.0 %	$ -	-
Bank	106,075	15.5 %	54,890	8.0 %	68,613	10.0%

Tier I Capital (to Risk Weighted						
Assets) Consolidated	100,338	14.5 %	27,603	4.0 %	-	-
Bank	97,402	14.2 %	27,418	4.0 %	41,127	6.0%
Tier I Capital (to Average						
Assets) Consolidated	100,338	9.7 %	41,505	4.0 %	-	-
Bank	97,402	9.4 %	41,492	4.0 %	51,865	5.0%

All dollar amounts are reported in thousands except share and per share data.

The Corporation is subject to certain restrictions on the amount of dividends that it may declare without prior regulatory approval. At December 31, 2013, approximately $15,022 of retained earnings were available for dividend declaration without prior approval.

NOTE 13 FAIR VALUE MEASUREMENT

The fair value of an asset or liability is the price that would be received to sell that asset or paid to transfer that liability in an orderly transaction occurring in the principal market (or most advantageous market in the absence of a principal market) for such asset or liability. Fair value measurement must maximize the use of observable inputs and minimize the use of unobservable inputs. In estimating fair value, the Corporation utilizes valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Such valuation techniques are consistently applied. Inputs to valuation techniques include the assumptions that market participants would use in pricing an asset or liability. Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 820, Fair Value Measurements and Disclosures (ASC Topic 820) establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

- *Level 1 Inputs* - Unadjusted quoted prices in active markets for identical assets or liabilities.
- *Level 2 Inputs* - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, market consensus, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.
- *Level 3 Inputs* - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity s own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

Recurring Measurements

The following table summarizes financial assets measured at fair value on a recurring basis as of December 31, 2013 and 2012, and by the level within the fair value hierarchy utilized to measure fair value:

December 31, 2013

Available-For-Sale Securities	Level 1	Level 2	Level 3	Total
U.S. Government agencies	$ -	$ 105,072	$ -	$ 105,072
U.S. government sponsored agency mortgage backed securities	-	157,423	-	157,423
States and political subdivisions	-	46,337	-	46,337
Corporate bonds	-	20,882	-	20,882
Total assets at fair value	$ -	$ 329,714	$ -	$ 329,714

December 31, 2012

Available-For-Sale Securities	Level 1	Level 2	Level 3	Total
U.S. Government agencies	$ -	$ 144,017	$ -	$ 144,017
U.S. government sponsored agency mortgage backed securities	-	133,718	-	133,718
States and political subdivisions	-	50,579	-	50,579
Corporate bonds	-	17,404	-	17,404
Total assets at fair value	$ -	$ 345,718	$ -	$ 345,718

The following is a description of the valuation methodologies and inputs used for assets measured at fair value on a recurring basis and recognized in the accompanying balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended December 31, 2013.

All dollar amounts are reported in thousands except share and per share data.

Available-for-Sale Securities

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, the Corporation obtains fair value measurements from an independent pricing service, such as Interactive Data, which utilizes pricing models to determine fair value measurement. The Corporation reviews the pricing quarterly to verify the reasonableness of the pricing. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond s terms and conditions, among other factors. U.S. government agencies, state and political subdivisions, U.S. government sponsored agency mortgage-backed securities and corporate bonds are classified as Level 2 inputs.

Nonrecurring Measurements

The following table summarizes financial assets measured at fair value on a nonrecurring basis as of December 31, 2013 and December 31, 2012, by the level within the fair value hierarchy utilized to measure fair value:

Assets measured at fair value on a nonrecurring basis as of December 31, 2013				
	Level 1	Level 2	Level 3	Total
Impaired loans (collateral-dependent)	$ -	$ -	$ 2,214	$ 2,214
Other real estate owned	-	-	208	208
Assets measured at fair value on a nonrecurring basis as of December 31, 2012				
	Level 1	Level 2	Level 3	Total
Impaired loans (collateral-dependent)	$ -	$ -	$ 4,840	$ 4,840
Other real estate owned	-	-	3,385	3,385

Impaired Loans (Collateral-Dependent)

The estimated fair value of collateral-dependent impaired loans is based on the appraised fair value of the collateral, less estimated cost to sell. Collateral-dependent impaired loans are classified within Level 3 of the fair value hierarchy.

