

FEDERAL DEPOSIT INSURANCE CORPORATION
Washington, D.C. 20429

FORM 10-K

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2010

FDIC Certificate No. 58248

PATRIOT STATE BANK

(Exact Name of Registrant as specified in its charter)

NORTH CAROLINA

(State of Incorporation)

20-5380738

(I.R.S. Employer Identification No.)

210 North Main Street, Fuquay-Varina, North Carolina 27526

(Address of Principal Office)

(919) 577-2265

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

NONE

Securities registered pursuant to Section 12(g) of the Act:

COMMON STOCK, \$5.00 PAR VALUE

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant as of the last business day of the registrant's most recently completed second fiscal quarter (June 30, 2010) was \$14,120,000.

The number of shares of the Registrant's Common Stock outstanding on March 17, 2011 was 1,765,000.

Documents Incorporated by Reference:

Portions of the registrant's definitive proxy statement as filed with the Federal Deposit Insurance Corporation in connection with its 2011 annual meeting are incorporated into Part III of this report.

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PART I

[In this Report, the terms “Registrant,” “Bank,” “we,” “us,” “our” and similar terms refer to Patriot State Bank.]

ITEM 1 – BUSINESS

General

Patriot State Bank (herein “Registrant” or “Bank”) was incorporated on August 15, 2006, as a North Carolina-chartered commercial bank. The Registrant opened for business on August 21, 2006 at 210 North Main Street, Fuquay-Varina, North Carolina. The Registrant operates for the primary purpose of serving the banking needs of individuals and small- to medium-sized businesses in its market area. The Registrant offers a range of banking services including checking and savings accounts, commercial, consumer and personal loans and other associated services.

Market Area

The Bank's market area consists of the towns of Fuquay-Varina, Clayton, and Clinton, located in Wake, Johnston, and Sampson counties respectively. The Bank also has a loan production office in Cary, North Carolina (located in Wake County) and has plans to convert the Cary office to a full service branch. The Bank also considers Holly Springs and the surrounding areas of Wake and Harnett Counties, North Carolina, as parts of its target market area.

Fuquay-Varina, Cary, and Holly Springs had estimated 2009 populations of 17,905, 136,600 and 21,743, respectively, and Wake County had a 2009 estimated population of 897,214. In 2009, the U.S. Census Bureau ranked Wake County seventh in the nation in terms of population inflow. For the foreseeable future, population growth rate projections suggest Wake County's growth rate and those of Fuquay-Varina, Cary and Holly Springs will continue to outpace that of North Carolina and the nation. Clinton had estimated 2009 population of 8,736 and Clayton had estimated 2009 population of 16,362. Sampson and Johnston Counties had estimated 2009 populations of 63,713 and 168,525, respectively.

The unemployment rate in Wake County, approximately 7.5% in December 2010, fared better than the state and national rates, at 9.6% and 9.4%, respectively. Unemployment rates in Sampson and Johnston Counties were at 7.6% and 8.9% respectively.

As of June 2010, bank deposits in Wake County totaled \$18.5 billion and totaled \$484 million, \$2.19 billion and \$89 million in Fuquay-Varina, Cary, and Holly Springs, respectively. At the same date, bank deposits in Sampson County equaled \$476 million and Clinton's deposits equaled \$332 million. Clayton's deposits as of June 2010 equaled \$300 million and Johnston County's equaled \$1.69 billion.

Competition

Registrant competes for deposits in its banking market with other commercial banks, savings banks and other thrift institutions, credit unions, agencies issuing United States government securities and all other organizations and institutions engaged in money market transactions. In its lending activities, Registrant competes with all other financial institutions as well as consumer finance companies, mortgage companies and other lenders. Commercial banking in our market area and in North Carolina as a whole is extremely competitive. As of June 30, 2010, the most recent data provided by the FDIC Deposit Market Share Report indicated that there were 256 offices of 30 other commercial banks operating in Wake County, 42 offices of 12 other commercial banks operating in Johnston County, and 15 offices of 7 other commercial banks operating in Sampson County.

Interest rates, both on loans and deposits, and prices of fee-based services, are significant competitive factors among financial institutions generally. Other important competitive factors include office location, office hours, the quality of customer service, community reputation, continuity of personnel and services, and, in the case of larger commercial customers, relative lending limits and the ability to offer sophisticated cash management and other commercial banking services. Many of Registrant's competitors have greater resources, broader geographic markets and higher lending limits than Registrant, and they can offer more products and services and can better afford and make more effective use of media advertising, support services and electronic technology than can Registrant.

In recent years, federal and state legislation has heightened the competitive environment in which all financial institutions conduct their business, and the potential for competition among financial institutions of all types has increased significantly. Additionally, with the elimination of restrictions on interstate banking, a North Carolina commercial bank may be required to compete not only with other North Carolina-based financial institutions, but also with out-of-state financial institutions which may acquire North Carolina institutions, establish or acquire branch offices in North Carolina, or otherwise offer financial services across state lines, thereby adding to the competitive atmosphere of the industry in general. In terms of assets, Registrant is one of the smaller commercial banks in North Carolina.

To counter its competitive disadvantages, Registrant attempts to differentiate itself from its larger competitors with its focus on relationship banking, personalized service, direct customer contact, and its ability to make credit and other business decisions locally. Registrant also depends on its reputation as a community bank in its banking markets and its involvement in the communities it serves.

Employees

The Registrant currently employs twenty-five full-time and seven part-time employees. None of the Registrant's employees are covered by a collective bargaining agreement. The Registrant believes its relations with its employees to be good.

Regulation

The Registrant is extensively regulated under both federal and state law. Generally, these laws and regulations are intended to protect depositors and borrowers, not shareholders. To the extent that the following information describes statutory and regulatory provisions, it is qualified in its entirety by reference to the particular statutory and regulatory provisions. Any change in applicable law or regulation may have a material effect on the business of the Registrant.

State Law. The Registrant is subject to extensive supervision and regulation by the North Carolina Commissioner of Banks (the "Commissioner"). The Commissioner oversees state laws that set specific requirements for bank capital and regulate deposits in, and loans and investments by, banks, including the amounts, types, and in some cases, rates. The Commissioner supervises and performs periodic examinations of North Carolina-chartered banks to assure compliance with state banking statutes and regulations, and the Registrant is required to make regular reports to the Commissioner describing in detail the resources, assets, liabilities and financial condition of the Registrant. Among other things, the Commissioner regulates mergers and consolidations of state-chartered banks, the payment of dividends, loans to officers and directors, record keeping, types and amounts of loans and investments, and the establishment of branches.

Dodd-Frank Wall Street Reform and Consumer Protection Act. On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act") was signed into law. The Dodd-Frank Act represents a comprehensive overhaul of the financial services industry in the United States. The Dodd-Frank Act includes, among other things:

- the creation of a Financial Stability Oversight Council to identify emerging systemic risks posed by financial firms, activities and practices, and to improve cooperation between federal agencies;
- the creation of a Bureau of Consumer Financial Protection authorized to promulgate and enforce consumer protection regulations relating to financial products, which would affect both banks and non-bank financial companies;
- the establishment of strengthened capital and prudential standards for banks and bank holding companies;
- enhanced regulation of financial markets, including derivatives and securitization markets;
- the elimination of certain trading activities by banks;
- a permanent increase of the previously implemented temporary increase of FDIC deposit insurance to \$250,000 per account, an extension of unlimited deposit insurance on qualifying noninterest-bearing transaction accounts, and an increase in the minimum deposit insurance fund reserve requirement from 1.15% to 1.35%, with assessments to be based on assets as opposed to deposits;
- amendments to the Truth in Lending Act aimed at improving consumer protections with respect to mortgage originations, including originator compensation, minimum repayment standards, and prepayment considerations; and
- new disclosure and other requirements relating to executive compensation and corporate governance.

Although the Dodd-Frank Act has been signed into law, a number of provisions remain to be implemented through the rulemaking process at various regulatory agencies. We are unable to predict the extent to which the Dodd-Frank Act or the forthcoming rules and regulations will impact our business. However, we believe that certain aspects of the new legislation, including, without limitation, the additional cost of higher deposit insurance coverage and the costs of compliance with disclosure and reporting requirements and examinations could have a significant impact on our business, financial condition, and results of operations. Additionally, we cannot predict whether there will be additional proposed laws or reforms that would affect the U.S. financial system or financial institutions, whether or when such changes may be adopted, how such changes may be interpreted and enforced, or how such changes may affect us.

Deposit Insurance. The Bank's deposits are insured up to limits set by the Deposit Insurance Fund (the "DIF") of the FDIC. The DIF was formed on March 31, 2006, upon the merger of the Bank Insurance Fund and the Savings Insurance Fund in accordance with the Federal Deposit Insurance Reform Act of 2005 (the "Reform Act"). The Reform Act established a range of 1.15% to 1.50% within which the FDIC may set the Designated Reserve Ratio (the "reserve ratio" or "DRR"). The Dodd-Frank Act gave the FDIC greater discretion to manage the DIF, raised the minimum DIF reserve ratio to 1.35%, and removed the upper limit of 1.50%. In October 2010, the FDIC adopted a restoration plan to ensure that the DIF reserve ratio reaches 1.35% by September 30, 2020, as required by the Dodd-Frank Act. The FDIC also proposed a comprehensive, long-range plan for management of the DIF. As part of this comprehensive plan, the FDIC has adopted a final rule to set the DRR at 2.0%.

