

Annual Disclosure Statement

The attached annual report serves as Bank of Tennessee's 2010 Annual Disclosure Statement as required by the Federal Deposit Insurance Corporation ("FDIC"). The Annual Report has not been reviewed, or confirmed for accuracy or relevance, by the FDIC.

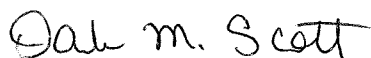
Please contact either Roy L. Harmon, Jr. (President & CEO) or Darla M. Scott (EVP & CFO) for any additional information.

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Bank of Tennessee
EVP and CFO



BancTenn Corporation
2010 ANNUAL REPORT

BANCTENN CORP. AND SUBSIDIARY
CONSOLIDATED FINANCIAL REPORT
DECEMBER 31, 2010

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Report of Independent Certified Public Accountants
on the Financial Statements

To the Stockholders and
Board of Directors
BancTenn Corp.
Kingsport, Tennessee

We have audited the accompanying consolidated balance sheets of BancTenn Corp. and subsidiary as of December 31, 2010 and 2009, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of BancTenn Corp. and subsidiary as of December 31, 2010 and 2009, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Hazlett, Lewis & Bieter, PLLC

Chattanooga, Tennessee
April 5, 2011

BANCTENN CORP. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

December 31, 2010 and 2009

	2010	2009
ASSETS		
Cash and due from banks:		
Noninterest-bearing	\$ 8,737,143	\$ 10,206,623
Interest-bearing	<u>21,526,431</u>	<u>5,277</u>
Total cash and due from banks	30,263,574	10,211,900
Certificates of deposit with other financial institutions	248,000	248,000
Securities available for sale	76,307,741	93,964,861
Investment in Paragon Commercial Corporation	10,438,500	13,111,058
Investment in Appalachian Fund for Growth II	3,227,705	3,149,074
Restricted investments, at cost	2,426,700	2,426,700
Federal funds sold	340,000	1,135,000
Loans, net of allowance for loan losses	464,155,234	472,488,022
Premises and equipment	28,107,304	28,088,600
Accrued interest receivable	1,738,617	2,058,644
Cash surrender value of life insurance	14,070,635	13,508,606
Foreclosed real estate	7,273,649	5,414,511
Other assets	<u>6,438,957</u>	<u>6,665,702</u>
Total assets	<u>\$ 645,036,616</u>	<u>\$ 652,470,678</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Noninterest-bearing	\$ 124,452,704	\$ 93,793,923
Interest-bearing	<u>397,055,033</u>	<u>376,384,044</u>
Total deposits	521,507,737	470,177,967
Securities sold under agreements to repurchase	16,090,232	53,987,082
Federal funds purchased	1,535,658	1,780,885
Federal Home Loan Bank advances	35,817,782	41,286,380
Other borrowings	-	10,000,000
Subordinated debentures	15,465,000	15,465,000
Borrowings under line of credit	160,000	-
Accrued interest payable	319,474	511,100
Accrued expenses and other liabilities	<u>4,615,242</u>	<u>4,217,338</u>
Total liabilities	<u>595,511,125</u>	<u>597,425,752</u>
Stockholders' equity:		
Common stock, \$8 par value, 6,000,000 shares authorized, 1,582,400 shares outstanding in 2010; 1,573,447 shares outstanding in 2009	12,659,200	12,587,576
Additional paid-in capital	11,871,981	11,832,109
Retained earnings	26,587,655	28,565,045
Accumulated other comprehensive income	(942,356)	2,874,381
Unallocated ESOP shares	<u>(650,989)</u>	<u>(814,185)</u>
Total stockholders' equity	<u>49,525,491</u>	<u>55,044,926</u>
Total liabilities and stockholders' equity	<u>\$ 645,036,616</u>	<u>\$ 652,470,678</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

BANCTENN CORP. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
Years Ended December 31, 2010 and 2009

	2010	2009
INTEREST INCOME		
Loans, including fees	\$ 25,903,618	\$ 27,383,813
Securities	3,275,384	5,041,747
Federal funds sold	17,891	14,401
	29,196,893	32,439,961
INTEREST EXPENSE		
	7,443,160	9,467,273
Net interest income	21,753,733	22,972,688
Provision for loan losses	5,136,337	4,668,000
Net interest income after provision for loan losses	16,617,396	18,304,688
NONINTEREST INCOME		
Customer service fees	1,784,205	2,273,367
Service revenue	3,460,503	4,392,185
Other	3,031,299	2,334,339
	8,276,007	8,999,891
NONINTEREST EXPENSES		
Salaries and employee benefits	11,436,425	12,056,564
Occupancy expenses	1,425,206	1,503,316
Other operating expenses	7,946,099	8,061,692
Loss on other assets	3,504,352	3,186,799
	24,312,082	24,808,371
Income before income taxes	581,321	2,496,208
Income taxes	66,648	94,673
Net income	\$ 514,673	\$ 2,401,535

The Notes to Consolidated Financial Statements are an integral part of these statements.

BANCTENN CORP. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
Years Ended December 31, 2010 and 2009

	<u>Comprehensive Income</u>	<u>Total Stockholders' Equity</u>	<u>Common Stock</u>	<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income</u>	<u>Unallocated ESOP Shares</u>
BALANCE, December 31, 2008		\$ 54,453,205	\$ 12,529,912	\$ 11,825,358	\$ 29,871,923	\$ 1,203,393	\$ (977,381)
Comprehensive income:							
Net income	\$ 2,401,535	2,401,535	-	-	2,401,535	-	-
Other comprehensive income, net of tax:							
Unrealized holding gains (losses) on securities available for sale, net of reclassification adjustment	730,190	730,190	-	-	-	730,190	-
Unrealized holding gains (losses) on interest rate swaps, net of reclassification adjustment	<u>940,798</u>	940,798	-	-	-	940,798	-
Total comprehensive income (loss)	<u>\$ 4,072,523</u>						
Purchase of 8,972 common shares		(414,886)	(71,776)	(343,110)	-	-	-
Employee stock ownership plan:							
Shares released to participants		202,050	-	38,854	-	-	163,196
Distributions to unallocated shares		59,751	-	-	59,751	-	-
Distributions to stockholders		(3,768,164)	-	-	(3,768,164)	-	-
Issuance of 16,180 common shares pursuant to stock option plan		435,725	129,440	306,285	-	-	-
Stock compensation expense, net of tax benefits		<u>4,722</u>	<u>-</u>	<u>4,722</u>	<u>-</u>	<u>-</u>	<u>-</u>
BALANCE, December 31, 2009		55,044,926	12,587,576	11,832,109	28,565,045	2,874,381	(814,185)
Comprehensive income:							
Net income	\$ 514,673	514,673	-	-	514,673	-	-
Other comprehensive income, net of tax:							
Unrealized holding gains (losses) on securities available for sale, net of reclassification adjustment	(3,111,879)	(3,111,879)	-	-	-	(3,111,879)	-
Unrealized holding gains (losses) on interest rate swaps, net of reclassification adjustment	<u>(704,858)</u>	(704,858)	-	-	-	(704,858)	-
Total comprehensive income (loss)	<u>\$ (3,302,064)</u>						
Purchase of 12,185 common shares		(464,858)	(97,480)	(367,378)	-	-	-
Employee stock ownership plan:							
Shares released to participants		166,526	-	3,330	-	-	163,196
Distributions to unallocated shares		32,919	-	-	32,919	-	-
Distributions to stockholders		(2,524,982)	-	-	(2,524,982)	-	-
Issuance of 21,138 common shares pursuant to stock option plan		568,257	169,104	399,153	-	-	-
Stock compensation expense, net of tax benefits		<u>4,767</u>	<u>-</u>	<u>4,767</u>	<u>-</u>	<u>-</u>	<u>-</u>
BALANCE, December 31, 2010		<u>\$ 49,525,491</u>	<u>\$ 12,659,200</u>	<u>\$ 11,871,981</u>	<u>\$ 26,587,655</u>	<u>\$ (942,356)</u>	<u>\$ (650,989)</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