The Corporation considers the appraisal or evaluation as the starting point for determining fair value and then considers other factors and events in the environment that may affect the fair value. Appraisals of the collateral underlying collateral-dependent loans are obtained when the loan is determined to be collateral-dependent and subsequently as deemed necessary by the Chief Credit Officer. Appraisals are reviewed for accuracy and consistency by the Chief Credit Officer. Appraisers are selected from the list of approved appraisers maintained by management.

The appraised values are reduced by discounts to consider lack of marketability and estimated cost to sell if repayment or satisfaction of the loan is dependent on the sale of the collateral. These discounts and estimates are developed by the Chief Credit Officer by comparison to historical results. Fair value adjustments were approximately $79 at December 31, 2013 and $3,300 at December 31, 2012.

Loans considered impaired under ASC 310-35, Impairment of a Loan, are loans for which, based on current information and events, it is probable that the creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. Impaired loans are subject to nonrecurring fair value adjustments to reflect (1) subsequent partial write-downs that are based on the observable market price or current appraised value of the collateral or (2) the full charge-off of the loan carrying value.

Other Real Estate Owned

Other real estate owned (OREO) is initially recorded at fair value at the time of acquisition, as determined by independent appraisal or evaluation by the Corporation, less costs to sell when the real estate is acquired in settlement of loans. Quarterly evaluations of OREO are performed to determine if there has been any subsequent decline in the value of OREO properties. Estimated fair value of OREO is based on appraisals or evaluations, less costs to sell. OREO is classified within Level 3 of the fair value hierarchy. OREO assets are subject to nonrecurring fair value adjustments to reflect subsequent partial write-downs that are based on the observable market price or current appraised value of the collateral. Fair value adjustments were approximately $395 at December 31, 2013 and $1,200 at December 31, 2012.

All dollar amounts are reported in thousands except share and per share data.

Appraisals of OREO are obtained when the real estate is acquired and subsequently as deemed necessary by the Chief Credit Officer. Appraisals are required annually and reviewed for accuracy and consistency by the Chief Credit Officer. The appraised values are reduced by discounts to consider lack of marketability and estimated cost to sell. Appraisers are selected from the list of approved appraisers maintained by management.

Unobservable (Level 3) Inputs

The following table presents quantitative information about unobservable inputs used in nonrecurring Level 3 fair value measurements as of December 31, 2013 and 2012:

	Quantitative Information about Level 3 Fair Value Measurements				
December 31, 2013	Fair Value		Valuation Technique(s)	Unobservable Input	Range (Weighted Average)
Impaired loans (collateral-dependent)	$	2,214	Market comparable properties	Marketability discount	5.0% - 10.0% (7%)
Other real estate/assets owned	$	208	Market comparable properties	Marketability discount	5.0% - 10.0% (7%)

	Quantitative Information about Level 3 Fair Value Measurements				
December 31, 2012	Fair Value		Valuation Technique(s)	Unobservable Input	Range (Weighted Average)
Impaired loans (collateral-dependent)	$	4,840	Market comparable properties	Marketability discount	5.0% - 10.0% (7%)
Other real estate/assets owned	$	3,385	Market comparable properties	Marketability discount	5.0% - 10.0% (7%)

ASC Topic 825, Financial Instruments, requires disclosure of the fair value of financial assets and liabilities, including those financial assets and liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and due from banks The carrying amount approximates fair value.

Interest bearing deposits in other banks The carrying amount approximates fair value.

Federal funds sold The carrying amount approximates fair value.

Securities held-to-maturity Fair values are based on quoted market prices, if available. If a quoted price is not available, fair value is estimated using quoted prices for similar securities. The fair value estimate is provided to management from a third party using modeling assumptions specific to each type of security that are reviewed and approved by management. Quarterly sampling of fair values provided by additional third parties supplement the fair value review process.

Loans held for sale The fair value is predetermined at origination based on sale price.

All dollar amounts are reported in thousands except share and per share data.

Loans (net of the allowance for loan losses) The fair value of fixed rate loans and variable rate mortgage loans is estimated by discounting the future cash flows using current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. For other variable rate loans, the carrying amount approximates fair value.

Federal Home Loan Bank stock The carrying value of Federal Home Loan Bank (FHLB) stock approximates fair value based on the redemption provisions of the FHLB.

Federal Reserve Bank stock The carrying value of Federal Reserve Bank stock approximates fair value based on the redemption provisions of the Federal Reserve Bank.

Accrued interest receivable The carrying amount approximates fair value.

Deposits The fair value of fixed maturity time deposits is estimated by discounting the future cash flows using the rates currently offered for deposits of similar remaining maturities. For deposits including demand deposits, savings accounts, NOW accounts, and certain money market accounts, the carrying value approximates fair value.