On October 3, 2008, the Emergency Economic Stabilization Act of 2008 was enacted and temporarily raised the standard limit of FDIC insurance coverage from \$100,000 to \$250,000 per depositor. On May 20, 2009, the Helping Families Save Their Homes Act extended the temporary increase in the standard maximum deposit insurance amount (SMDIA) to per depositor through December 31, 2013. On July 21, 2010, the Dodd-Frank Act permanently increased FDIC insurance coverage to \$250,000 per depositor.

The FDIC imposes a risk-based deposit insurance premium assessment on member institutions in order to maintain the DIF. This assessment system was amended by the Reform Act and further amended by the Dodd-Frank Act. Under this system, as amended, the assessment rates for an insured depository institution vary according to the level of risk incurred in its activities. To arrive at an assessment rate for a banking institution, the FDIC places it in one of four risk categories determined by reference to its capital levels and supervisory ratings. In addition, in the case of those institutions in the lowest risk category, the FDIC further determines its assessment rate based on certain specified financial ratios or, if applicable, its long-term debt ratings. The assessment rate schedule can change from time to time, at the discretion of the FDIC, subject to certain limits. The Dodd-Frank Act changed the methodology for calculating deposit insurance assessments from the amount of an insured institution's domestic deposits to its total assets minus tangible capital. On February 7, 2011, the FDIC issued a new regulation implementing these revisions to the assessment system. The regulation will be effective April 1, 2011.

On October 14, 2008, the FDIC announced the Temporary Liquidity Guarantee Program (the "TLGP") to strengthen confidence and encourage liquidity in the banking system. The TLGP consists of two components: a temporary guarantee of newly-issued senior unsecured debt named the Debt Guarantee Program, and a temporary unlimited guarantee of funds in noninterest-bearing transaction accounts at FDIC insured institutions named the Transaction Account Guarantee Program ("TAG"). All newly-issued senior unsecured debt will be charged an annual assessment of up to 100 basis points (depending on term) multiplied by the amount of debt issued and calculated through the date of that debt or June 30, 2012, whichever is earlier. The Bank elected to opt out of the Debt Guarantee Program and elected to participate in the TAG Program. On August 26, 2009, the FDIC adopted a final rule extending the TAG portion of the TLGP for six months through June 30, 2010 and it was extended again through December 31, 2010. The Bank elected to continue to participate in the TAG Program through December 31, 2010. On July 21, 2010, the Dodd-Frank Act extended unlimited FDIC insurance coverage to noninterest-bearing transaction deposit accounts. It does not apply to accounts earning any level of interest with the exception of Interest on Lawyers' Trust Accounts ("IOLTA") accounts. This unlimited FDIC insurance coverage is applicable to all applicable deposits at any FDIC-insured financial institution. Therefore, there is no additional FDIC insurance surcharge related to this coverage after December 31, 2010.

During 2009, the FDIC took several measures aimed at replenishing the DIF. On May 22, 2009, the FDIC imposed a 5 basis point special assessment on each insured institution's assets minus Tier 1 capital as of June 30, 2009. On November 17, 2009, the FDIC voted to require insured institutions to prepay their estimated quarterly risk-based assessments for the fourth quarter of 2009, as well as all of 2010, 2011, and 2012. For purposes of determining the prepayment, the FDIC used an institution's assessment rate in effect on September 30, 2009.

The FDIC has authority to increase insurance assessments. A significant increase in insurance premiums would likely have an adverse effect on the operating expenses and results of operations of the Bank. Management cannot predict what insurance assessment rates will be in the future.

Insurance of deposits may be terminated by the FDIC upon a finding that an insured institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC.

Capital Requirements. The federal banking regulators have adopted certain risk-based capital guidelines to assist in the assessment of the capital adequacy of a banking organization's operations for both transactions reported on the balance sheet as assets and transactions, such as letters of credit, and recourse arrangements, which are recorded as off balance sheet items. Under these guidelines, nominal dollar amounts of assets and credit equivalent amounts of off balance sheet items are multiplied by one of several risk adjustment percentages which range from 0% for assets with low credit risk, such as certain U.S. Treasury securities, to 100% for assets with relatively high credit risk, such as business loans.

A banking organization's risk-based capital ratios are obtained by dividing its qualifying capital by its total risk-adjusted assets. The regulators measure risk-adjusted assets, which include off balance sheet items, against both total qualifying capital (the sum of Tier 1 capital and limited amounts of Tier 2 capital) and Tier 1 capital. "Tier 1," or core capital, includes common equity, qualifying noncumulative perpetual preferred stock and minority interests in equity accounts of consolidated subsidiaries, less goodwill and other intangibles, subject to certain exceptions. "Tier 2," or supplementary capital, includes among other things, limited-life preferred stock, hybrid capital instruments, mandatory convertible securities, qualifying subordinated debt, and the allowance for loan and lease losses, subject to certain limitations and less required deductions. The inclusion of elements of Tier 2 capital is subject to certain other requirements and limitations of the federal banking agencies. Banks and bank holding companies subject to the risk-based capital guidelines are required to maintain a ratio of Tier 1 capital to risk-weighted assets of at least 4% and a ratio of total capital to risk-weighted assets of at least 8%. The appropriate regulatory authority may set higher capital requirements when particular circumstances warrant. As of December 31, 2010, the Registrant was classified as "well-capitalized" with Tier 1 and Total Risk - Based Capital of 14.87 % and 16.12% respectively.

The federal banking agencies have adopted regulations specifying that they will include, in their evaluations of a bank's capital adequacy, an assessment of a bank's interest rate risk ("IRR") exposure. The standards for measuring the adequacy and effectiveness of a banking organization's IRR management include a measurement of board of directors and senior management oversight, and a determination of whether a banking organization's procedures for comprehensive risk management are appropriate for the circumstances of the specific banking organization.

Failure to meet applicable capital guidelines could subject a banking organization to a variety of enforcement actions, including limitations on its ability to pay dividends, the issuance by the applicable regulatory authority of a capital directive to increase capital and, in the case of depository institutions, the termination of deposit insurance by the FDIC, as well as the measures described under the "Federal Deposit Insurance Corporation Improvement Act of 1991" below, as applicable to undercapitalized institutions. In addition, future changes in regulations or practices could further reduce the amount of capital recognized for purposes of capital adequacy. Such a change could affect the ability of the Registrant to grow and could restrict the amount of profits, if any, available for the payment of dividends to the shareholders.

Federal Deposit Insurance Corporation Improvement Act of 1991. In December 1991, Congress enacted the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA"), which substantially revised the bank regulatory and funding provisions of the Federal Deposit Insurance Act ("FDIA") and made significant revisions to several other federal banking statutes. FDICIA provides for, among other things:

- publicly available annual financial condition and management reports for certain financial institutions, including audits by independent accountants,
- the establishment of uniform accounting standards by federal banking agencies,
- the establishment of a "prompt corrective action" system of regulatory supervision and intervention, based on capitalization levels, with greater scrutiny and restrictions placed on depository institutions with lower levels of capital,
- additional grounds for the appointment of a conservator or receiver,

- restrictions or prohibitions on accepting brokered deposits, except for institutions which significantly exceed minimum capital requirements, and
- increased funding of the FDIC insurance funds and the implementation of risk-based premiums.

A central feature of FDICIA is the requirement that the federal banking agencies take "prompt corrective action" with respect to depository institutions that do not meet minimum capital requirements. Pursuant to FDICIA, the federal bank regulatory authorities have adopted regulations setting forth a five-tiered system for measuring the capital adequacy of the depository institutions that they supervise. Under these regulations, a depository institution is classified in one of the following capital categories: "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized." An institution may be deemed by the regulators to be in a capitalization category that is lower than is indicated by its actual capital position if, among other things, it receives an unsatisfactory examination rating with respect to asset quality, management, earnings or liquidity.

FDICIA provides the federal banking agencies with significantly expanded powers to take enforcement action against institutions which fail to comply with capital or other standards. Such action may include the termination of deposit insurance by the FDIC or the appointment of a receiver or conservator for the institution. FDICIA also limits the circumstances under which the FDIC is permitted to provide financial assistance to an insured institution before appointment of a conservator or receiver.

International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001. On October 26, 2001, the USA Patriot Act of 2001 was enacted. This Act contains the International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001, which sets forth anti-money laundering measures affecting insured depository institutions, broker-dealers and other financial institutions. The Act requires U.S. financial institutions to adopt new policies and procedures to combat money laundering and grants the Secretary of the Treasury broad authority to establish regulations and to impose requirements and restrictions on the operations of financial institutions. The Act has not had a material impact on our operations.