BANCTENN CORP. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2010 and 2009

	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 514,673	\$ 2,401,535
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	1,730,708	1,797,530
Provision for loan losses	5,136,337	4,668,000
Deferred income taxes	(120,852)	(336,627)
Stock compensation expense	4,767	4,722
Net amortization on securities	166,858	2,815
Undistributed earnings of equity investments	(78,631)	(71,364)
Writedown of investment in Paragon Commercial Corporation	2,672,558	2,353,793
Other (gains) losses, net	(1,018,914)	1,445,622
Change in operating assets and liabilities:		
Accrued interest receivable	320,027	138,047
Accrued interest payable	(191,626)	(299,098)
Other assets and liabilities	(873,470)	(2,137,136)
Net cash provided by operating activities	<u>8,262,435</u>	<u>9,967,839</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales, maturities, prepayments and calls of securities available for sale	96,298,097	44,210,740
Purchase of securities available for sale	(79,612,496)	(14,722,470)
Purchase of equity investments	(223,700)	(133,750)
Purchase of restricted investments	-	(352,400)
Purchase of investment in Paragon Commercial Corporation	-	(465,000)
Purchase of certificates of deposit with other financial institutions	-	(248,000)
Decrease (increase) in federal funds sold	795,000	(865,000)
Proceeds from sale of foreclosed real estate	3,809,369	3,263,253
Proceeds from sale of repossessions	318,025	535,578
Loan originations and principal collections, net	(3,502,901)	12,278,199
Purchase of premises and equipment	(1,749,412)	(740,046)
Proceeds from sale of premises and equipment	300	13,323
Net cash provided by investing activities	<u>16,132,282</u>	<u>42,774,427</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in demand deposits and NOW, money market, and savings accounts	63,402,197	41,712,751
Net decrease in time deposits	(12,072,427)	(70,900,750)
Net decrease in federal funds purchased and securities sold under agreements to repurchase	(38,142,077)	(22,415,592)
Net decrease in Federal Home Loan Bank advances	(5,468,598)	(12,057,061)
Net increase (decrease) in other borrowings	(10,000,000)	10,000,000
Net increase in borrowings under line of credit	160,000	-
Issuance of common stock	568,257	435,725
Purchase of common stock	(464,858)	(414,886)
Net ESOP transactions	199,445	261,801
Distributions to stockholders	(2,524,982)	(3,768,164)
Net cash used in financing activities	<u>(4,343,043)</u>	<u>(57,146,176)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	20,051,674	(4,403,910)
CASH AND CASH EQUIVALENTS, beginning of year	<u>10,211,900</u>	<u>14,615,810</u>
CASH AND CASH EQUIVALENTS, end of year	<u>\$ 30,263,574</u>	<u>\$ 10,211,900</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid during the year for interest	\$ 7,634,786	\$ 9,766,371
Cash paid during the year for income taxes	<u>569,655</u>	<u>395,608</u>
NONCASH INVESTING ACTIVITIES		
Real estate acquired in settlement of loans	<u>\$ 6,047,347</u>	<u>\$ 6,682,810</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1. Summary of Significant Accounting Policies

The accounting and reporting policies of BancTenn Corp. (the Company) conform with United States generally accepted accounting principles (GAAP) and practices within the banking industry. The Financial Accounting Standards Board (FASB) has adopted the FASB Accounting Standards Codification (ASC) as the single source of authoritative nongovernmental GAAP.

The policies that materially affect financial position and results of operations are summarized as follows:

Nature of operations:

BancTenn Corp. is a bank holding company whose principal activity is the ownership and management of its wholly owned subsidiary, Bank of Tennessee (the Bank). The Bank generates commercial, mortgage and consumer loans and receives deposits from customers located primarily in the Tri-Cities area of upper east Tennessee. The Bank's primary deposit products are transaction and savings accounts and certificates of deposit. Its primary lending products are commercial loans, residential real estate loans, and consumer loans. The Bank also provides data processing and other operating services to other financial institutions. Other operating services include deposit operations, item processing, and human resources.

Basis of consolidation:

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Bank of Tennessee. All material intercompany balances and transactions have been eliminated in consolidation.

Use of estimates:

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

The determination of the adequacy of the allowance for loan losses is based on estimates that are particularly susceptible to significant changes in the economic environment and market conditions. In connection with the determination of the estimated losses on loans, management obtains independent appraisals for significant collateral.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1. Summary of Significant Accounting Policies (continued)

Significant group concentrations of credit risk:

Most of the Company's activities are with customers located in eastern Tennessee. The types of securities that the Company invests in are included in Note 3. The types of lending the Company engages in are included in Note 5. The Company does not have any significant concentrations to any one industry or customer.

Commercial real estate, including commercial construction loans, represented 41 percent of the loan portfolio at December 31, 2010, and 40 percent of the loan portfolio at December 31, 2009.

Securities available for sale:

Securities available for sale are carried at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income. Realized gains and losses on securities available for sale are included in other income and, when applicable, are reported as a reclassification adjustment, net of tax, in other comprehensive income.

Gains and losses on sales of securities are determined on the specific-identification method. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities.

The Company conducts a regular assessment of its securities portfolio to determine whether any are other-than-temporarily impaired. In estimating other-than-temporary impairment losses, management considers, among other factors, the length of time and extent to which the fair value has been less than cost, the financial condition and near term prospects of the issuer, and the intent and ability of the Company to retain its investment for a period of time sufficient to allow for any anticipated recovery. The term "other-than-temporary" is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value for a debt security is determined to be other-than-temporary, the other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income. For equity securities, the full amount of the other-than-temporary impairment is recorded in non-interest income as an impairment loss on investment securities.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1. Summary of Significant Accounting Policies (continued)

Equity investment:

The Company is accounting for its investment in Appalachian Fund for Growth II, a 25% owned affiliate, by the equity method of accounting. The Company's share of the net income of the affiliate is recognized as income in the Company's income statement and added to the investment account. Dividends received are treated as a reduction of the investment account.

Loans:

The Bank grants mortgage, commercial and consumer loans to customers. A substantial portion of the loan portfolio is represented by real estate loans secured by properties located in Tennessee. The ability of the Bank's debtors to honor their contracts is somewhat dependent on the real estate and economic conditions in these states.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity are stated at unpaid principal balances less the allowance for loan losses.

The Bank does not defer loan fees and related loan origination costs. Based on management's assessment, the difference between deferral and immediate recognition of such fees and related costs is not material.

Interest income is accrued based on the unpaid principal balance. 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. Credit card loans and other consumer loans are typically charged off between 90 and 120 days past due. 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 charged off is 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.

Allowance for loan losses:

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1. Summary of Significant Accounting Policies (continued)

Allowance for loan losses: (continued)

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of allocated and general components. The allocated component relates to loans that are classified as impaired. For those loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical charge-off experience and expected loss given default derived from the Bank's internal risk rating process. Other adjustments may be made to the allowance for pools of loans after an assessment of internal or external influences on credit quality that are not fully reflected in the historical loss or risk rating data.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due 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.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer and residential loans for impairment disclosures, unless such loans are the subject of a restructuring agreement due to financial difficulties of the borrower.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1. Summary of Significant Accounting Policies (continued)

Derivatives:

Derivatives are recognized as assets and liabilities on the consolidated balance sheet and measured at fair value. For exchange-traded contracts, fair value is based on quoted market prices. For nonexchange traded contracts, fair value is based on dealer quotes, pricing models, discounted cash flow methodologies, or similar techniques for which the determination of fair value may require significant management judgment or estimation.

For asset/liability management purposes, the Company and Bank use interest rate swap agreements to hedge various exposures or to modify interest rate characteristics of various balance sheet accounts. Interest rate swaps are contracts in which a series of interest rate flows are exchanged over a prescribed period. The notional amount on which the interest payments are based is not exchanged. These swap agreements are derivative instruments and generally convert a portion of the Company's and Bank's variable-rate debt to a fixed rate.

The effective portion of the gain or loss on a derivative designated and qualifying as a cash flow hedging instrument is initially reported as a component of other comprehensive income and subsequently reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. The ineffective portion of the gain or loss on the derivative instrument, if any, is recognized currently in earnings.

Interest rate derivative financial instruments receive hedge accounting treatment only if they are designated as hedge and are expected to be, and are, effective in substantially reducing interest rate risk arising from the assets and liabilities identified as exposing the Company and Bank to risk. Those derivative financial instruments that do not meet specified hedging criteria are recorded at fair value with changes in fair value recorded in income. If periodic assessment indicates derivatives no longer provide an effective hedge, the derivative contracts would be closed out and settled, or classified as a trading activity.

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 Bank, (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 Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before maturity.