Repurchase agreements The fair value is estimated by discounting future cash flows using current rates.

Advances from FHLB The fair value of these fixed-maturity advances is estimated by discounting future cash flows using rates currently offered for advances of similar remaining maturities.

Accrued interest payable The carrying amount approximates fair value.

Commitments to extend credit and letters of credit The fair value of commitments to originate loans is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair values of letters of credit and lines of credit are based on fees currently charged for similar agreements or on the estimated cost to terminate or otherwise settle the obligations with the counterparties at the reporting date. The fair values of these commitments are not material.

The following tables present estimated fair values of the Corporation s financial instruments as of December 31, 2013 and 2012, and indicate the levels within the fair value hierarchy of the valuation techniques:

Fair Value Measurements at December 31, 2013 Using

	Carrying Amount	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Financial assets				
Cash and due from banks	$ 20,391	$ 20,391	$ -	$ -
Interest-bearing deposits in other banks	25,167	25,167	-	-
Federal funds sold	9,850	9,850	-	-
Federal Home Loan Bank and Federal Reserve Bank stock	3,879	-	3,879	-
Securities available-for-sale	329,714	-	329,714	-
Securities held-to-maturity	27,839	-	28,595	-
Loans held for sale	327	327	-	-
Loans, net	598,171	-	-	607,113
Accrued interest receivable	4,183	-	4,183	-
Financial liabilities				
Non-interest bearing deposits	179,823	179,823	-	-
Interest bearing deposits	777,514	-	778,682	-
Repurchase agreements	18,095	-	18,095	-
Accrued interest payable	663	-	663	-
Off-balance sheet credit related instruments:				
Commitments to extend credit and letters of credit		-	-	-

All dollar amounts are reported in thousands except share and per share data.

Fair Value Measurements at December 31, 2012 Using

	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial assets				
Cash and due from banks	$ 23,443	$ 23,443	$ -	$ -
Interest-bearing deposits in other banks	31,953	31,953	-	-
Federal funds sold	15,000	15,000	-	-
Federal Home Loan Bank and Federal Reserve Bank stock	3,879	-	3,879	-
Securities available-for-sale	345,718	-	345,718	-
Securities held-to-maturity	31,755	-	33,420	-
Loans held for sale	2,456	2,456	-	-
Loans, net	558,350	-	-	572,277
Accrued interest receivable	4,060	-	4,060	-
Financial liabilities				
Non-interest bearing deposits	169,136	169,136	-	-
Interest bearing deposits	763,713	-	766,043	-
Repurchase agreements	17,068	-	17,068	-
Advances from Federal Home Loan Bank	10,100	-	10,215	-
Accrued interest payable	754	-	754	-
Off-balance sheet credit related instruments:				
Commitments to extend credit and letters of credit		-	-	-

NOTE 14 QUARTERLY RESULTS OF OPERATIONS (Unaudited)

The following table presents unaudited quarterly interim financial information for the Corporation for the years ended December 31, 2013 and 2012:

2013	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
Interest income	$ 9,223	$ 9,523	$ 9,328	$ 9,287	$ 37,361
Interest expense	834	751	679	643	2,907

Net interest income	8,389	8,772	8,649	8,644	34,454
Provision for possible loan losses, net	-	-	-	-	-
Noninterest income	3,329	2,620	2,509	2,658	11,116
Noninterest expenses	8,105	8,165	8,322	8,237	32,829
Income before income taxes	3,613	3,227	2,836	3,065	12,741
Income taxes	557	842	779	687	2,865
Net income	$ 3,056	$ 2,385	$ 2,057	$ 2,378	$ 9,876
Basic earnings per share	0.59	0.46	0.40	0.47	1.93
Weighted average shares outstanding per quarter	5,178,759	5,133,051	5,086,469	5,046,833	5,110,849

2012	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
Interest income	$ 9,065	$ 9,095	$ 9,114	$ 9,110	$ 36,384
Interest expense	1,071	979	917	874	3,841
Net interest income	7,994	8,116	8,197	8,236	32,543
Provision for possible loan losses, net	600	520	-	-	1,120
Noninterest income	3,379	3,360	2,276	2,616	11,631
Noninterest expenses	7,754	8,424	8,145	9,207	33,530
Income before income taxes	3,019	2,532	2,328	1,645	9,524
Income taxes	690	451	373	402	1,916
Net income	$ 2,329	$ 2,081	$ 1,955	$ 1,243	$ 7,608
Basic earnings per share	0.44	0.39	0.37	0.23	1.43
Weighted average shares outstanding per quarter	5,330,000	5,330,000	5,328,002	5,332,893	5,315,634

All dollar amounts are reported in thousands except share and per share data.