Community Reinvestment Act. The Registrant is subject to the provisions of the Community Reinvestment Act of 1977, as amended (CRA). Under the terms of the CRA, the appropriate federal bank regulatory agency is required, in connection with the examination of a bank, to assess such bank's record in meeting the credit needs of the community served by that bank, including low- and moderate-income neighborhoods. The regulatory agency's assessment of the Registrant's record is made available to the public. Such an assessment is required of any bank which has made application for a domestic deposit-taking branch, relocation of a main office, branch or ATM, merger or consolidation with or acquisition of assets or assumption of liabilities of a federally insured depository institution.

Under CRA regulations, banks with assets of less than \$250,000,000 that are independent, such as the Registrant, or affiliated with a holding company with total banking assets of less than \$1 billion, are subject to streamlined small bank performance standards and much less stringent data collection and reporting requirements than larger banks. The agencies emphasize that small banks are not exempt from CRA requirements. The streamlined performance method for small banks focuses on the bank's loan-to-deposit ratio, adjusted for seasonal variations and as appropriate, other lending-related activities, such as loan originations for sale to secondary markets or community development lending or qualified investments; the percentage of loans and, as appropriate, other lending-related activities located in the Registrant's assessment areas; the Registrant's record of lending to and, as appropriate, other lending-related activities for borrowers of different income levels and businesses and farms of different sizes; the geographic distribution of the Registrant's loans given its assessment areas, capacity to lend, local economic conditions, and lending opportunities; and the Registrant's record of taking action, if warranted, in response to written complaints about its performance in meeting the credit needs of its assessment areas.

Regulatory agencies will assign a composite rating of "outstanding," "satisfactory," "needs to improve," or "substantial noncompliance" to the institution using the foregoing ground rules. A bank's performance need not fit each aspect of a particular rating profile in order for the bank to receive that rating; exceptionally strong performance with respect to some aspects may compensate for weak performance in others, and the bank's overall performance must be consistent with safe and sound banking practices and generally with the appropriate rating profile. To earn an outstanding rating, the bank first must exceed some or all of the standards mentioned above. The agencies may assign a "needs to improve" or "substantial noncompliance" rating depending on the degree to which the bank has failed to meet the standards mentioned above.

The regulation further states that the agencies will take into consideration these CRA ratings when considering any application and that a bank's record of performance may be the basis for denying or conditioning the approval of an

application. Patriot State Bank was examined by the Federal Deposit Insurance Corporation under the small bank CRA examination procedures as of September 8, 2008 and received a “Satisfactory” rating.

Small Business Lending Fund. In September 2010, the Small Business Lending Fund Program (“SBLF”) was created by the Small Business Jobs Act of 2010. Under the SBLF, the U.S. Treasury may invest in preferred stock and other debt instruments issued by financial institutions. To be eligible, an institution must have total assets of \$10 billion or less. An institution between \$1 billion and \$10 billion may apply for up to 3% of its total risk-weighted assets as long as it is otherwise eligible. An institution with assets of \$1 billion or less may apply for up to 5% of its total risk-weighted assets as long as it is otherwise eligible. The U.S. Treasury must consult with the institution’s regulators to determine if the institution should receive the investment. Institutions on the FDIC’s problem bank list as of, or within 90 days prior to, the date of the application, are ineligible to participate in the program.

Treasury’s investment must be repaid within 10 years. While the investment is outstanding, the rate at which dividends are payable varies between 1% and 7%, with an initial rate of 5%, and is wholly dependent upon the amount of increase in the bank’s quarterly small business lending following Treasury’s capital investment. If the amount of small business lending does not increase within 2 years, the dividend rate increases to 7%. If Treasury’s investment is not redeemed on or before 4¹/₂ years following its investment, the dividend rate increases to 9%.

The application for participation in the SBLF along with a business plan for increasing small business lending must be submitted to the Treasury and the institution’s primary federal regulator prior to March 31, 2011. The Bank intends to submit an application for participation in the SBLF. If the application is accepted, there is uncertainty as to whether the Bank will be able to increase the level of small business lending in order to qualify for a reduced level of dividend payments. There is also uncertainty as to the capital treatment of any funds received under the SBLF due to conflicts in capital treatment under the Dodd-Frank Act and the proposed Basel III rules. Further, Treasury could change the rules regarding participation in the SBLF at any time.

Incentive Compensation Policies and Restrictions. In July 2010, the federal banking agencies issued guidance which applies to all banking organizations supervised by the agencies. Pursuant to the guidance, to be consistent with safety and soundness principles, a banking organization’s incentive compensation arrangements should: (1) provide employees with incentives that appropriately balance risk and reward; (2) be compatible with effective controls and risk management; and (3) be supported by strong corporate governance including active and effective oversight by the banking organization’s board of directors. Monitoring methods and processes used by a banking organization should be commensurate with the size and complexity of the organization and its use of incentive compensation.

Miscellaneous. The dividends that may be paid by the Registrant are subject to legal limitations. In accordance with North Carolina banking law, dividends may not be paid unless the Registrant’s capital surplus is at least 50% of its paid-in capital.

Shareholders of banks may be compelled by the Commissioner pursuant to North Carolina law to invest additional capital in the event their bank’s capital shall have become impaired by losses or otherwise. Failure to pay such an assessment could result in a forced sale of a shareholder’s bank stock.

The earnings of the Registrant will be affected significantly by the policies of the Federal Reserve Board, which is responsible for regulating the United States money supply in order to mitigate recessionary and inflationary pressures. Among the techniques used to implement these objectives are open market transactions in United States government securities, changes in the rate paid by banks on bank borrowings, and changes in reserve requirements against bank deposits. These techniques are used in varying combinations to influence overall growth and distribution of bank loans, investments, and deposits, and their use may also affect interest rates charged on loans or paid for deposits.

The monetary policies of the Federal Reserve Board have had a significant effect on the operating results of commercial banks in the past and are expected to continue to do so in the future. In view of changing conditions in the national economy and money markets, as well as the effect of actions by monetary and fiscal authorities, no prediction can be made as to possible future changes in interest rates, deposit levels, loan demand or the business and earnings of the Registrant.

The Registrant cannot predict what legislation might be enacted or what regulations might be adopted, or if enacted or adopted, the effect thereof on the Registrant’s operations.

ITEM 1A – RISK FACTORS

Smaller reporting companies such as the Registrant are not required to provide the information required by this item.

ITEM 1B – UNRESOLVED STAFF COMMENTS

Smaller reporting companies such as the Registrant are not required to provide the information required by this item.

ITEM 2 – PROPERTIES

The following table sets forth the location of the Registrant’s offices as well as certain information relating to these offices to date:

<u>Office Location</u>	<u>Year Opened</u>	<u>Approximate Square Footage</u>	<u>Owned or Leased</u>
Main Office 210 N. Main St. Fuquay-Varina, NC 27526	2006	6,000	Owned
Clayton 490 Hwy 42 West Professional Park Clayton, NC 27250	2007	900	Leased
Clinton 1008 Sunset Avenue Clinton, NC 28328	2010	4,610	Owned
Cary Loan Production Office 51 Kilmayne Drive, Suite 303 Cary, NC 27511	2008	2,279	Leased

ITEM 3 – LEGAL PROCEEDINGS

From time to time as part of our business, we are subject to routine litigation. To the best of our knowledge, there is no pending material litigation to which we are subject.

ITEM 4 – RESERVED

PART II

ITEM 5 – MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Bank's common stock is traded on the over-the-counter bulletin board under the symbol PTOK.OB.

The following table lists the high and low sales information for our common stock for the periods indicated. Prices in the table reflect inter-dealer prices, without retail mark-up, mark-down, or commission, and may not represent actual transactions. Through March 17, 2011, the last sale of our common stock quoted on the over-the-counter bulletin board on The Pink Sheets, LLC was at a price of \$6.50 per share. As of March 17, 2011, there were 623 record holders of the Bank's common stock.

	<u>High</u>	<u>Low</u>
2010		
First quarter	\$ 8.75	\$ 3.76
Second quarter	8.50	6.75
Third quarter	8.00	5.38
Fourth quarter	7.95	5.75
2009		
First quarter	\$ 10.50	\$ 6.00
Second quarter	10.50	10.50
Third quarter	10.50	3.80
Fourth quarter	9.00	5.00

As a state-chartered bank subject to North Carolina banking law, the Registrant may not pay cash dividends unless the Registrant's capital surplus is at least 50% of its paid-in capital.

See Item 12 of this report for disclosure regarding securities authorized for issuance under equity compensation plans.

ITEM 6 – SELECTED FINANCIAL DATA

Smaller reporting companies such as the Registrant are not required to provide the information required by this item.

ITEM 7 – MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

Management’s discussion and analysis is intended to assist readers in the understanding and evaluation of the financial condition and results of operations of the Bank. All statements in the following discussion and in this Report and its exhibits relating to projections of results of specific activities or investments, our expectations or beliefs about future events or results, our plans, strategies, economic performance and trends, and other statements that are not descriptions of historical facts, may be forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements may be identified by terms such as “may,” “will,” “should,” “could,” “likely,” “expects,” “plans,” “intends,” “anticipates,” “believes,” “estimates,” “predicts,” “forecasts,” “potential,” “continue,” or similar terms or the negative of these terms, or other statements concerning our management’s opinions or judgments about future events. Forward-looking information is inherently subject to risks and uncertainties, and our actual results could differ materially from those we currently anticipate due to a number of factors. Factors that could influence the accuracy of forward-looking statements include, but are not limited to: changes in market interest rates, changes in general economic conditions and real estate values in our banking market (particularly changes that affect our loan portfolio, the abilities of our borrowers to repay their loans, and the values of loan collateral), the financial success or changing strategies of our customers, actions of government regulators, our ability to compete successfully with the larger banks in our market, and other factors discussed in documents we file with the Federal Deposit Insurance Corporation from time to time. Although we believe the expectations reflected in forward-looking statements are reasonable, we cannot guarantee future results, performance or achievements. All forward-looking statements are expressly qualified in their entirety by the cautionary statements in this paragraph. We have no obligation, and do not intend, to update these forward-looking statements.