Premises and equipment:

Land is carried at cost. Other premises and equipment are carried at cost net of accumulated depreciation. Depreciation is computed using the straight-line and the declining balance methods based principally on the estimated useful lives of the assets. Maintenance and repairs are expensed as incurred while major additions and improvements are capitalized. Gains and losses on dispositions are included in current operations.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1. Summary of Significant Accounting Policies (continued)

Foreclosed assets:

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. Revenues and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets.

Income taxes:

The Company accounts for income taxes in accordance with income tax accounting guidance in ASC Topic 740. 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 taxable income or loss. The Company determines deferred income taxes using the liability 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. The Company's deferred taxes relate primarily to differences between the basis of the allowance for loan losses and accumulated depreciation. Deferred tax assets and liabilities are reflected at income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. The Company files consolidated income tax returns with its subsidiary. With few exceptions, the Company is no longer subject to tax examinations by tax authorities for years before 2007.

The Company has elected to be taxed under the provisions of Subchapter S of the Internal Revenue Code. Earnings and losses are included in the personal income tax returns of the stockholders and taxed depending on their personal tax strategies. Accordingly, the Company does not incur federal income tax obligations, and the financial statements do not include a provision for federal income taxes.

The Company recognizes deferred tax assets if it is more likely than not, based on the technical merits, that the tax position will be realized or sustained upon examination. The Company follows the statutory requirements for its income tax accounting and generally avoids risks associated with potentially problematic tax positions that may be challenged upon examination. The Company recognizes interest and penalties on income taxes as a component of income tax expense.

Advertising costs:

The Company follows the policy of charging the costs of advertising to expense as incurred. Advertising expense charged to operations was \$268,923 and \$304,141 for the years ended December 31, 2010 and 2009, respectively.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1. Summary of Significant Accounting Policies (continued)

Statements of cash flows:

The Company considers all cash and amounts due from depository institutions to be cash equivalents for purposes of the statements of cash flows.

Stock option plan:

The Company recognizes compensation cost relating to share-based payment transactions in accordance with ASC Topic 718. Compensation cost has been measured based on the grant date fair value of the equity or liability instruments issued. Compensation cost is calculated and recognized over the employee service period, generally defined as the vesting period. The Company uses a stock option pricing model to determine the fair value of the award on the grant date.

Variable interest entities:

An entity is referred to as a variable interest entity (VIE) if it meets the criteria outlined in ASC Topic 810, which are: (1) the entity has equity that is insufficient to permit the entity to finance its activities without additional subordinated financial support from other parties, or (2) the entity has equity investors that cannot make significant decisions about the entity's operations or that do not absorb the expected losses or receive the expected returns of the entity. A VIE must be consolidated by the Company if it is deemed to be the primary beneficiary of the VIE, which is the party involved with the VIE that has a majority of the expected losses, expected residual returns, or both. The Company has two wholly-owned subsidiary grantor trusts which are deemed to be VIEs. These two VIEs have not been consolidated by the Company as BancTenn Corp is not the primary beneficiary.

Subsequent events:

Management performed an evaluation of subsequent events through April 5, 2011 the date these financial statements were issued.

Note 2. Restrictions on Cash and Due From Banks

The Bank is required to maintain average balances on hand or with the Federal Reserve Bank based on a percentage of deposits. At December 31, 2010 and 2009, these reserve balances were approximately \$25,000.

BANCTENN CORP. AND SUBSIDIARY
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Note 3. Securities Available for Sale

Securities have been classified in the balance sheet according to management's intent as securities available for sale. The amortized cost and fair value of investment securities at December 31, 2010 and 2009 are as follows:

	2010			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Debt securities:				
U.S. Government-sponsored enterprises (GSEs)	\$ 14,570,974	\$ 5,730	\$ (121,475)	\$14,455,229
Obligations of states and political subdivisions	16,539,522	443,766	(138,240)	16,845,048
Mortgage-backed securities:				
GSE residential	45,243,976	35,415	(378,912)	44,900,479
Equity securities	<u>236,569</u>	<u>-</u>	<u>(129,584)</u>	<u>106,985</u>
	<u>\$ 76,591,041</u>	<u>\$ 484,911</u>	<u>\$ (768,211)</u>	<u>\$76,307,741</u>
	2009			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Debt securities:				
U.S. Government-sponsored enterprises (GSEs)	\$ 3,000,000	\$ 3,430	\$ -	\$ 3,003,430
Obligations of states and political subdivisions	27,551,530	744,620	(11,497)	28,284,653
Mortgage-backed securities:				
GSE residential	59,900,112	2,600,970	(40,991)	62,460,091
Equity securities	<u>468,305</u>	<u>-</u>	<u>(251,618)</u>	<u>216,687</u>
	<u>\$ 90,919,947</u>	<u>\$ 3,349,020</u>	<u>\$ (304,106)</u>	<u>\$93,964,861</u>

U.S. Government sponsored enterprises include entities such as Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, and Federal Home Loan Banks.

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Note 3. Securities Available for Sale (continued)

Upon acquisition of a security, the Company determines the appropriate impairment model that is applicable. If the security is a beneficial interest in securitized financial assets, the Company uses the beneficial interests in securitized financial assets impairment model. If the security is not a beneficial interest in securitized financial assets, the Company uses the debt and equity securities impairment model. The Company conducts periodic reviews to evaluate each security to determine whether an other-than-temporary impairment has occurred. The Company does not have any securities that have been classified as other-than-temporarily-impaired at December 31, 2010.

The scheduled maturities of securities available for sale at December 31, 2010, are as follows:

	Amortized Cost	Fair Value
Due in one year or less	\$ 265,187	\$ 267,634
Due from one year to five years	12,830,676	12,854,812
Due from five years to ten years	10,828,343	11,022,061
Due after ten years	7,186,290	7,155,770
Mortgage-backed and related securities	45,243,976	44,900,479
Securities with no stated maturity	236,569	106,985
	<u>\$76,591,041</u>	<u>\$76,307,741</u>

Sales of available for sale securities for the years ended December 31, 2010 and 2009 were as follows:

	2010	2009
Proceeds	\$65,221,826	\$17,751,993
Gross gains realized	2,733,314	488,698
Gross losses realized	(209,763)	(105,706)

At December 31, 2010 and 2009, gross unrealized losses on investments were insignificant in relation to the Company's investment portfolio.

Securities with an amortized cost of approximately \$40,572,000 and \$80,482,000 at December 31, 2010 and 2009, respectively, were pledged to secure various deposits and borrowings.

BANCTENN CORP. AND SUBSIDIARY
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Note 4. Equity Investments

Investment in Paragon Commercial Corporation:

During 2009, the Company determined Paragon Commercial Corporation (Paragon) experienced declining asset quality and would need additional capital. The Company has determined it is not likely to maintain its current level of ownership and will no longer have significant influence over the operations of Paragon. Accordingly, the Company stopped accounting for this investment using the equity method of accounting.

The Company also determined its investment in Paragon was impaired at December 31, 2010 and 2009, and recorded an impairment charge of \$2,672,558 and \$2,353,793, respectively.

Investment in Appalachian Fund for Growth II:

During 2006, the Company invested \$3,000,000 for a 25% share of the Appalachian Fund for Growth II partnership (AFG), which is managed by the Southeast Local Development Corporation (General Partner). AFG will use the investments received in formation to make below-market rate senior and subordinated debt products to businesses seeking to build, renovate, expand and equip their business facilities. AFG will target high job creation and retention businesses and businesses providing important community services. The funds will be deployed to help: (1) attract new businesses to its under-served service area by offering creative financing; (2) supply creative financing for businesses to rehabilitate existing distressed properties to facilitate community development; and (3) leverage other private investment into its targeted communities. In return for their investment the Company and the other investors will receive new market tax credits. For 2010 the Company received approximately \$180,000 in new market tax credits.

AFG meets the criteria of a VIE outlined in ASC Topic 810. AFG has not been consolidated by the Company as the Company is not the primary beneficiary.