NOTE 15 DEPOSITS

The Bank does not have any foreign offices and all deposits are serviced in its 16 domestic offices. Maturities of time deposits of $100 or more at December 31, 2013 and 2012 are as follows:

	2013	2012
Under 3 months	$ 31,514	$ 28,504
3 to 12 months	$ 63,429	64,639
Over 12 months	$ 27,834	27,018
Total	$ 122,777	$ 120,161

The following table presents maturities of interest-bearing time deposits as of December 31, 2013:

2014	$ 185,687
2015	$ 25,422
2016	$ 14,712
2017	$ 7,120
2018	$ 5,893
Thereafter	$ -
Total	$ 238,834

NOTE 16 CONDENSED FINANCIAL INFORMATION OF THE CORPORATION

The following tables present the condensed balance sheets, statements of income, comprehensive income, and cash flows of the Corporation as of December 31, 2013 and 2012:

CONDENSED BALANCE SHEETS

	As of December 31,	
	2013	2012
Cash	$ 23	$ 61
Investment in bank subsidiary	99,695	111,655
Investment in credit life insurance company	54	54

Investment in other securities	17	17
Dividends receivable from bank subsidiary	2,058	1,917
Cash surrender value - life insurance	4,409	4,395
Total assets	$ 106,256	$ 118,099
Liabilities		
Accrued liabilities	$ 1,820	$ 1,686
Dividends payable	1,858	1,917
Total liabilities	3,678	3,603
Shareholders' equity		
Common stock - $10 par value, 8,000,000 shares authorized; 5,021,012 and 5,180,000 shares issued and outstanding, as of December 31, 2013 and December 31, 2012, respectively	50,210	51,800
Retained earnings	61,369	57,366
Accumulated other comprehensive income (loss)	(9,001)	5,330
Total shareholders' equity	102,578	114,496
Total liabilities and shareholders' equity	$ 106,256	$ 118,099

All dollar amounts are reported in thousands except share and per share data.

CONDENSED STATEMENTS OF INCOME

	Years ended December 31,		
	2013	2012	2011
Operating income			
Dividends from bank subsidiary	$ 7,663	$ 7,289	$ 6,974
Other dividend income	15	18	15
Other	65	135	130
Operating expenses	(238)	(218)	(199)
Income before equity in undistributed net income of bank subsidiary	7,505	7,224	6,920
Equity in undistributed net income of bank subsidiary	2,371	384	76
Net Income	$ 9,876	$ 7,608	$ 6,996

CONDENSED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

	Year Ended December 31,		
	2013	2012	2011
Net Income for common shareholders	$ 9,876	$ 7,608	$ 6,996
Other Comprehensive Income (Loss)			
Unrealized appreciation (depreciation) on available-for-sale securities, net of tax expense (benefit) of ($8,507), $1,204, and $2,960	(13,589)	1,923	4,728
Reclassification adjustment for realized gains included in net income, net of taxes of ($319), ($883), and ($561), respectively	(510)	(1,411)	(897)
Change in unfunded portion of postretirement benefit obligations, net of tax of ($146), $1,008 and $1,214, respectively	(232)	1,610	1,940
Other Comprehensive Income (Loss)	(14,331)	2,122	5,771
Total Comprehensive Income (Loss)	$ (4,455)	$ 9,730	$ 12,767

All dollar amounts are reported in thousands except share and per share data.

CONDENSED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2013	2012	2011
Operating activities			
Net income for the year	$ 9,876	$ 7,608	$ 6,996
Adjustments to reconcile net income to net cash provided by operating activities			
Equity in undistributed net income of bank subsidiary	(2,371)	(384)	(76)
Increase in cash surrender value of life insurance contracts	(65)	(135)	(130)
(Increase) decrease in other assets	(90)	56	(1,972)
Decrease in payables	84	127	126
Total adjustments	(2,442)	(336)	(2,052)
Net cash provided by operating activities	7,434	7,272	4,944
Investing activities			
Purchase of single premium life insurance policy	-	(310)	-
Net cash used by investing activities	-	(310)	-
Financing activities			
Payment to repurchase common stock	(3,722)	(3,400)	(3,011)
Cash dividends paid	(3,800)	(3,944)	(1,991)
Advance from subsidiary	50	-	-
Net cash used by financing activities	(7,472)	(7,344)	(5,002)
Decrease in cash	(38)	(382)	(58)
Cash at beginning of year	61	443	501
Cash at end of year	$ 23	$ 61	$ 443