FINANCIAL CONDITION AT December 31, 2010 and December 31, 2009

During 2010, Patriot State Bank limited asset growth in order to maintain capital and ensure adequate liquidity. The Bank’s total assets increased slightly to \$139.1 million, an increase of \$1.7 million or 1% from total assets at December 31, 2009 of \$137.4 million. Net loans actually decreased \$2.4 million or 2% from \$107.1 million at December 31, 2009 to \$104.7 million at December 31, 2010. Patriot State Bank completed our new “state of the art” branch facility, which opened in Clinton, N.C. in June of 2010. The completion of this new branch building resulted in an increase of \$1.4 million in fixed assets to \$3.8 million at December 31, 2010 up from \$2.4 million at December 31, 2009.

Liquid investments, consisting of cash and due from banks, interest-bearing deposits in banks and investment securities available for sale totaled \$27.9 million, or 20% of total assets and 23% of total deposits, at December 31, 2010, as compared to \$24.8 million at December 31, 2009. Total stockholders’ equity increased from \$15.8 million at December 31, 2009 to \$16.0 million at December 31, 2010 primarily as a result of the net income of \$359,064 for the year ended December 31, 2010. At December 31, 2010, the Bank’s capital ratios exceeded the levels that are deemed to be “well-capitalized” under applicable regulatory capital requirements.

RESULTS OF OPERATIONS

The following discussion relates to operations for the year ended December 31, 2010 compared to the year ended December 31, 2009.

Overview. In 2010 the Bank had a net income of \$359,064 or \$0.20 income per diluted share compared to a net loss of \$1,950,677 or \$1.11 loss per diluted share, in 2009. The components of net income are discussed in detail below.

Net Interest Income. Net interest income for 2010 increased by \$761,816, or 22%, to \$4,253,359 from \$3,491,543 in 2009. Interest income in 2010 was \$6,327,012 up \$545,507 or 9% from \$5,781,505 in 2009. The yield on interest earning assets for 2010 was 4.75%, down from 4.99% in 2009. Interest expense for 2010 decreased by \$216,309 or 9% to \$2,073,653 compared to \$2,289,962 in 2009. The cost of interest bearing liabilities for 2010 was 1.88%, down from 2.45% in 2009. The decrease in cost of funds is due to rollover and maturity of higher interest rate certificates of deposits to the lower current interest rates. The Bank’s net interest margin was 3.19% in 2010 compared to 3.01% in 2009.

Provision for Loan Losses. Provision for loan losses decreased 87% to \$243,620 in 2010 compared to \$1,945,081 in 2009. During 2010 there were fourteen charge-offs totaling \$1,286,593 and no recoveries; in 2009 there were seven charge-offs totaling \$381,534 and one recovery of \$13,250. During 2010, the provision for loan losses was made in response to higher delinquency rates, the continuing local and national economic downturn, and specific reserves for nonperforming loans adjusted to reflect actual losses incurred. The Bank has \$5,448,728 in loans that are still performing in accordance with contractual terms, which management is monitoring the borrower's ability to comply with repayment terms. Provisions for loan losses are charged to income to bring the allowance for loan losses to a level deemed appropriate by management. In evaluating the allowance for loan losses, management considers factors that include an analysis of the risk characteristics of various classifications of loans, previous loan loss experience, specific loans which have loan loss potential, delinquency trends, estimated fair values of underlying collateral, current economic conditions, the views of the Bank's regulators (who have the authority to require additional reserves), and geographic and industry loan concentrations. The Bank determined that there are risk factors for the Bank that required adjustment for the historical losses, expected economic conditions that may affect the borrower's ability to repay and concentrations of credit in commercial real estate. The Bank has also determined that there are significant general factors requiring adjustment to the Bank's allowance calculation, trends in the level of nonperforming and classified loans, and depressed market values of collateral in the local market due to the weak economy.

Historically, the Bank has used peer loss history to determine the adequacy of the allowance. Beginning in 2010, the Bank has reviewed its actual loss history for the past twelve quarters. The Bank compared the three year average loss rate with the two year average loss rate and current year loss rates and determined that the best ratio to use for the average annual net loss ratio was the average of the most recent two years. This analysis was conducted on all relevant federal call report categories. The Bank determined there were several risk factors for the Bank that required adjustment for the historical losses. Management evaluates the historical loss rates, the economic factors that existed during the historical period used; and the future impact of current conditions relative to those historical rates.

The allowance for loan losses at December 31, 2010 and 2009 was \$1,701,617 and \$2,744,590 respectively, representing 1.60% of loans outstanding for 2010 and 2.50% in 2009. The Bank had twenty-nine impaired loans as of December 31, 2010 with a total amount of \$8,336,240 net of specific reserves. Specific reserves for these impaired loans were \$393,286 in 2010. The Bank had twenty-two impaired loans as of December 31, 2009 with a total amount of \$4,494,678 net of specific reserves. Specific reserves for these impaired loans were \$1,321,240 in 2009. See Note 5 on impaired loans.

Non-interest Income. For 2010, total non-interest income was \$242,889, up \$8,083 from \$234,806 in 2009. Service charges on deposit accounts, which represent a relatively stable and predictable source of non-interest income, totaled \$63,518 for 2010 compared to \$52,023 for 2009. The Bank has established associations with certain mortgage lending companies. The Bank originates a full range of competitively priced residential long-term mortgages, at both fixed and variable rates. These loans are originated in the mortgage lending company's name. The Bank earns fees for mortgage loans originated. The volume of mortgage loans closed in 2010 was down from 2009 resulting in fees earned during 2010 for mortgage loan originations of \$130,753 compared to \$151,126 during 2009.

Non-interest Expense. Total non-interest expenses totaled \$3,893,564 during 2010, up \$161,619 or 4%, from \$3,731,945 in 2009. Total personnel costs, the major component of non-interest expense, were \$2,169,893 in 2010, up \$18,564 or 1% from \$2,151,329 in 2009. Personnel costs include salaries and benefits and represent 56% of noninterest expense. Included in the personnel costs are employee stock option expenses which were \$62,769 in 2010 and \$146,400 in 2009. Directors' stock option expense was \$26,112 in 2010 and \$104,448 in 2009. The decrease in both employee and director's stock option expense is due to the majority of the options issued have been fully expensed. Occupancy expenses increased \$39,817 or 17% in 2010 to \$268,981 from \$229,164 in 2009. Furniture and equipment expenses totaled \$206,868 in 2010 up \$43,698 or 27% from \$163,170 in 2009. The increases in occupancy expenses and furniture and equipment expenses are a result of the opening of the new branch facility in Clinton, N.C. Data processing for 2010 was \$266,914, up \$18,206 or 7% from \$248,708 in 2009. Also included in non-interest expense is the FDIC deposit insurance assessment. The FDIC deposit insurance expense for 2010 was \$285,516, an increase of \$43,516 from \$242,000 in 2009. This increase is mainly due to the FDIC increasing the assessment rate.

Income Taxes. The Bank did not record any income tax expense during the year ended December 31, 2010. The Bank is in the early stage of its operation and did not generate taxable income during 2010. The tax benefit of \$1,481,963 is being fully reserved because of the lack of profitable operating history.

LIQUIDITY

Our liquidity is a measure of our ability to fund loans, withdrawals and maturities of deposits, and other cash outflows in a cost effective manner. Our principal sources of liquidity are deposits, scheduled payments and prepayments of loan principal, maturities of investment securities, access to liquid deposits, and funds provided by operations. While scheduled loan payments and maturing investments are relatively predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition.

Liquid assets, (consisting of cash and due from banks, interest-earning deposits with other banks, federal funds sold and investment securities classified as available for sale) comprised 20% of our total assets at December 31, 2010. As of December 31, 2010, there were no purchased federal funds. Should the need arise; we would have the capability to sell securities classified as available for sale or to borrow funds as necessary. We have established credit lines with other financial institutions to purchase up to \$13.2 million in federal funds. Management believes that our current sources of funds provide adequate liquidity for our current cash flow needs.