Note 5. Loans and Allowance For Loan Losses

A summary of transactions in the allowance for loan losses for the years ended December 31, 2010 and 2009, is as follows:

	<u>2010</u>	<u>2009</u>
Balance, beginning of year	\$7,201,023	\$5,627,070
Loans charge off	(5,131,042)	(3,257,127)
Recoveries of loans charged off	463,750	163,080
Provision charged to operating expense	<u>5,136,337</u>	<u>4,668,000</u>
Balance, end of year	<u><u>\$7,670,068</u></u>	<u><u>\$7,201,023</u></u>

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Note 5. Loans and Allowance For Loan Losses (continued)

At December 31, 2010 and 2009, the Bank's loans consist of the following (in thousands):

	<u>2010</u>	<u>2009</u>
Loans secured by real estate:		
Residential	\$200,457	\$186,547
Commercial	150,065	144,783
Construction	54,735	63,634
Other	<u>1,219</u>	<u>1,234</u>
Total loans secured by real estate	406,476	396,198
Commercial loans	41,500	51,236
Consumer loans	5,398	5,650
State and political subdivisions	4,284	4,176
Other loans	<u>14,167</u>	<u>22,429</u>
Total loans	471,825	479,689
Less - Allowance for loan losses	<u>(7,670)</u>	<u>(7,201)</u>
Net loans	<u>\$464,155</u>	<u>\$472,488</u>

In the normal course of business, the Bank makes loans to directors and executive officers of the Bank on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other borrowers. Loans to directors and executive officers totaled \$570,738 and \$706,828 at December 31, 2010 and 2009, respectively.

The Company follows the loan impairment accounting guidance in ASC Topic 310. A loan is considered impaired when, based on current information and events, it is probable that the Company 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 and loans modified in troubled debt restructurings where concessions have been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in interest rates, payment extensions, forgiveness of principal, forbearance or other actions intended to maximize collections.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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Note 5. Loans and Allowance For Loan Losses (continued)

At December 31, 2010 and 2009, information pertaining to impaired loans is as follows (in thousands):

	<u>2010</u>	<u>2009</u>
Impaired loans without a valuation allowance	\$ 19,231	\$ 13,524
Impaired loans with a valuation allowance	<u>11,883</u>	<u>10,636</u>
Total impaired loans	<u>\$ 31,114</u>	<u>\$ 24,160</u>
Valuation allowance related to impaired loans	<u>\$ 1,717</u>	<u>\$ 2,022</u>
Total nonaccrual loans	<u>\$ 5,347</u>	<u>\$ 6,420</u>
Total loans past due ninety days or more and still accruing	<u>\$ 26</u>	<u>\$ -</u>
Average investment in impaired loans	<u>\$ 25,686</u>	<u>\$ 22,117</u>

Included in impaired loans are troubled debt restructurings that are classified as impaired. At December 31, 2010 and 2009, the Company had loans of approximately \$11,889,000 and 5,470,000, respectively, that were modified in troubled debt restructurings and impaired.

The interest income recognized for cash payments received on impaired loans during 2010 and 2009 was \$1,404,087 and \$849,457, respectively.

Note 6. Premises and Equipment

A summary of premises and equipment at December 31, 2010 and 2009, is as follows:

	<u>2010</u>	<u>2009</u>
Land	\$ 5,377,122	\$ 5,088,426
Buildings and leasehold improvements	26,619,622	25,802,284
Furniture and equipment	9,118,978	8,506,829
Transportation equipment	1,155,910	1,155,910
Construction in progress	<u>54,828</u>	<u>167,175</u>
	42,326,460	40,720,624
Accumulated depreciation	<u>(14,219,156)</u>	<u>(12,632,024)</u>
	<u>\$ 28,107,304</u>	<u>\$ 28,088,600</u>

BANCTENN CORP. AND SUBSIDIARY
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Note 7. Foreclosed real estate

Foreclosed real estate is held for sale and is initially recorded at fair value less estimated selling cost at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed and any write-downs are recorded as a charge to operations, if necessary, to reduce the carrying value of a property to the lower of its cost or fair value less cost to sell. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. The portion of interest costs relating to development of real estate (if any) is capitalized.

Expenses applicable to foreclosed real estate during 2010 and 2009, include the following:

	<u>2010</u>	<u>2009</u>
Net loss (gain) on sales of real estate	\$ 289,924	\$ (95,437)
Provision for losses	88,916	371,905
Property taxes	115,398	39,067
Maintenance and insurance	139,051	40,315
Other	96,942	30,406
	<u>\$ 730,231</u>	<u>\$ 386,256</u>

Note 8. Deposits

The composition of deposits at December 31, 2010 and 2009, is as follows:

	<u>2010</u>	<u>2009</u>
Demand deposits, noninterest bearing	\$ 124,452,704	\$ 93,793,923
NOW accounts	86,195,896	83,212,166
Money market accounts	148,574,710	120,049,843
Savings accounts	35,524,520	34,289,701
Time deposits	126,759,907	138,832,334
Total	<u>\$ 521,507,737</u>	<u>\$ 470,177,967</u>

The aggregate amount of time deposits in denominations of \$100,000 or more at December 31, 2010, were approximately \$67,071,000. At December 31, 2010, the scheduled maturities of time deposits are as follows (in thousands):

Less than one year	\$ 102,299
One through three years	13,322
Three years and greater	<u>11,139</u>
	<u>\$ 126,760</u>

BANCTENN CORP. AND SUBSIDIARY
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Note 9. Federal Home Loan Bank Advances

The Bank has an agreement with the Federal Home Loan Bank (FHLB) that can provide short-term and long-term funding to the Bank in an amount up to \$90,266,243. The Bank has pledged its loans secured by one to four single-family mortgages, second mortgages and home equity lines, multi-family, commercial real estate, and agricultural real estate properties. The collateral to loan ratio ranges from 140% to 320%.

At December 31, 2010, the Bank held a letter of credit from the Federal Home Loan Bank totaling \$30,000,000. The letter of credit is used by the Bank as collateral for public deposits.

At December 31, 2010 and 2009, FHLB advances consist of the following:

	<u>2010</u>	<u>2009</u>
Long-term advance requiring monthly interest payments, fixed at 2.86% until December 2017, principal due in December 2017	\$ 10,000,000	\$ 10,000,000
Long-term advance requiring monthly interest payments, fixed at 3.90% until June 2013, principal due in June 2013	5,000,000	5,000,000
Long-term advance requiring monthly interest payments, fixed at 3.73% until August 2013, principal due in August 2013	10,000,000	10,000,000
Long-term advance requiring monthly interest payments, fixed at 2.76% until October 2013, principal due in October 2013	5,000,000	5,000,000
Long-term advance requiring monthly interest payments, fixed at 2.85% until September 2014, principal due in September 2014	3,000,000	3,000,000
Long-term amortizing advance requiring monthly principal and interest payments, fixed at 2.30% until February 2023, final payment due in February 2023	2,227,992	2,286,380
Long-term amortizing advance requiring monthly principal and interest payments, fixed at 2.00% until July 2030, final payment due in July 2030	589,790	-
Short-term advance requiring principal and interest payment in January 2010, fixed at 0.09%	-	6,000,000
	<u>\$ 35,817,782</u>	<u>\$ 41,286,380</u>

BANCTENN CORP. AND SUBSIDIARY
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Note 9. Federal Home Loan Bank Advances (continued)

The long-term advances may be prepaid subject to a prepayment penalty as defined in the agreements. The FHLB has the right to exercise a put on certain of these advances as defined in the agreements.

Maturities by year at December 31, 2010, are as follows:

2013	\$ 20,000,000
2014	3,000,000
Thereafter	<u>12,817,782</u>
	<u>\$ 35,817,782</u>

Note 10. Borrowings Under Line of Credit and Other Borrowings

During 2010, the Company entered into a line of credit with another financial institution. This line of credit requires monthly interest payments with a prime based interest rate of 3.25%. The line is renewable each year with a current maturity date of August 31, 2011. This line is secured by 100% of the Bank's common stock. At December 31, 2010 and 2009, the Company had \$160,000 and zero outstanding, respectively.

During 2009, the Bank began participating in the Federal Reserve's Term Auction Facility program. Total borrowings under this program were \$10,000,000 at December 31, 2009. The borrowing was a short-term advance requiring principal and interest payment in January 2010 with interest fixed at 0.25%. At December 31, 2010, the Bank had no outstanding borrowings under this program.

Note 11. Securities Sold Under Agreements to Repurchase

Securities sold under agreements to repurchase represent the purchase of interest in securities by commercial checking customers. The Company may also enter into structured repurchase agreements with other financial institutions. Repurchase agreements with commercial checking customers generally settle the following business day, while structured repurchase agreements with other financial institutions will have varying terms.

At December 31, 2010 and 2009, the Company had securities sold under agreements to repurchase of \$6,090,232 and \$18,987,082, respectively, with commercial checking customers. The Company had structured repurchase agreements with other financial institutions of \$10,000,000 at December 31, 2010 and \$35,000,000 at December 31, 2009.