NOTE 17 EMPLOYEE BENEFIT PLANS

The Bank contributes to a qualified profit-sharing plan covering employees who meet participation requirements. To be eligible to participate, employees must complete 1,000 hours of service within the twelve month time period following their date of hire. Employees must be age twenty or older. The amount of the contribution is at the discretion of the Bank s Board of Directors, up to the maximum deduction allowed for federal income tax purposes. Contributions to the plan, which amounted to approximately $1,596, $1,019 and $874 in 2013, 2012 and 2011, respectively, are included in salaries and employee benefits expense.

The Bank formalized a nonqualified salary continuation plan for certain key officers. In connection with this plan, the value of the single premium universal life insurance policies (approximately $975 at December 31, 2013 and approximately $963 at December 31, 2012) purchased in 1993 to fund the plan and the related liability (approximately $49 at December 31, 2013 and $59 at December 31, 2012) were included in other assets and other liabilities, respectively. The principal cost of the plan is accrued over the anticipated remaining period of active employment, based on the present value of the expected retirement benefit.

The Corporation and Bank implemented a deferred compensation plan that permits directors to defer their director s fees and earn interest on the deferred amount in the amount of the wall street journal prime rate plus three percent. The agreements provide for a lump sum payment or 120 month payments of deferred fees plus accrued interest after retirement, separation from service, or death. The liability accrued for this plan totaled $6,487 and $6,226 at December 30, 2013 and 2012, respectively. The charge to expense for the agreements was $722, $853 and $711 for the years ended December 31 2013, 2012 and 2011, respectively.

All dollar amounts are reported in thousands except share and per share data.

NOTE 18 POST RETIREMENT BENEFIT PLAN

Effective July 1, 2013, the Corporation revised its retiree medical benefit plan for employees who were hired before March 27, 2007. Newly retiring employees will no longer be offered medical, dental or life insurance coverage. Instead, qualified retirees will receive a post retirement bonus. The Corporation will pay a post retirement bonus equal to $20,000 to employees (i) who were hired prior to March 20, 2007; (ii) who retire on or after July 1, 2013; (iii) who are at least age 59 ½ at the time of retirement; and (iv) who have at least twenty-five years of service to the Corporation as of retirement. The bonus will be paid in a lump sum cash payment (subject to applicable tax withholding requirements) within 60 days after the employee s retirement, provided such retirement constitutes a separation from service under section 409A of the Internal Revenue Code. The Corporation still sponsors a defined benefit post-retirement health care plan for retirees who retired prior to July 1, 2007. Under this plan, premiums paid by retirees and spouses depend on date of retirement, age and coverage election.

The Corporation funding policy is to make the minimal annual contribution that is required by applicable regulations, plus such amounts as the Corporation may determine to be appropriate from time to time. The Corporation expects to contribute $145 to the plan in 2014.

The following table provides further information about the plan:

	Post-Retirement Benefits	
	2013	2012
Change in benefit obligation		
Benefit obligation at beginning of year	$ 7,421	$ 4,572
Service cost	138	91
Interest cost	292	351
Plan participants contribution	77	(81)
Expected benefits paid	(343)	(128)
Actuarial (gain) loss	(5,220)	2,616
Amendments	(52)	-
Benefit obligation at end of year	$ 2,313	$ 7,421
Change in fair value of assets		
Fair value of plans assets at beginning of year	$ -	$ -
Employer contribution	77	(209)
Plan participants' contributions	266	(105)
Benefits paid	(343)	(314)
Fair value of plan assets at end of year	$ -	$ -
Reconciliation of funded status to benefit costs recognized		
Projected benefit obligation, end of year	$ (2,313)	$ (7,421)
Fair value of assets, end of year	-	-
Funded status, end of year	(2,313)	(7,421)
Unrecognized prior service cost	(52)	-

Unrecognized net loss/(gain)	(2,490)	2,920
Prepaid/(accrued) benefit cost	(4,855)	(4,501)

Amounts recognized in accumulated other comprehensive income not yet recognized as components of net periodic benefit cost consist of:

	2013	2012
Unrecognized net actuarial gain/loss	$ 2,490	$ 2,920
Unrecognized prior service cost	52	-
	$ 2,542	$ 2,920

Amounts recognized in statement of financial position are as follows:

	2013	2012
Current Liability	$ 183	$ 266
Noncurrent liability	4,672	4,235
Total	$ 4,855	$ 4,501

All dollar amounts are reported in thousands except share and per share data.