CAPITAL

A significant measure of the strength of a financial institution is its capital base. Our federal regulators have classified and defined capital into the following components: (1) Tier 1 capital, which includes common stockholders' equity and qualifying preferred equity, and (2) Tier 2 capital, which includes a portion of the allowance for loan losses, certain qualifying long-term debt and preferred stock which does not qualify as Tier 1 capital. Minimum capital levels are regulated by risk-based capital adequacy guidelines, which require a financial institution to maintain capital as a percent of its assets and certain off-balance sheet items adjusted for predefined credit risk factors (risk-adjusted assets). A financial institution is required to maintain, at a minimum, Tier 1 capital as a percentage of risk-adjusted assets of 4.0% and combined Tier 1 and Tier 2 capital as a percentage of risk-adjusted assets of 8.0%. In addition to the risk-based guidelines, federal regulations require that we maintain a minimum leverage ratio (Tier 1 capital as a percentage of tangible assets) of 4.0%. As of December 31, 2010, the Bank had a Tier 1 capital ratio of 14.87%, a total risk based capital ratio of 16.12% and a Tier 1 leverage ratio of 11.23%. All these ratios exceeded the regulatory capital levels above which an institution is considered to be "well capitalized." Management expects that the Bank will remain "well-capitalized" for regulatory purposes, although there can be no assurance that additional capital will not be required in the near future due to greater-than-expected growth, or otherwise.

ITEM 7A – QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Smaller reporting companies such as the Registrant are not required to provide the information required by this item.

ITEM 8 – FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
Patriot State Bank
Fuquay-Varina, North Carolina

We have audited the accompanying balance sheets of Patriot State Bank as of December 31, 2010 and 2009, and the related statements of operations, changes in stockholders' equity and cash flows for each of the two years in the period ended December 31, 2010. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Bank is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting 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 financial statements referred to above present fairly, in all material respects, the financial position of Patriot State Bank at December 31, 2010 and 2009, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2010, in conformity with U.S. generally accepted accounting principles.

Elliott Davis, PLLC

Galax, Virginia
March 28, 2011

Balance Sheets

December 31, 2010 and 2009

	<u>December 31, 2010</u>	<u>December 31, 2009</u>
ASSETS		
Cash and due from banks	\$ 1,813,842	\$ 1,397,677
Interest-bearing deposits in banks	9,898,214	8,634,547
Cash and cash equivalents	<u>11,712,056</u>	<u>10,032,224</u>
Investment securities, available for sale	16,223,090	14,750,044
Other investments	557,900	527,600
Loans	106,379,554	109,875,990
Allowance for loan losses	<u>(1,701,617)</u>	<u>(2,744,590)</u>
Net loans	<u>104,677,937</u>	<u>107,131,400</u>
Premises and equipment, net	3,800,046	2,398,241
Other real estate	1,010,000	915,000
Accrued interest receivable	542,638	631,208
Other assets	<u>617,721</u>	<u>988,328</u>
TOTAL ASSETS	<u>\$ 139,141,388</u>	<u>\$ 137,374,045</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Deposits		
Non-interest bearing deposits	\$ 14,044,719	\$ 10,537,417
NOW accounts	7,646,588	3,294,015
Savings and interest-checking	20,753,668	16,950,649
Individual retirement accounts	10,316,775	7,045,734
Certificates of deposit	<u>69,941,240</u>	<u>83,229,972</u>
Total deposits	122,702,990	121,057,787
Secured borrowings	250,000	250,000
Accrued interest payable	78,343	101,931
Other liabilities	<u>71,167</u>	<u>186,357</u>
TOTAL LIABILITIES	<u>123,102,500</u>	<u>121,596,075</u>
COMMITMENTS AND CONTINGENCIES (Note 13)	-	-
STOCKHOLDERS' EQUITY		
Preferred stock, 1,000,000 shares authorized; none issued	-	-
Common stock, \$5 par value, 10,000,000 shares authorized; 1,765,000 shares issued and outstanding	8,825,000	8,825,000
Surplus	11,342,473	11,253,592
Accumulated deficit	(4,213,040)	(4,572,104)
Accumulated other comprehensive income	<u>84,455</u>	<u>271,482</u>
TOTAL STOCKHOLDERS' EQUITY	<u>16,038,888</u>	<u>15,777,970</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$ 139,141,388</u>	<u>\$ 137,374,045</u>

See Notes to Financial Statements

Statements of Operations

For the years ended December 31, 2010 and 2009

	Twelve Months Ended December 31, 2010	Twelve Months Ended December 31, 2009
INTEREST INCOME		
Loans and fees on loans	\$ 5,645,483	\$ 5,025,404
Investments	646,682	718,075
Equity securities	1,282	4,296
Federal funds sold	-	1,461
Deposits in other banks	33,565	32,269
TOTAL INTEREST INCOME	6,327,012	5,781,505
INTEREST EXPENSE		
Money market, NOW and savings deposits	238,558	271,071
Time deposits	1,828,193	2,009,029
Borrowings	4,688	4,688
Federal funds purchased	2,214	5,174
TOTAL INTEREST EXPENSE	2,073,653	2,289,962
NET INTEREST INCOME	4,253,359	3,491,543
PROVISION FOR LOAN LOSSES	243,620	1,945,081
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	4,009,739	1,546,462
NON-INTEREST INCOME		
Service charges on deposit accounts	63,518	52,023
Mortgage fees	130,753	151,126
Other	48,618	31,657
TOTAL NON-INTEREST INCOME	242,889	234,806
NON-INTEREST EXPENSE		
Personnel expense	2,169,893	2,151,329
Occupancy expense	268,981	229,164
Furniture and equipment expense	206,868	163,170
Advertising and promotion	89,867	80,093
Data processing	266,914	248,708
Office supplies, printing and postage	81,595	59,156
Professional services	217,930	204,693
Director stock option expense	26,112	104,448
Loss on disposal of equipment	1,392	-
Other real estate expenses, net	57,462	28,446
Federal deposit insurance premiums	285,516	242,000
Other non-interest expense	221,034	220,738
TOTAL NON-INTEREST EXPENSE	3,893,564	3,731,945
NET INCOME (LOSS) BEFORE INCOME TAXES	359,064	(1,950,677)
INCOME TAX EXPENSE	-	-
NET INCOME (LOSS)	\$ 359,064	\$ (1,950,677)
Net income (loss) per weighted average common share, basic	\$ 0.20	\$ (1.11)
Net income (loss) per weighted average common share, diluted	\$ 0.20	\$ (1.11)
Weighted average common shares outstanding, basic	1,765,000	1,765,000

See Notes to Financial Statements

Statements of Changes in Stockholders' Equity and Comprehensive Income (Loss)

For the years ended December 31, 2010 and 2009

	Common Stock			Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total
	Shares	Amount	Surplus			
<i>Balance, December 31, 2008</i>	1,765,000	\$ 8,825,000	\$ 11,002,144	\$ (2,621,427)	\$ (245,131)	\$ 16,960,586
<i>Comprehensive income (loss)</i>						
Net loss	-	-	-	(1,950,677)	-	(1,950,677)
Unrealized appreciation on available for sale investment securities	-	-	-	-	516,613	516,613
<i>Total comprehensive loss</i>						(1,434,064)
Reimbursement from short sale			600			600
Stock compensation expense	-	-	250,848	-	-	250,848
<i>Balance, December 31, 2009</i>	1,765,000	8,825,000	11,253,592	(4,572,104)	271,482	15,777,970
<i>Comprehensive income (loss)</i>						
Net income	-	-	-	359,064	-	359,064
Unrealized depreciation on available for sale investment securities	-	-	-	-	(187,027)	(187,027)
<i>Total comprehensive income</i>						172,037
Stock compensation expense	-	-	88,881	-	-	88,881
<i>Balance, December 31, 2010</i>	1,765,000	\$ 8,825,000	\$ 11,342,473	\$ (4,213,040)	\$ 84,455	\$ 16,038,888

See Notes to Financial Statements

Statements of Cash Flows

For the years ended December 31, 2010 and 2009

	Twelve Months Ended	
	December 31, 2010	December 31, 2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income (loss)	\$ 359,064	\$ (1,950,677)
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities		
Provision for loan losses	243,620	1,945,081
Stock based compensation	88,881	250,848
Depreciation and amortization	208,608	158,520
Net amortization of bond premium/discounts	26,523	20,886
Loss on disposal of equipment	1,392	-
Gain on sale of other real estate	(397)	(17,814)
Other real estate write down	-	1,000
Changes in assets and liabilities		
Decrease (increase) in accrued interest receivable	88,570	(199,341)
Decrease (increase) in other assets	370,607	(860,967)
Decrease in accrued interest payable	(23,588)	(4,817)
Decrease in accrued expenses and other liabilities	(115,190)	(2,284)
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	1,248,090	(659,565)
CASH FLOWS FROM INVESTING ACTIVITIES		
Decrease in federal funds sold	-	3,000,000
Purchases of available for sale securities	(8,002,250)	(5,611,380)
Proceeds from called available for sale securities	3,350,000	1,500,000
Proceeds from paydowns of available for sale securities	2,965,657	2,765,359
Purchase of other investments	(30,300)	(54,100)
Net decrease (increase) in loans	1,709,842	(33,857,003)
Proceeds from sale of other real estate	405,397	550,814
Purchases of bank premises and equipment, net	(1,611,805)	(1,123,160)
NET CASH USED BY INVESTING ACTIVITIES	(1,213,459)	(32,829,470)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in deposits	1,645,203	41,333,589
Net decrease in federal funds purchased	-	(425,000)
Reimbursement from short sale	-	600
NET CASH PROVIDED BY FINANCING ACTIVITIES	1,645,203	40,909,189
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,679,834	7,420,154
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	10,032,224	2,612,070
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 11,712,058	\$ 10,032,224
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid for interest	\$ 2,097,241	\$ 2,294,788
Cash paid for taxes	\$ -	\$ -
SUPPLEMENTAL NONCASH DISCLOSURES		
Other real estate acquired upon loan settlement	\$ 500,000	\$ 1,225,000
Securitized received upon loan settlement	\$ -	\$ 173,240
Construction-in-process payable	\$ -	\$ 117,429

See Notes to Financial Statements

Notes to Financial Statements

Note 1. Organization and Summary of Significant Accounting Policies

Organization

Patriot State Bank (the “Bank” or “Patriot”) was organized and incorporated under the laws of the State of North Carolina and commenced operations on August 21, 2006. The Bank currently serves southern Wake County, North Carolina and surrounding areas through its banking office in Fuquay-Varina. The Bank has also opened two full service branches in Clayton and Clinton as well as a loan production office in Cary that it plans to convert to a full service branch. As a state chartered bank, Patriot is subject to regulation by the Commissioner of Banks of the State of North Carolina and the Federal Deposit Insurance Corporation. The Bank is not a member of the Federal Reserve System.