At December 31, 2010, the structured repurchase agreement has a ten-year term with a fixed interest rate of 3.72%. This agreement matures in 2018. The Company has pledged securities with an amortized cost of approximately \$12,678,127 to secure this agreement. During 2010, the Company reduced its structured repurchase agreement obligation by \$25,000,000 and incurred a \$1,638,000 prepayment penalty.

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Note 12. Subordinated Debentures

Effective June 22, 2004 and December 4, 2006, two wholly-owned subsidiary grantor trusts were established by the Company, BancTenn Capital Trust II and BancTenn Capital Trust III, respectively. These subsidiaries issued \$6,000,000 and \$9,000,000 of pooled Trust Preferred Securities (“trust preferred securities”), respectively. Trust preferred securities accrue and pay distributions periodically at specified annual rates as provided in the indentures. The trust used the net proceeds from the offering to purchase a like amount of Junior Subordinated Debentures (the “Debentures”) of the Company. The Debentures are the sole assets of the trust. The trust preferred securities are mandatorily redeemable upon the maturity of the Debentures, or upon earlier redemption as provided in the indentures. The Company has the right to redeem the Debentures in whole or in part after specific dates, at a redemption price specified in the indenture plus any accrued but unpaid interest to the redemption date. The trust preferred securities have a maturity of 30 years and are redeemable after five years with certain exceptions. At December 31, 2010, the floating-rate securities in BancTenn Capital Trust II had a 2.94% interest rate which resets quarterly at the three-month LIBOR rate plus 2.65% and BancTenn Capital Trust III had a 1.95% interest rate which resets quarterly at the three-month LIBOR rate plus 1.65%.

For regulatory capital purposes, these trust-preferred securities qualify as a component of Tier I capital, subject to certain limitations.

ASC Topic 810 resulted in the Company’s investment in the common equity of the trust being included in the consolidated balance sheets as other assets, totaling \$465,000 at December 31, 2010 and 2009. The outstanding balance of the subordinated debentures was \$15,465,000 at December 31, 2010 and 2009.

Note 13. Derivatives Instruments – Interest Rate Contracts

Cash flow hedges:

The Company currently has two interest rate swap derivative instruments, used to minimize interest rate volatility on trust preferred securities, which are designated and qualify as cash flow hedges.

In March 2008, the Company, relating to the Company’s subordinated debentures, entered into an interest rate swap agreement with Compass Bank to pay a fixed rate of 5.49% while receiving a variable rate of the three-month LIBOR plus 165 basis points. This swap has a \$9 million notional value and the termination date is March 2015.

In December 2008, the Company, relating to the Company’s subordinated debentures, entered into a second interest rate swap agreement with Compass Bank to pay a fixed rate of 5.48% while receiving a variable rate of the three-month LIBOR plus 265 basis points. This swap has a \$6 million notional value and the termination date is January 2019.

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Note 13. Derivatives Instruments – Interest Rate Contracts (continued)

Cash flow hedges: (continued)

At December 31, 2010, the estimated fair value of the cash flow hedge derivative instruments recorded in other liabilities was \$724,568. At December 31, 2009, the estimated fair value of the cash flow hedge derivative instruments recorded in other assets was \$29,291. Changes in the fair value of the derivative instruments are reported in accumulated other comprehensive income. These amounts subsequently are reclassified into interest expense as a yield adjustment in the same period in which the related interest on the subordinated debentures affects earnings. Included in interest expense is \$470,786 which resulted from the reclassification of accumulated other comprehensive income into earnings during 2010. The interest expense recorded for the hedged derivatives in 2009 was \$377,197. Hedge ineffectiveness recognized into income during 2010 and 2009 was insignificant.

Non-hedged derivatives:

The Company also entered into three interest rate swap agreements with Compass Bank to pay a fixed rate of 5.21% while receiving a variable rate of the one-month LIBOR plus 225 basis points. The Company then entered into reciprocal agreements with three customers. These swaps had an initial notional value of \$13,010,517 and will decline until the termination dates from May 2013 through February 2014 based on a set amortization schedule. At December 31, 2010, the estimated fair value of the non-hedged derivative instruments recorded in other assets and liabilities was \$634,865. At December 31, 2009, the estimated fair value of the non-hedge derivative instruments recorded in other assets and liabilities was \$279,006. Included in interest income and interest expense are offsetting revenues and expenses of approximately \$343,985 in 2010 and \$333,754 in 2009 related to the non-hedged derivatives.

Note 14. Stock Option Plan

The Company has a stock option plan, which is administered by the Board of Directors, that provides for both incentive stock options and nonqualified stock options. The Company also grants non-qualified stock options to the Board of Directors. The maximum number of common shares that can be sold or optioned under the plan is 670,000 shares. Under the plan, the exercise price of each option shall not be less than 100 percent of the fair market value of the common stock on the date of grant. The effect of stock options forfeited is recognized as the forfeitures occur. For the years ended December 31, 2010 and 2009, the Company recognized \$4,767 and \$4,722 respectively, in compensation expense for stock options. At December 31, 2010, there is \$9,853 remaining compensation expense to be recognized on non-vested options.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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Note 14. Stock Option Plan (continued)

The fair value of options granted in 2009 was \$.17 per share. The fair value was estimated on the grant date using the Black-Scholes option pricing model assuming risk-free interest rates of 1.08% - 2.47%, a stock price volatility of 0.69%, an expected dividend yield of 2.50% and a life expectancy of 2.5 - 7.5 years for all options granted. If not exercised, the options will expire from December 13, 2011 to April 13, 2019.

The expected volatility is estimated from historical volatility. The risk-free interest rates for periods within the contractual life of the awards are based on the U.S. Treasury yield curve in effect at the time of the grant. The expected life is based on historical exercise experience. The dividend yield assumption is based on the Company's long-term business plan.

A summary of activity in the stock option plan for the years ended December 31, 2010 and 2009, is as follows:

	<u>2010</u>		<u>2009</u>	
	Number	Weighted	Number	Weighted
	of Shares	Average	of Shares	Average
	<u>Exercise Price</u>	<u>Exercise Price</u>	<u>Exercise Price</u>	<u>Exercise Price</u>
Outstanding, at beginning of year	144,610	\$42.30	155,290	\$40.56
Options granted	-	-	5,500	46.20
Options exercised	(21,138)	(26.88)	(16,180)	(26.93)
Options forfeited/expired	<u>(12,500)</u>	(49.38)	<u>-</u>	-
Outstanding at end of year	<u>110,972</u>	44.44	<u>144,610</u>	42.30

The aggregate intrinsic value of options outstanding at December 31, 2010, is \$107,125. The aggregate intrinsic value represents the total pre-tax intrinsic value (the amount by which the current market value of the underlying stock exceeds the exercise price of the option) that would have been received by the option holders had all option holders exercised their options on December 31, 2010. This amount changes based on changes in the market value of the Company's stock. The fair value (present value of the estimated future benefit to the option holder) of each option grant is estimated on the date of grant using the Black-Scholes option pricing model.

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Note 14. Stock Option Plan (continued)

Information pertaining to options outstanding at December 31, 2010, is as follows:

Number Outstanding	Options Outstanding		Number Exercisable	Options Exercisable	
	Weighted Average Remaining Life	Weighted Average Exercise Price		Weighted Average Exercise Price	Weighted Average Exercise Price
8,092	1.0 Years	\$25.85	8,092	\$25.85	
7,000	2.2 Years	28.67	7,000	28.67	
2,800	2.9 Years	32.30	2,800	32.30	
10,080	4.0 Years	36.25	10,080	36.25	
5,500	6.9 Years	46.20	2,300	46.20	
19,000	5.0 Years	48.50	19,000	48.50	
46,500	6.9 Years	48.55	20,700	48.55	
2,000	6.7 Years	49.10	1,200	49.10	
<u>10,000</u>	2.2 Years	53.41	<u>4,000</u>	53.41	
<u>110,972</u>	5.06 Years	44.44	<u>75,172</u>	42.18	

Information related to non-vested options for the year ended December 31, 2010, is as follows:

	Number of Shares	Weighted Average Grant Date Fair Value
Non-vested Options, December 31, 2009	54,450	\$49.10
Granted	-	-
Vested	(13,650)	(49.13)
Forfeited	<u>(5,000)</u>	(48.53)
Non-vested options, December 31, 2010	<u>35,800</u>	49.17

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Note 15. Income Taxes

The Company files consolidated income tax returns with its subsidiary, Bank of Tennessee. Under the terms of a tax-sharing agreement, the subsidiary's allocated portion of the consolidated tax liability is computed as if it were reporting its income and expenses as a separate entity.