A reconciliation of other comprehensive income is as follows:

	Post-Retirement Benefits		
	2013	2012	2011
Accumulated other comprehensive income beginning of year	$ 2,920	$ 305	$ (2,849)
Less: loss/(gain) recognized in current year	(190)	-	205
Plus: loss/(gain) incurred in current year	(136)	2,615	-
Plus: prior service cost established in current year	(52)	-	-
Other comprehensive income/(loss)	(378)	2,615	2,950
Ending balance (before tax effects)	$ 2,542	$ 2,920	$ 305

	Post-Retirement Benefits		
Components of net periodic benefit cost:	2013	2012	2011
Service cost	$ 138	$ 91	$ 24
Interest cost	292	351	139
Recognized net actuarial (gain) loss	190	-	(205)
Net periodic benefit cost (income)	$ 620	$ 442	$ (42)

The estimated net gain for the defined benefits postretirement plan that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year is $188.

	Post-Retirement Benefits	
Weighted-average assumption used to determine benefit obligation:	2013	2012
Discount rate	5%	4%
Rate of compensation increase	NA	NA

	Post-Retirement Benefits	
Weighted-average assumptions used to determine benefit costs:	2013	2012
Discount rate	4%	8%

The following table gives the Health Care Cost Trend, which is applied to gross charges, net claims and retiree paid premiums to reflect the Corporation s past practice and stated ongoing intention to maintain relatively constant cost sharing between the Corporation and retirees:

Health care trend rate	2013	2012
Initial		
Pre-65	11%	11%
Post-65	7.50%	8%
Ultimate (pre and post-65	5.00%	5%
Years to ultimate		
Pre-65	6	6
Post-65	5	6

All dollar amounts are reported in thousands except share and per share data.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid, net of participant contributions:

FYE	Company Benefits
2014	$ 183
2015	167
2016	178
2017	169
2018	191
2019-2025	935
	$ 1,823

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

	1-Percentage-Point Increase	1-Percentage-Point Decrease
Effect on total of service and interest cost	$ 29	$ (16)
Effect on postretirement benefit obligation	212	(109)

All dollar amounts are reported in thousands except share and per share data.

PART IV

Item 15. Exhibits and Financial Statement Schedules.

(a) Index to Consolidated Financial Statements, Financial Statement Schedules and Exhibits:

(1) ***Consolidated Financial Statements***: See Item 8 under Part II, Financial Statements and Supplementary Data.

(2) ***Consolidated Financial Statement Schedules***: All schedules are omitted because they are not applicable or not required, or because the required information is included in the consolidated financial statements or notes in this report.

(3) ***Exhibits:***

3.1 Charter. (1)

3.2 Articles of Amendment to Charter. (1)

3.3 Second Amended and Restated Bylaws, as amended. (2)

4 Specimen Stock Certificate. (1)

10.1 Profit Sharing Plan. (3)*

10.2 First Amendment to Profit Sharing Plan. (3)*

10.3 Second Amendment to Profit Sharing Plan. (3)*

10.4 Executive Salary Continuation Agreement by and between First Farmers and Merchants National Bank and Waymon L. Hickman, dated as of December 1, 1992. (3)*

10.5 Benefits Agreement by and between First Farmers and Merchants Bank and Thomas Randall Stevens, the Bank s and the Corporation s Chairman and Chief Executive Officer, dated as of January 26, 2007. (4)*

10.6 Benefits Agreement by and between John P. Tomlinson, III, the Bank s and Corporation s Chief Administrative Officer, dated as of January 29, 2007. (4)*

10.7 Form of First Farmers and Merchants Corporation Amended and Restated Director Deferred Compensation Agreement.(5)*

10.8 First Amendment to the First Farmers and Merchants Corporation Amended and Restated Director Deferred Compensation Agreement with John P. Tomlinson, III, dated as of December 18, 2007. (5)*

10.9 Form of First Farmers and Merchants Bank Amended and Restated Director Deferred Compensation Agreement. (5)*

10.10 First Amendment to the First Farmers and Merchants Bank Director Deferred Compensation Agreement with Thomas Randall Stevens, dated as of January 5, 2007. (5)*