The accounting and reporting policies of the Bank follow U.S. generally accepted accounting principles and general practices within the financial services industry. Following is a summary of the more significant policies:

Critical Accounting Policies

Management believes policies with respect to the methodology for determination of the allowance for loan losses involve a high degree of complexity and require management to make difficult and subjective judgments which often require assumptions or estimates about highly uncertain matters. Changes in these assumptions, judgments or estimates could cause reported results to differ materially. These critical policies and their application are periodically reviewed with the Audit Committee and the Board of Directors.

Business Segments

The Bank reports its activities as a single business segment. In determining the appropriateness of segment definition, the Bank considers the materiality of a potential segment and components of the business about which financial information is available and regularly evaluated relative to resource allocation and performance assessment.

Use of Estimates

The preparation of financial statements in conformity with U.S. Generally Accepted Accounting Principles (“GAAP”) 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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, and foreclosed real estate losses.

Substantially all of the Bank’s loan portfolio consists of loans in its market area. Accordingly, the ultimate collectability of a substantial portion of the Bank’s loan portfolio is susceptible to changes in local market conditions. The regional economy is diverse and influenced to an extent by state government, major educational institutions, and activities in Research Triangle Park.

While management uses available information to recognize loan losses; future additions to the allowance may be necessary based on changes in local economic conditions. In addition, regulatory agencies, as part of their routine examination process, will review the Bank’s allowances for loan and foreclosed real estate losses. Such agencies may require the Bank to recognize additions to the allowances based on their judgments about information available to them at the time of their examinations. Because of these factors, it is reasonably possible that the allowances for loan and foreclosed real estate losses could change materially in the near term.

Cash and Cash Equivalents

For the purpose of presentation in the statement of cash flows, cash and cash equivalents are defined as those amounts included in the balance sheet caption “cash and due from banks” and “interest-bearing deposits in banks.”

Trading Securities

The Bank does not hold securities for short-term resale and, therefore, does not maintain a trading securities portfolio.

Notes to Financial Statements

Note 1. Organization and Summary of Significant Accounting Policies (continued)

Securities Held to Maturity

Bonds, notes, and debentures for which the Bank has the positive intent and ability to hold to maturity are reported at cost, adjusted for premiums and discounts that are recognized in interest income using the interest method over the period to maturity or to call dates. The Bank did not hold any securities as held to maturity for the periods presented.

Securities Available for Sale

Available for sale securities are reported at fair value and consist of bonds, notes, debentures, and certain equity securities not classified as trading securities or as held to maturity securities.

Unrealized holding gains and losses on available for sale securities are reported as a net amount in a separate component of stockholders' equity. Realized gains and losses on the sale of available for sale securities are determined using the specific-identification method and are recognized on a trade-date basis. Premiums and discounts are recognized in interest income using the interest method over the period to maturity or to call dates.

Declines in fair value of individual held to maturity and available for sale securities below cost that are other than temporary are reflected as write-downs of the individual securities to fair value. Related write-downs are included in earnings as realized losses.

Loans Receivable

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding principal amount adjusted for any charge-offs and the allowance for loan losses. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method. Discounts and premiums on any purchased loans are amortized to income using the interest method over the remaining period to contractual maturity, adjusted for anticipated prepayments.

Interest is accrued and credited to income based on principal amount outstanding. The accrual of interest on impaired loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due. When interest accrual is discontinued, all unpaid accrued interest for the current year is reversed. Interest income is subsequently recognized on the cash basis or cost recovery method, as appropriate. When facts and circumstances indicate the borrower has regained the ability to meet the required payments, the loan is returned to accrual status. Past due status of loans is determined based on contractual terms.

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 uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

Historically, the Bank has used peer loss history to determine the adequacy of the allowance. Beginning in 2010, the Bank has reviewed its actual loss history for the past twelve quarters. The Bank compared the three year average loss rate with the two year average loss rate and current year loss rates and determined that the best ratio to use for the average annual net loss ratio was the average of the most recent two years. This analysis was conducted on all relevant federal call report categories. The Bank determined there were several risk factors for the Bank that required adjustment for the historical losses. Management evaluates the historical loss rates, the economic factors that existed during the historical period used; and the future impact of current conditions relative to those historical rates.

Additionally, the allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability 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

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.

Notes to Financial Statements

Note 1. Organization and Summary of Significant Accounting Policies (continued)

Allowance for Loan Losses (continued)

The allowance consists of specific and general components. The specific component relates to loans that are classified as impaired. For such loans, 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-impaired loans and is based on historical loss experience adjusted for qualitative factors.

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 and other circumstances impacting 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 loans obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Premises and Equipment

Bank premises, furniture and equipment, and leasehold improvements are carried at cost, less accumulated depreciation and amortization computed by the straight-line method over the following estimated useful lives:

	<u>Years</u>
Building and improvements	20-30
Furniture and equipment	3-10
Leasehold improvements	shorter of lease term or estimated useful life

Other Real Estate

Real estate properties acquired through, or in lieu of, loan foreclosure are to be sold and are initially recorded at fair value less anticipated cost to sell at the date of foreclosure establishing a new cost basis. After foreclosure, valuations are periodically performed by management, and the real estate is 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 other real estate expenses, net. The Bank held eight foreclosed properties with a total carrying amount of \$1,010,000 at December 31, 2010. The Bank held ten foreclosed properties with a total carrying amount of \$915,000 at December 31, 2009.

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 their maturity.

Advertising Costs

The Bank expenses advertising costs as they are incurred.

Notes to Financial Statements

Note 1. Organization and Summary of Significant Accounting Policies (continued)

Income Taxes

Provision for income taxes is based on amounts reported in the statements of income (after exclusion of non-taxable income such as interest on state and municipal securities) and consists of taxes currently due plus deferred taxes on temporary differences in the recognition of income and expense for tax and financial statement purposes. Deferred tax assets and liabilities are included in the financial statements at currently enacted 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 tax.

Deferred income tax liability relating to unrealized appreciation (or the deferred tax asset in the case of unrealized depreciation) on investment securities available for sale is recorded in other liabilities (assets) when applicable. Such unrealized appreciation or depreciation is recorded as an adjustment to equity in the financial statements and not included in income determination until realized. Accordingly, the resulting deferred income tax liability or asset is also recorded as an adjustment to equity.

Basic Earnings per Share

Basic earnings per share is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding during the period, after giving retroactive effect to stock splits and dividends.

Diluted Earnings per Share

The computation of diluted earnings per share is similar to the computation of basic earnings per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if dilutive potential common shares had been issued. The numerator is adjusted for any changes in income or loss that would result from the assumed conversion of those potential common shares.

Comprehensive Income

Annual comprehensive income reflects the change in the Bank's equity during the year arising from transactions and events other than investment by and distributions to shareholders. It consists of net income plus certain other changes in assets and liabilities that are reported as separate components of stockholders' equity rather than as income or expense.

Employee Benefit Plans

The Bank has a defined contribution plan qualifying under Internal Revenue Code Section 401(k). The Bank will contribute up to four percent of an employee's compensation based on the following allocation. Employee contributions are matched one-hundred percent by the Bank up to the first three percent of the employee's contributions and up to fifty percent of the amount over three percent, subject to an overall limitation of five percent of compensation. The Bank's match is expensed as incurred.

Stock-based Compensation

Compensation cost has been measured using the fair value of awards on their grant dates and is recognized over the service period, which is usually the vesting period.

Notes to Financial Statements

Note 1. Organization and Summary of Significant Accounting Policies (continued)

Fair Value of Financial Instruments

FASB ASC 825-10, "Disclosures about Fair Value of Financial Instruments," requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet. 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. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instruments. FASB ASC 825-10 excludes certain financial instruments and all nonfinancial instruments from disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Bank.

Subsequent Events

These financial statements have not been updated for subsequent events occurring after the date these financial statements were issued.