The provision for income taxes in the consolidated statements of income for the years ended December 31, 2010 and 2009, includes the following:

	2010	2009
Current tax expense:		
State	\$ 187,500	\$ 418,700
Federal	-	12,600
	\$ 187,500	\$ 431,300
Deferred income taxes related to:		
Provision for loan losses	(30,500)	(102,300)
Depreciation	3,100	8,200
Deferred compensation retirement plans	(20,400)	(31,900)
Undistributed net earnings of investee	(173,700)	(153,100)
Cash method of accounting	42,100	5,300
Other	58,548	(62,827)
Provision for income taxes	\$ 66,648	\$ 94,673

Deferred tax assets recognized for deductible temporary differences totaled \$880,017 and \$734,183 at December 31, 2010 and 2009, respectively. Deferred tax liabilities for taxable temporary differences totaled \$390,875 and \$721,536 at December 31, 2010 and 2009, respectively.

The Company files its consolidated tax return as an S Corporation under the Internal Revenue Code. Consequently, the Company no longer pays normal federal income tax. The federal income tax effects of the Company's operations will be included in each stockholder's personal tax return. Federal tax expense for 2010 and 2009 shown above represents tax on built-in-gains existing at the date of conversion to S Corporation status.

BANCTENN CORP. AND SUBSIDIARY

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Note 16. Employee Retirement Plans

The Company has a salary reduction/profit-sharing plan under the provisions of Section 401(k) of the Internal Revenue Code. All employees are eligible to participate immediately upon hire. The Plan provides for contributions by the Company in such amounts as determined by the Board of Directors not to exceed 6 percent of the participant's annual compensation. In addition, the Plan provides for the Company to match employee contributions to the Plan equal to 50 percent of the first 6 percent of the participant's annual compensation. The Company contributed \$171,386 and \$201,693 to the Plan for the years ended December 31, 2010 and 2009, respectively.

The Company and the Bank provide deferred compensation agreements for the benefit of senior and executive officers. The Bank records the estimated amount of future payments to be made over the active service periods of the officers. Deferred compensation expense under these agreements was \$336,703 and \$394,204 for the years ended December 31, 2010 and 2009, respectively.

Note 17. Employee Stock Ownership Plan

Effective January 1, 2004, the Company established an Employee Stock Ownership Plan (the Plan), within the guidelines as defined by the Internal Revenue Code, for the purpose of enabling participants to acquire an ownership interest in the Company. All employees are eligible to participate in the Plan after completing one year of service with a minimum of 1,000 hours. Initial funding for the purchase of the Company's common stock was provided by Security Acquisition Loans from the Company to the Plan. The Security Acquisition Loans call for principal and interest to be repaid in ten equal annual installments of principal and interest. Shares obtained in connection with Security Acquisition Loans are held in a suspense account and are classified as unallocated shares.

Contributions are made to the Plan as determined by the Company's Board of Directors, generally commensurate with the debt service requirements set forth in the loan agreements. Unallocated shares held in suspense by the Plan are released based on the ratio of principal payments made in the current year to total required future principal payments. Shares of the Company's common stock owned by the Plan are allocated as of each year end to each participant based on the ratio of individual compensation to total covered compensation, as defined by the agreement. Contributions can be in the form of cash, shares of Company stock, or other property as determined by the Board.

S Corporation distributions related to unallocated shares are used to fund the debt service requirements defined in the Security Acquisition Loans. Any remaining distributions are allocated proportionately to the participant, as defined by the plan agreement. At the Board's discretion, S Corporation distributions related to allocated shares may be used to make payments on Securities Acquisition Loans or shall be allocated to the participants, in accordance with the plan agreement.

The Company recognizes compensation expense for contributions and for allocated shares that were previously unallocated. The fair value, as determined by an independent appraisal, is used to calculate the compensation expense. Compensation expense recognized in association with the Plan for 2010 and 2009 totaled \$211,811 and \$272,910, respectively.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 17. Employee Stock Ownership Plan (continued)

When a participant retires or otherwise terminates from the Plan, the Company is required to offer the participant the fair value for any allocated, vested shares of company stock. If the participant declines this option, the Company retains the right of first refusal of such shares. At December 31, 2010 and 2009, there were no repurchase obligations outstanding.

The fair value of unallocated shares at December 31, 2010, was \$33.95 per share. This value was determined by the most recent stock valuation performed as of August 15, 2010. The number of shares allocated, unallocated and committed to be released totaled 29,965, 16,253 and zero, respectively, as of December 31, 2010.

Note 18. Financial Instruments With Off-Balance-Sheet Risk

In the normal course of business, the Bank has outstanding commitments and contingent liabilities, such as commitments to extend credit and standby letters of credit, which are not included in the accompanying financial statements. The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual or notional amount of those instruments. The Bank uses the same credit policies in making such commitments as it does for instruments that are included in the balance sheet. At December 31, 2010, commitments under standby letters of credit were approximately \$1,653,000, and undisbursed loan commitments aggregated approximately \$66,590,000.

Commitments to extend credit 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 many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include accounts receivable, inventory, property and equipment, and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Standby letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank's policy for obtaining collateral, and the nature of such collateral, is essentially the same as that involved in making commitments to extend credit.

At December 31, 2010 and 2009, the financial guarantees the Bank was required to fund were insignificant. The Bank has not incurred any losses on its commitments in either 2010 or 2009.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 19. Fair Value Disclosures

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. In accordance with ASC Topic 820, "Fair Value Measurements and Disclosures", the fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

ASC Topic 820 provides a consistent definition of fair value, which focuses on exit price in an orderly transaction between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions.

ASC Topic 820 also establishes a three-tier fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value, as follows:

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access.

Level 2 - Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities in active markets, quoted prices in markets that are not active and other inputs that are observable or can be corroborated by observable market data.

Level 3 - Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 19. Fair Value Disclosures (continued)

The following methods and assumptions were used by the Company in estimating fair value disclosures for financial instruments:

Cash and cash equivalents:

The carrying amounts of cash and cash equivalents approximate fair values based on the short-term nature of the assets.

Certificates of deposit with other financial institutions:

The carrying amount of certificates of deposit with other financial institutions approximates fair value based on the short-term nature of these assets.

Securities available for sale:

Fair values are estimated using pricing models and discounted cash flows that consider standard input factors such as observable market data, benchmark yields, interest rate volatilities, broker/dealer quotes, and credit spreads. Securities classified as available for sale are reported at fair value utilizing Level 2 inputs.

Restricted investments:

The carrying value of restricted investments approximates fair value based on the stock redemption provisions of the respective entities.

Federal funds sold:

For federal funds sold, the carrying amount is a reasonable estimate of fair value.

Loans:

For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for fixed-rate loans are estimated using discounted cash flow analyses, using market interest rates for comparable loans. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment in accordance with ASC Topic 310, "Accounting by Creditors for Impairment of a Loan". The fair value of impaired loans is estimated using several methods including collateral value, liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 19. Fair Value Disclosures (continued)

Loans: (continued)

exceed the recorded investments in such loans. At December 31, 2010 and 2009, substantially all of the total impaired loans were evaluated based on the fair value of collateral. In accordance with ASC Topic 820, impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3.

Cash surrender value of life insurance:

The carrying amounts of cash surrender value of life insurance approximate their fair value. The carrying amount is based on information received from the insurance carriers indicating the financial performance of the policies and the amount the Company would receive should the policies be surrendered. The Company reflects these assets within Level 2 of the valuation hierarchy.

Foreclosed real estate and repossessed assets:

Foreclosed real estate and repossessed assets, consisting of properties and other assets obtained through foreclosure, repossession or in satisfaction of loans, is initially recorded at fair value, determined on the basis of current appraisals, comparable sales, and other estimates of value obtained principally from independent sources, adjusted for estimated selling costs. At the time of foreclosure or repossession, any excess of the loan balance over the fair value of the asset held as collateral is treated as a charge against the allowance for loan losses. Gains or losses on sale and any subsequent adjustment to the fair value are recorded as a component of foreclosed real estate or repossession expense. When the fair value is based on an observable market price or a current appraised value, the Company records the asset as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the asset is further impaired below the appraised value and there is no observable market price, the Company records the asset as nonrecurring Level 3.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 19. Fair Value Disclosures (continued)

Deposits:

The fair value of deposits with no stated maturity, such as noninterest-bearing demand deposits and NOW, money market, and savings accounts, is equal to the amount payable on demand at the reporting date. The carrying amounts of variable-rate, fixed-term money market accounts and certificates of deposit approximate their fair values at the reporting date. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates on comparable instruments to a schedule of aggregated expected monthly maturities on time deposits.