10.11 First Amendment to the First Farmers and Merchants Bank Amended and Restated Director Deferred Compensation Agreement with John P. Tomlinson, III, dated as of December 18, 2007. (5)*

10.12 Form of First Farmers and Merchants National Bank Director Split Dollar Agreement. (5)*

10.13 Form of Amendment to the First Farmers and Merchants National Bank Director Split Dollar Agreement. (5)*

10.14 First Farmers & Merchants Bank Group Term Carve-Out Plan, dated as of March 27, 2007. (5)*

10.15 First Farmers and Merchants National Bank Group Term Carve-Out Plan, dated as of July 23, 2002. (5)*

10.16 Amendment to the First Farmers and Merchants National Bank Group Term Carve-Out Plan, dated as of July 23, 2002. (5)*

10.17 First Farmers & Merchants Bank Life Insurance Endorsement Method Split Dollar Plan Agreement, dated as of January 7, 2008. (5)*

10.18 Form of First Farmers and Merchants Corporation Director Deferred Compensation Agreement. (5)*

10.19 Form of First Farmers and Merchants Bank Director Deferred Compensation Agreement. (5)*

10.20 First Farmers and Merchants Bank Director Deferred Compensation Agreement with Tim E. Pettus, dated as of March 5, 2008. (5)*

10.21 First Farmers and Merchants Corporation Director Deferred Compensation Agreement with Tim E. Pettus, dated as of March 5, 2008. (5)*

13 Selected sections from Annual Report to Shareholders. (6)

21 List of Subsidiaries. (6)

31.1 Certification of the Chief Executive Officer of First Farmers and Merchants Corporation pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of the Treasurer (principal financial officer) of First Farmers and Merchants Corporation pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32 Certification of the Chief Executive Officer and Treasurer (principal financial officer) of First Farmers

and Merchants Corporation pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101 Pursuant to Rule 405 of Regulation S-T, the following financial information from the Company s Annual Report on Form 10-K for the year ended December 31, 2013, is formatted in XBRL (Extensible Business Reporting Language) interactive data files: (i) the Consolidated Balance Sheets as of December 31, 2013 and 2012; (ii) the Consolidated Statements of Income for each of the years ended December 31, 2013, 2012 and 2011; (iii) the Consolidated Statements of Changes in Shareholders Equity for each of the years ended December 31, 2013, 2012 and 2011; (iv) the Consolidated Statements of Cash Flows for each of the years ended December 31, 2013, 2012 and 2011; and (v) the Notes to Consolidated Financial Statements, tagged as blocks of text. (6)

* Indicates a compensatory plan or arrangement.

(1) Incorporated by reference to the First Farmers and Merchants Corporation Amendment No. 1 to the Annual Report on Form 10-K/A for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on May 7, 2004 (File Number 000-10972).

(2) Incorporated by reference to the First Farmers and Merchants Corporation Annual Report on Form 10-K for the year ended December 31, 2011, as filed with the Securities and Exchange Commission on March 13, 2011 (File Number 000-10972).

(3) Incorporated by reference to the First Farmers and Merchants Corporation Amendment No. 2 to the Annual Report on Form 10-K/A for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on July 19, 2004 (File Number 000-10972).

(4) Incorporated by reference to the First Farmers and Merchants Corporation Current Report on Form 8-K, as filed with the Securities and Exchange Commission on January 30, 2007 (File Number 000-10972).

(5) Incorporated by reference to the First Farmers and Merchants Corporation Annual Report on Form 10-K for the year ended December 31, 2008, as filed with the Securities and Exchange Commission on March 13, 2009 (File Number 000-10972).

(6) Included in the Original Filing under the captions Comparative Performance and Management s Discussion and Analysis of Financial Condition and Results of Operations.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

FIRST FARMERS AND MERCHANTS CORPORATION

By: /s/ T. Randy Stevens
T. Randy Stevens
Chief Executive Officer
Date: September 9, 2014

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EXHIBIT INDEX

FIRST FARMERS AND MERCHANTS CORPORATION

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10.4	Executive Salary Continuation Agreement by and between First Farmers and Merchants National Bank and Waymon L. Hickman, dated as of December 1, 1992. (3)*
10.5	Benefits Agreement by and between First Farmers and Merchants Bank and Thomas Randall Stevens, the Bank s and the Corporation s Chairman and Chief Executive Officer, dated as of January 26, 2007. (4)*
10.6	Benefits Agreement by and between John P. Tomlinson, III, the Bank s and Corporation s Chief Administrative Officer, dated as of January 29, 2007. (4)*
10.7	Form of First Farmers and Merchants Corporation Amended and Restated Director Deferred Compensation Agreement.(5)*
10.8	First Amendment to the First Farmers and Merchants Corporation Amended and Restated Director Deferred Compensation Agreement with John P. Tomlinson, III, dated as of December 18, 2007. (5)*
10.9	Form of First Farmers and Merchants Bank Amended and Restated Director Deferred Compensation Agreement. (5)*