Recent Accounting Pronouncements

The following is a summary of recent authoritative pronouncements:

In July 2010, the Receivables topic of the ASC was amended to require expanded disclosures related to a company's allowance for credit losses and the credit quality of its financing receivables. The amendments will require the allowance disclosures to be provided on a disaggregated basis. The Bank complies with the disclosures in its financial statements for the year ended December 31, 2010. Disclosures about Troubled Debt Restructurings (TDRs) required by the Update have been deferred by FASB in an update issued in early 2011. The TDR disclosures are anticipated to be effective for periods ending after June 15, 2011. See Note. 5.

On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), which significantly changes the regulation of financial institutions and the financial services industry. The Dodd-Frank Act includes several provisions that will affect how community banks, thrifts, and small bank and thrift holding companies will be regulated in the future. Among other things, these provisions abolish the Office of Thrift Supervision and transfer its functions to the other federal banking agencies, relax rules regarding interstate branching, allow financial institutions to pay interest on business checking accounts, change the scope of federal deposit insurance coverage, and impose new capital requirements on bank and thrift holding companies. The Dodd-Frank Act also establishes the Bureau of Consumer Financial Protection as an independent entity within the Federal Reserve, which will be given the authority to promulgate consumer protection regulations applicable to all entities offering consumer financial services or products, including banks. Additionally, the Dodd-Frank Act includes a series of provisions covering mortgage loan origination standards affecting originator compensation, minimum repayment standards, and pre-payments. Management is actively reviewing the provisions of the Dodd-Frank Act and assessing its probable impact on our business, financial condition, and results of operations.

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

Notes to Financial Statements

Note 2. Fair Value

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

Cash and due from banks: The carrying amounts reported in the balance sheet for cash and due from banks approximate their fair values.

Interest-bearing deposits with banks: Fair values for time deposits are estimated using a discounted cash flow analysis that applies interest rates currently being offered on certificates to a schedule of aggregated contractual maturities on such time deposits. Carrying values of interest-bearing money market deposits approximate their fair values.

Federal funds sold: Carrying values for federal funds sold approximate their fair values.

Securities: Fair values for securities, excluding restricted equity securities, are based on quoted market prices, where available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. The carrying values of other securities approximate fair values.

Loans receivable: For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying amounts. The fair values for other loans are estimated using discounted cash flow analysis, based on interest rates currently being offered for loans with similar terms to borrowers with similar credit quality. Loan fair value estimates include judgments regarding future expected loss experience and risk characteristics. The fair value of impaired loans is estimated using one of several methods, including collateral value, quoted market prices, and discounted cash flows. The carrying amount of accrued interest receivable approximates its fair value.

Deposit liabilities: The fair values disclosed for demand and savings deposits are, by definition, equal to the amount payable on demand at the reporting date. The fair values for certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated contractual maturities on such time deposits. The carrying amount of accrued interest payable approximates fair value.

Secured borrowings: Carrying values for secured borrowings approximate their fair values.

Federal funds purchased: Carrying values for federal funds purchased approximate their fair values.

Other liabilities: For fixed-rate loan commitments, fair value considers the difference between current levels of interest rates and the committed rates. The carrying amounts of other liabilities approximate fair value.

Notes to Financial Statements

Note 2. Fair Value (continued)

Following is a summary of the carrying amounts and fair values of the Bank's financial assets and liabilities:

	December 31, 2010		December 31, 2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<i>Financial assets</i>				
Cash and due from banks	\$ 1,813,842	\$ 1,813,842	\$ 1,397,677	\$ 1,397,677
Interest-bearing deposits in banks	9,898,214	9,898,214	8,634,547	8,634,547
Securities available for sale	16,223,090	16,223,090	14,750,044	14,750,044
Other investments	557,900	557,900	527,600	527,600
Loans, net	104,677,937	104,736,000	107,131,400	107,092,000
Accrued interest receivable	542,638	542,638	631,208	631,208
<i>Financial liabilities</i>				
Deposits	\$ 122,702,990	\$ 123,214,990	\$ 121,057,787	\$ 124,882,000
Secured borrowings	250,000	250,000	250,000	250,000
Accrued interest payable	\$ 78,343	\$ 78,343	\$ 101,931	\$ 101,931

The Bank utilizes fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Securities available for sale are recorded at fair value on a recurring basis. Additionally, from time to time, the Bank may be required to record at fair value other assets or liabilities on a nonrecurring basis, such as loans held for sale, loans held for investment and certain other assets or liabilities. These nonrecurring fair value adjustments typically involve application of lower of cost or market accounting or write-downs of individual assets or liabilities.

Fair Value Hierarchy

The Bank groups assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

- Level 1 – Valuation is based upon quoted prices for identical instruments traded in active markets.
- Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 – Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

Notes to Financial Statements

Note 2. Fair Value (continued)

Assets and Liabilities Recorded at Fair Value on a Recurring Basis

Following is a description of methodologies used for assets and liabilities recorded at fair value on a recurring basis.

Investment Securities Available for Sale

Investment securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include mortgage-backed securities issued by government sponsored entities, municipal bonds and corporate debt securities. Securities classified as Level 3 include asset-backed securities in less liquid markets.

Description	Market Values 12/31/10	Quoted Prices in Active Markets for		
		Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
U.S. Government Agencies	\$ 6,271,836	\$ -	\$ 6,271,836	\$ -
Government Sponsored MBS - Residential	\$ 7,410,649	-	\$ 7,410,649	-
Other Securities	\$ 2,540,605	-	\$ 2,540,605	-
Total	\$ 16,223,090	\$ -	\$ 16,223,090	\$ -

Description	Market Values 12/31/09	Quoted Prices in Active Markets for		
		Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
U.S. Government Agencies	\$ 1,797,406	\$ -	\$ 1,797,406	\$ -
Government Sponsored MBS - Residential	\$ 10,437,754	-	\$ 10,437,754	-
Other Securities	\$ 2,514,884	-	\$ 2,514,884	-
Total	\$ 14,750,044	\$ -	\$ 14,750,044	\$ -

Assets and Liabilities Recorded at Fair Value on a Nonrecurring Basis

Following is a description of methodologies used for assets and liabilities recorded at fair value on a nonrecurring basis.

Loans

The Bank does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and an allowance for loan losses is established. 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, the fair value is estimated using one of several methods, including collateral value, quoted market prices, and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At December 31, 2010, substantially all of the impaired loans were evaluated based on the fair value of the collateral. 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

Notes to Financial Statements

Note 2. Fair Value (continued)

or a current appraised value, the Bank records the impaired loan as nonrecurring Level 2. When the 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 Bank records the impaired loan as nonrecurring Level 3.

Other Real Estate

Other Real Estate is recorded at the lesser of cost or current market value. The current market value is based on existing or new appraisals discounted for expected costs to sell.

Description	Market Values 12/31/10	Quoted Prices in Active Markets		
		for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
Impaired Loans				
Commercial and agricultural	\$ 75,000	\$ -	\$ -	\$ 75,000
Real estate construction and development	612,477	-	-	612,477
Real estate mortgage nonresidential	578,875	-	-	578,875
Real estate mortgage residential	94,073	-	-	94,073
Other Real Estate	1,010,000	-	-	1,010,000
Total	\$ 2,370,425	\$ -	\$ -	\$ 2,370,425

Description	Market Values 12/31/09	Quoted Prices in Active Markets		
		for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
Impaired Loans				
Commercial and agricultural	\$ 122,500	-	-	\$ 122,500
Real estate construction and development	2,814,550	-	-	2,814,550
Real estate mortgage nonresidential	500,000	-	-	500,000
Real estate mortgage residential	249,313	-	-	249,313
Other Real Estate	915,000	-	-	915,000
Total	\$ 4,601,363	\$ -	\$ -	\$ 4,601,363

Note 3. Restrictions on Cash

To comply with banking regulations, the Bank is required to maintain certain average cash reserve balances. For the periods including December 31, 2010 and 2009, approximately \$3,709,000 and \$3,631,000, respectively, of cash on hand and in banks was reserved to comply with such regulations.

Notes to Financial Statements

Note 4. Securities

Following is a summary of investment securities, all of which are classified as available for sale:

	December 31, 2010			
	Amortized	Gross	Gross	
	Cost	Unrealized	Unrealized	Fair Value
		Gains	Losses	
U.S. Government Agencies	\$ 6,500,000	\$ -	\$ (228,164)	\$ 6,271,836
Government Sponsored MBS - Residential	7,024,311	386,338	-	7,410,649
Other securities	2,614,324	17,795	(91,514)	2,540,605
Total available for sale	<u>\$16,138,635</u>	<u>\$ 404,133</u>	<u>\$ (319,678)</u>	<u>\$16,223,090</u>

	December 31, 2009			
	Amortized	Gross	Gross	
	Cost	Unrealized	Unrealized	Fair Value
		Gains	Losses	
U.S. Government Agencies	\$ 1,850,000	\$ 1,312	\$ (53,906)	\$ 1,797,406
Government Sponsored MBS - Residential	10,011,549	427,613	(1,408)	10,437,754
Other securities	2,617,013	-	(102,129)	2,514,884
Total available for sale	<u>\$14,478,562</u>	<u>\$ 428,925</u>	<u>\$ (157,443)</u>	<u>\$14,750,044</u>

The Bank had \$250,000 of investment securities pledged to The Senior Housing Crime Prevention Foundation (the Foundation) at December 31, 2010 and 2009. These securities are pledged in conjunction with the acquisition of preferred stock in the Foundation. Income from the pledged securities is used by the Foundation to maintain its operations and to contract for the operation of crime reduction and prevention programs in a senior housing facility in Harnett County in the State of North Carolina. The Bank is required to maintain the investment in the Foundation until May 23, 2012.