Securities sold under agreements to repurchase and federal funds purchased:

For securities sold under agreements to repurchase with commercial checking customers and federal funds purchased, the estimated fair value approximates their carrying value.

The fair value of structured repurchase agreements is calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates.

Subordinated debentures:

The carrying amount of the subordinated debentures with floating interest rates is a reasonable estimate of fair value.

Borrowings under line of credit:

The carrying amount of the borrowings under line of credit with floating interest rates is a reasonable estimate of fair value.

Interest rate swaps:

Substantially all interest rate swaps held or issued by the Company for risk management are traded in over-the-counter markets where quoted market prices are not readily available. For these derivatives, the Company measures fair value using models that use primarily market observable inputs, such as yield curves and option volatilities, and include the value associated with counterparty risk. The Company classifies interest rate swaps held or issued for risk management activities as Level 2 inputs.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 19. Fair Value Disclosures (continued)

Federal Home Loan Bank advances:

Fair values of advances are estimated using discounted cash flow analyses based on current market rates for similar types of borrowing arrangements.

Other borrowings:

The carrying value approximates the estimated fair value based on the short-term nature of the borrowings.

Accrued interest:

The carrying amounts of accrued interest approximate fair value.

The tables below present the recorded amount of assets and liabilities measured at fair value on a recurring basis.

	Balance as of December 31, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Financial Assets:				
Securities available for sale:				
U.S. Government sponsored enterprises	\$14,455,229	\$ -	\$ 14,455,229	\$ -
Obligations of states and political subdivisions	16,845,048	-	16,845,048	-
Mortgage-backed securities - GSE residential	44,900,479	-	44,900,479	-
Equity securities	106,985	-	106,985	-
Total securities available for sale	<u>\$76,307,741</u>	<u>\$ -</u>	<u>\$ 76,307,741</u>	<u>\$ -</u>
Cash surrender value of life insurance	\$14,070,635	\$ -	\$ 14,070,635	\$ -
Financial Liabilities:				
Interest rate swaps	\$ 724,568	\$ -	\$ 724,568	\$ -

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 19. Fair Value Disclosures (continued)

	Balance as of December 31, 2009	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Financial Assets:				
Securities available for sale:				
U.S. Government				
sponsored enterprises	\$ 3,003,430	\$ -	\$ 3,003,430	\$ -
Obligations of states				
and political				
subdivisions	28,284,653	-	28,284,653	-
Mortgage-backed				
securities -				
GSE residential	62,460,091	-	62,460,091	-
Equity securities	<u>216,687</u>	<u>-</u>	<u>216,687</u>	<u>-</u>
Total securities				
available for sale	<u>\$ 93,964,861</u>	<u>\$ -</u>	<u>\$ 93,964,861</u>	<u>\$ -</u>
Interest rate swaps	\$ 29,291	\$ -	\$ 29,291	\$ -
Cash surrender value of				
life insurance	13,508,606	-	13,508,606	-

The Company has no assets or liabilities whose fair values are measured on a recurring basis using Level 3 inputs.

Certain assets and liabilities are measured at fair value on a nonrecurring basis, which means the assets and liabilities are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 19. Fair Value Disclosures (continued)

The tables below present information about assets and liabilities on the balance sheet at December 31, 2010 and 2009, for which a nonrecurring change in fair value was recorded (in thousands):

	Balance as of December 31, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Impaired loans	\$ 10,166	\$ -	\$ 1,761	\$ 8,405
Foreclosed real estate	7,274	-	5,441	1,833
Repossessed assets	409	-	-	409
Investment in Paragon Commercial Corporation	10,439	-	10,439	-
Other assets	83	-	-	83

	Balance as of December 31, 2009	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Impaired loans	\$ 8,614	\$ -	\$ 3,309	\$ 5,305
Foreclosed real estate	5,415	-	3,421	1,994
Repossessed assets	510	-	-	510
Investment in Paragon Commercial Corporation	13,111	-	13,111	-
Other assets	238	-	-	238

Loans include impaired loans held for investment for which an allowance for loan losses has been calculated based upon the fair value of the loans at December 31, 2010 and 2009. Losses derived from Level 2 inputs were calculated by models incorporating significant observable market data. Losses derived from Level 3 inputs were calculated primarily by models utilizing management's estimate of the collateral value.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 19. Fair Value Disclosures (continued)

The carrying amount and estimated fair value of the Company's financial instruments at December 31, 2010 and 2009, are as follows (in thousands):

	2010		2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets:				
Cash and due from banks	\$30,264	\$30,264	\$10,212	\$10,212
Certificates of deposit with other financial institutions	248	248	248	248
Securities available for sale	76,308	76,308	93,965	93,965
Restricted investments	2,427	2,427	2,427	2,427
Federal funds sold	340	340	1,135	1,135
Net loans	464,155	462,278	472,488	470,825
Cash surrender value of life insurance	14,071	14,071	13,509	13,509
Interest rate swaps	635	635	308	308
Accrued interest receivable	1,739	1,739	2,059	2,059
Liabilities:				
Noninterest-bearing demand deposits	124,453	124,453	93,794	93,794
NOW accounts	86,196	86,196	83,212	83,212
Savings and money market accounts	184,099	184,099	154,340	154,340
Time deposits	126,760	127,755	138,832	139,564
Securities sold under agreements to repurchase	16,090	16,876	53,987	55,948
Federal funds purchased	1,536	1,536	1,781	1,781
Subordinated debentures	15,465	15,465	15,465	15,465
Borrowings under line of credit	160	160	-	-
Interest rate swaps	1,359	1,359	279	279
Federal Home Loan Bank advances	35,818	37,776	41,286	41,972
Other borrowings	-	-	10,000	10,000
Accrued interest payable	319	319	511	511

Note 20. Liquidity and Capital Resources

The Company's primary source of funds with which to pay its future obligations is the receipt of dividends from its subsidiary bank. Bank regulations limit the amount of dividends that may be paid without prior approval of the Bank's regulatory authorities. It is management's intent to limit the amount of dividends paid in order to maintain compliance with capital guidelines and to maintain a strong capital position in the Bank.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 21. Related-Party Transactions

Bank of Tennessee provides data processing and other banking operational services to Carter County Bancorp and its wholly-owned subsidiary Carter County Bank, whose major shareholder is a principal shareholder and officer of the Company. Service revenue from Carter County Bancorp and Carter County Bank totaled \$1,137,781 and \$1,100,601 in 2010 and 2009, respectively.

Note 22. Other Comprehensive Income

Other comprehensive income consists of unrealized gains and losses on securities available for sale and interest rate swaps. A summary of other comprehensive income and the related tax effects for the years ended December 31, 2010 and 2009 is as follows:

	<u>Before Tax</u>	<u>Tax</u>	<u>Net of Tax</u>
	<u>Amount</u>	<u>(Expense)</u> <u>Benefit</u>	<u>Amount</u>
Year ended December 31, 2010:			
Unrealized holding gains and losses arising during the period	\$(1,558,521)	\$ 101,304	\$(1,457,217)
Less reclassification adjustment for gains realized in net income	<u>2,523,551</u>	<u>(164,031)</u>	<u>2,359,520</u>
	<u><u>\$(4,082,072)</u></u>	<u><u>\$ 265,335</u></u>	<u><u>\$(3,816,737)</u></u>
Year ended December 31, 2009:			
Unrealized holding gains and losses arising during the period	\$ 2,170,145	\$(141,059)	\$ 2,029,086
Less reclassification adjustment for gains realized in net income	<u>382,992</u>	<u>(24,894)</u>	<u>358,098</u>
	<u><u>\$ 1,787,153</u></u>	<u><u>\$(116,165)</u></u>	<u><u>\$ 1,670,988</u></u>

Note 23. Regulatory Matters

The Company (on a consolidated basis) and the Bank are subject to various regulatory capital requirements administered by the State of Tennessee Department of Financial Institutions and the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of the Company's and Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices.