10.10 First Amendment to the First Farmers and Merchants Bank Director Deferred Compensation Agreement with Thomas Randall Stevens, dated as of January 5, 2007. (5)*

10.11 First Amendment to the First Farmers and Merchants Bank Amended and Restated Director Deferred Compensation Agreement with John P. Tomlinson, III, dated as of December 18, 2007. (5)*

10.12 Form of First Farmers and Merchants National Bank Director Split Dollar Agreement. (5)*

10.13 Form of Amendment to the First Farmers and Merchants National Bank Director Split Dollar Agreement. (5)*

10.14 First Farmers & Merchants Bank Group Term Carve-Out Plan, dated as of March 27, 2007. (5)*

10.15 First Farmers and Merchants National Bank Group Term Carve-Out Plan, dated as of July 23, 2002. (5)*

10.16 Amendment to the First Farmers and Merchants National Bank Group Term Carve-Out Plan, dated as of July 23, 2002. (5)*

10.17 First Farmers & Merchants Bank Life Insurance Endorsement Method Split Dollar Plan Agreement, dated as of January 7, 2008. (5)*

10.18 Form of First Farmers and Merchants Corporation Director Deferred Compensation Agreement. (5)*

10.19 Form of First Farmers and Merchants Bank Director Deferred Compensation Agreement. (5)*

10.20 First Farmers and Merchants Bank Director Deferred Compensation Agreement with Tim E. Pettus, dated as of March 5, 2008. (5)*

10.21 First Farmers and Merchants Corporation Director Deferred Compensation Agreement with Tim E. Pettus, dated as of March 5, 2008. (5)*

13 Selected sections from Annual Report to Shareholders. (6)

21 List of Subsidiaries. (6)

31.1 Certification of the Chief Executive Officer of First Farmers and Merchants Corporation pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of the Treasurer (principal financial officer) of First Farmers and Merchants Corporation pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32 Certification of the Chief Executive Officer and Treasurer (principal financial officer) of First Farmers and Merchants Corporation pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101 Pursuant to Rule 405 of Regulation S-T, the following financial information from the Company s Annual Report on Form 10-K for the year ended December 31, 2013, is formatted in XBRL (Extensible Business Reporting Language) interactive data files: (i) the Consolidated Balance Sheets as of December 31, 2013 and 2012; (ii) the Consolidated Statements of Income for each of the years ended December 31, 2013, 2012 and 2011; (iii) the Consolidated Statements of Changes in Shareholders Equity for each of the years ended December 31, 2013, 2012 and 2011; (iv) the Consolidated Statements of Cash Flows for each of the years ended December 31, 2013, 2012 and 2011; and (v) the Notes to Consolidated

Financial Statements, tagged as blocks of text. (6)

* Indicates a compensatory plan or arrangement.

* Indicates a compensatory plan or arrangement.

(1) Incorporated by reference to the First Farmers and Merchants Corporation Amendment No. 1 to the Annual Report on Form 10-K/A for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on May 7, 2004 (File Number 000-10972).

(2) Incorporated by reference to the First Farmers and Merchants Corporation Annual Report on Form 10-K for the year ended December 31, 2011, as filed with the Securities and Exchange Commission on March 13, 2011 (File Number 000-10972).

(3) Incorporated by reference to the First Farmers and Merchants Corporation Amendment No. 2 to the Annual Report on Form 10-K/A for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on July 19, 2004 (File Number 000-10972).

(4) Incorporated by reference to the First Farmers and Merchants Corporation Current Report on Form 8-K, as filed with the Securities and Exchange Commission on January 30, 2007 (File Number 000-10972).

(5) Incorporated by reference to the First Farmers and Merchants Corporation Annual Report on Form 10-K for the year ended December 31, 2008, as filed with the Securities and Exchange Commission on March 13, 2009 (File Number 000-10972).

(6) Included in the Original Filing under the captions Comparative Performance and Management s Discussion and Analysis of Financial Condition and Results of Operations.

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