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 23. Regulatory Matters

The Company's and the Bank's capital amounts and classification are 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 Company and the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 2010 and 2009, that the Company and the Bank meet all capital adequacy requirements to which they are subject.

As of December 31, 2010, the most recent notification from the regulators categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the Bank's prompt corrective action category.

The Company's and the Bank's actual capital amounts and ratios are also presented in the table. Dollar amounts are presented in thousands.

	Actual		For Capital Adequacy	
	Amount	Ratio	Amount	Ratio
As of December 31, 2010:				
Total capital to risk-weighted assets:				
Consolidated	\$71,721	14.38%	\$39,914	8.00%
Bank of Tennessee	59,887	12.28%	39,021	8.00%
Tier I capital to risk-weighted assets:				
Consolidated	65,467	13.12%	19,957	4.00%
Bank of Tennessee	53,770	11.02%	19,511	4.00%
Tier I capital to average assets:				
Consolidated	65,467	9.77%	26,794	4.00%
Bank of Tennessee	53,770	8.17%	26,322	4.00%
As of December 31, 2009:				
Total capital to risk-weighted assets:				
Consolidated	\$73,719	14.09%	\$41,856	8.00%
Bank of Tennessee	58,507	11.52%	40,615	8.00%
Tier I capital to risk-weighted assets:				
Consolidated	67,171	12.84%	20,928	4.00%
Bank of Tennessee	52,150	10.27%	20,307	4.00%
Tier I capital to average assets:				
Consolidated	67,171	10.07%	26,672	4.00%
Bank of Tennessee	52,150	8.03%	25,983	4.00%

BANCTENN CORP. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 24. Contingencies

During the normal course of business, the Company is subject to various lawsuits and claims. As of December 31, 2010, management believes that there are no current proceedings that would materially impact the consolidated financials of the Company.

Note 25. Concentrations in Deposits

The Company had a concentration in its deposits of one customer totaling approximately \$34,065,000 at December 31, 2010. There were no concentrations at December 31, 2009.

Report of Independent Certified Public Accountants
on Accompanying Information

To the Stockholders and
Board of Directors
BancTenn Corp.
Kingsport, Tennessee

Our report on our audits of the basic consolidated financial statements of BancTenn Corp. and subsidiary for 2010 and 2009 appears on page 1. Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The consolidating information on pages 40 and 41 is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position and results of operations of the individual companies. The consolidating information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.

Hazlett, Lewis & Bieter, PLLC

Chattanooga, Tennessee
April 5, 2011

BANCTENN CORP. AND SUBSIDIARY
CONSOLIDATING BALANCE SHEET
December 31, 2010

	Bank of Tennessee	BancTenn Corp.	Eliminations	Consolidated
ASSETS				
Cash and due from banks:				
Noninterest-bearing	\$ 8,737,143	\$ 92,562	\$ 92,562	\$ 8,737,143
Interest-bearing	<u>21,526,431</u>	<u>-</u>	<u>-</u>	<u>21,526,431</u>
Total cash and due from banks	30,263,574	92,562	92,562	30,263,574
Certificates of deposit with other financial institutions	248,000	-	-	248,000
Securities available for sale	76,200,756	106,985	-	76,307,741
Investment in Paragon Commercial Corporation	-	10,438,500	-	10,438,500
Investment in Appalachian Fund for Growth II	3,227,705	-	-	3,227,705
Restricted investments, at cost	2,426,700	-	-	2,426,700
Federal funds sold	340,000	-	-	340,000
Loans, net of allowance for loan losses	464,155,234	-	-	464,155,234
Premises and equipment	27,724,134	383,170	-	28,107,304
Accrued interest receivable	1,738,617	-	-	1,738,617
Cash surrender value of life insurance	14,070,635	-	-	14,070,635
Foreclosed real estate	7,273,649	-	-	7,273,649
Other assets	5,427,326	2,432,761	1,421,130	6,438,957
Investment in subsidiary	<u>-</u>	<u>53,626,261</u>	<u>53,626,261</u>	<u>-</u>
Total assets	<u>\$ 633,096,330</u>	<u>\$ 67,080,239</u>	<u>\$ 55,139,953</u>	<u>\$ 645,036,616</u>
LIABILITIES AND STOCKHOLDERS' EQUITY				
Deposits:				
Noninterest-bearing	\$ 124,545,266	\$ -	\$ 92,562	\$ 124,452,704
Interest-bearing	<u>397,055,033</u>	<u>-</u>	<u>-</u>	<u>397,055,033</u>
Total deposits	521,600,299	-	92,562	521,507,737
Securities sold under agreements to repurchase	16,090,232	-	-	16,090,232
Federal funds purchased	1,535,658	-	-	1,535,658
Federal Home Loan Bank advances	35,817,782	-	-	35,817,782
Subordinated debentures	-	15,465,000	-	15,465,000
Borrowings under line of credit	-	810,989	650,989	160,000
Accrued interest payable	234,133	85,341	-	319,474
Accrued expenses and other liabilities	<u>4,191,965</u>	<u>1,181,418</u>	<u>758,141</u>	<u>4,615,242</u>
Total liabilities	<u>579,470,069</u>	<u>17,542,748</u>	<u>1,501,692</u>	<u>595,511,125</u>
Stockholders' equity:				
Common stock, no par value; 250,000 shares authorized; 209,148 shares outstanding	1,673,184	-	1,673,184	-
Common stock, \$8 par value; 6,000,000 shares authorized; 1,582,400 shares outstanding	-	12,659,200	-	12,659,200
Additional paid-in capital	14,877,811	11,871,981	14,877,811	11,871,981
Retained earnings	37,218,990	26,599,655	37,230,990	26,587,655
Accumulated other comprehensive income	(143,724)	(942,356)	(143,724)	(942,356)
Unallocated ESOP shares	<u>-</u>	<u>(650,989)</u>	<u>-</u>	<u>(650,989)</u>
Total stockholders' equity	<u>53,626,261</u>	<u>49,537,491</u>	<u>53,638,261</u>	<u>49,525,491</u>
Total liabilities and stockholders' equity	<u>\$ 633,096,330</u>	<u>\$ 67,080,239</u>	<u>\$ 55,139,953</u>	<u>\$ 645,036,616</u>

BANCTENN CORP. AND SUBSIDIARY
CONSOLIDATING STATEMENT OF INCOME
Year Ended December 31, 2010

	Bank of Tennessee	BancTenn Corp.	Eliminations	Consolidated
INTEREST INCOME				
Loans, including fees	\$ 25,903,618	\$ -	\$ -	\$ 25,903,618
Securities	3,275,384	-	-	3,275,384
Federal funds sold	17,891	-	-	17,891
	<u>29,196,893</u>	<u>-</u>	<u>-</u>	<u>29,196,893</u>
INTEREST EXPENSE				
	<u>6,607,075</u>	<u>836,085</u>	<u>-</u>	<u>7,443,160</u>
Net interest income (expense)	22,589,818	(836,085)	-	21,753,733
Provision for loan losses	<u>5,136,337</u>	<u>-</u>	<u>-</u>	<u>5,136,337</u>
Net interest income (expense) after provision for loan losses	<u>17,453,481</u>	<u>(836,085)</u>	<u>-</u>	<u>16,617,396</u>
NONINTEREST INCOME				
Customer service fees	1,784,205	-	-	1,784,205
Service revenue	3,460,503	-	-	3,460,503
Other	3,043,299	-	12,000	3,031,299
Equity in subsidiary's earnings	<u>-</u>	<u>5,800,424</u>	<u>5,800,424</u>	<u>-</u>
	<u>8,288,007</u>	<u>5,800,424</u>	<u>5,812,424</u>	<u>8,276,007</u>
NONINTEREST EXPENSES				
Salaries and employee benefits	10,777,788	658,637	-	11,436,425
Occupancy expenses	1,425,206	-	-	1,425,206
Other operating expenses	7,393,608	552,491	-	7,946,099
Loss on other assets	<u>-</u>	<u>3,504,352</u>	<u>-</u>	<u>3,504,352</u>
	<u>19,596,602</u>	<u>4,715,480</u>	<u>-</u>	<u>24,312,082</u>
Income before income taxes	6,144,886	248,859	5,812,424	581,321
Income taxes	<u>344,462</u>	<u>(277,814)</u>	<u>-</u>	<u>66,648</u>
Net income	<u>\$ 5,800,424</u>	<u>\$ 526,673</u>	<u>\$ 5,812,424</u>	<u>\$ 514,673</u>