The Bank had \$557,900 in other investments as of December 31, 2010. This is comprised of a \$250,000 investment in the stock of the Senior Housing Crime Prevention Foundation discussed above, a \$205,900 investment in stock of the Federal Home Loan Bank and a \$102,000 investment in the stock of Pacific Coast Bankers Bank. The Bank had \$527,600 in other investments as of December 31, 2009. The \$527,600 includes a \$250,000 investment in the stock of the Senior Housing Crime Prevention Foundation discussed above, a \$175,600 investment in stock of the Federal Home Loan Bank and \$102,000 investment in the stock of Pacific Coast Bankers Bank.

There were no realized gains or losses related to the sale or maturity of investment securities for the periods ended December 31, 2010 and December 31, 2009.

Notes to Financial Statements

Note 4. Securities (continued)

The fair value and cost, by contractual maturity, of available for sale securities at December 31, 2010 follows:

December 31, 2010	No Maturity Date	Within 1 Year	After 1 Year Through 5 Years	After 5 Years Through 10 Years	After 10 Years	Total
Fair Value						
U.S. Government Agencies	\$ -	\$ -	\$ -	\$ 1,916,688	\$ 4,355,148	\$ 6,271,836
Government Sponsored MBS - Residential	-	-	7,410,649	-	-	7,410,649
Other securities	81,727	-	-	-	2,458,878	2,540,605
Total available for sale	<u>\$ 81,727</u>	<u>\$ -</u>	<u>\$ 7,410,649</u>	<u>\$ 1,916,688</u>	<u>\$ 6,814,026</u>	<u>\$ 16,223,090</u>
Cost						
U.S. Government Agencies	\$ -	\$ -	\$ -	\$ 2,000,000	\$ 4,500,000	\$ 6,500,000
Government Sponsored MBS - Residential	-	-	7,024,311	-	-	7,024,311
Other securities	173,241	-	-	-	2,441,083	2,614,324
Total available for sale	<u>\$ 173,241</u>	<u>\$ -</u>	<u>\$ 7,024,311</u>	<u>\$ 2,000,000</u>	<u>\$ 6,941,083</u>	<u>\$ 16,138,635</u>

The maturities of mortgage-backed securities are presented according to the date underlying mortgages in the pool are due. However, the Bank receives regular payments of principal on the securities in addition to prepayments of principal arising from repayment of the mortgages in advance of their scheduled due dates. During the periods ended December 31, 2010 and 2009, the Bank received principal payments of \$2,965,657 and \$2,765,359 respectively. When the Bank receives prepayments on mortgage backed securities, any unamortized discount associated with such prepayment is recognized as gain.

The following table details unrealized losses and related fair values in the Bank's available for sale investment securities portfolios. This information is aggregated by the length of time that individual securities have been in a continuous unrealized loss position as of December 31, 2010 and 2009.

December 31, 2010	Less Than 12 Months		12 Months or More		Total	
	Unrealized		Unrealized		Unrealized	
	Fair Value	Losses	Fair Value	Losses	Fair Value	Losses
U.S. Government Agencies	\$ 6,271,836	\$ 228,164	\$ -	\$ -	\$ 6,271,836	\$ 228,164
Other securities	-	-	81,727	91,514	81,727	91,514
Total available for sale	<u>\$ 6,271,836</u>	<u>\$ 228,164</u>	<u>\$ 81,727</u>	<u>\$ 91,514</u>	<u>\$ 6,353,563</u>	<u>\$ 319,678</u>
December 31, 2009						
U.S. Government Agencies	\$ 1,446,094	\$ 53,906	\$ -	\$ -	\$ 1,446,094	\$ 53,906
Government Sponsored MBS - Residential	1,030,902	1,408	-	-	1,030,902	1,408
Other securities	143,981	29,259	2,370,903	72,870	2,514,884	102,129
Total available for sale	<u>\$ 2,620,977</u>	<u>\$ 84,573</u>	<u>\$ 2,370,903</u>	<u>\$ 72,870</u>	<u>\$ 4,991,880</u>	<u>\$ 157,443</u>

As discussed in Note 1, the Bank began utilizing their historical charge-offs for the allowance calculation which resulted in a lower provision for the year ended December 31, 2010. Prior to 2010, the Bank relied on peer historical charge-offs.

Notes to Financial Statements

Note 4. Securities (continued)

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. As of December 31, 2010, the Bank had an investment in Four Oaks Fincorp Inc. with a book value of \$173,241 and a market value of \$81,727, resulting in an unrealized loss of \$91,514. The Four Oaks Fincorp Inc. security has been in a loss position for thirteen consecutive months. The market value of the Four Oaks security at December 31, 2009 was \$143,981. The Four Oaks security held fairly steady the first six months of 2010, and then dropped to a market value of \$95,987 in July of 2010. The Four Oaks security recovered to \$119,024 in August 2010. At November 30, 2010 the Four Oaks security market value had dropped to \$72,676 then recovered slightly in December 2010 to a market value of \$81,727. Management has reviewed quarterly and year end results for Four Oaks Fincorp, and, 2010 operating losses are attributable to high charge-offs for the year. Four Oaks still remains well capitalized. The Bank will continue to monitor closely the value of the Four Oaks Fincorp, Inc. securities, however we do not believe at this time that the decrease in market value should be considered other-than-temporary. The Bank believes the decline in market value to be temporary and expects to see a recovery in value in the future. It is more likely than not that the Bank will not have to sell the investments before recovery of their amortized cost basis. As of December 31, 2009, the Bank had an investment in Wachovia Trust Preferred Securities with a book value of \$2,443,773 and a market value of \$2,370,903 resulting in an unrealized loss of \$72,870. The Wachovia security had been in a loss position for twenty two consecutive months. The market value of the Wachovia security continued to recover in 2010 and has been in an unrealized gain position since April 2010.

Note 5. Loans

The major components of loans in the balance sheet at December 31, 2010 and 2009 are as follows:

	December 31,	
	2010	2009
Commercial and agricultural	\$ 7,078,442	\$ 6,893,133
Real estate construction and land development	8,025,088	19,030,259
Real estate mortgage loans		
Nonresidential	49,887,089	45,120,395
Residential	40,083,693	36,294,400
Consumer loans	1,305,242	2,537,803
Total loans	<u>106,379,554</u>	<u>109,875,990</u>
Allowance for loan losses	<u>(1,701,617)</u>	<u>(2,744,590)</u>
Net loans	<u>\$ 104,677,937</u>	<u>\$ 107,131,400</u>

The following table sets forth information regarding activity in the allowance for loan losses:

	At or for the Years Ended	
	December 31	
	2010	2009
Balance at beginning of period	\$ 2,744,590	\$ 1,167,793
Provision for loan losses	243,620	1,945,081
Amounts charged off	(1,286,593)	(381,534)
Recoveries	-	13,250
Balance at end of period	<u>\$ 1,701,617</u>	<u>\$ 2,744,590</u>

Notes to Financial Statements

Note 5. Loans (continued)

Allowance for Loan Losses

The following table presents information on the loans evaluated individually for impairment and collectively for impairment in the allowance for loan losses:

Allowance for Loan Losses and Recorded Investment in Loans Receivable For the Year Ended December 31, 2010

	Commercial and Agricultural	Real Estate Construction and Development	Real Estate Mortgage Nonresidential	Real Estate Mortgage Residential	Consumer	Unallocated	Total
Allowance for loan losses:							
Beginning balance	\$ 232,687	\$ 1,080,460	\$ 837,569	\$ 542,707	\$ 51,167	\$ -	\$ 2,744,590
Charge-offs	45,469	529,027	236,073	476,024	-	-	1,286,593
Recoveries	-	-	-	-	-	-	-
Provisions	(47,390)	(209,116)	107,365	422,262	(37,046)	7,545	243,620
Ending balance	<u>\$ 139,828</u>	<u>\$ 342,317</u>	<u>\$ 708,861</u>	<u>\$ 488,945</u>	<u>\$ 14,121</u>	<u>\$ 7,545</u>	<u>\$ 1,701,617</u>
Ending balance: individually evaluated for impairment	<u>\$ 60,097</u>	<u>\$ 199,048</u>	<u>\$ 133,550</u>	<u>\$ 591</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 393,286</u>
Ending balance: collectively evaluated for impairment	<u>\$ 79,731</u>	<u>\$ 143,269</u>	<u>\$ 575,311</u>	<u>\$ 488,354</u>	<u>\$ 14,121</u>	<u>\$ 7,545</u>	<u>\$ 1,308,331</u>
Loans receivable							
Ending balance	<u>\$ 7,078,442</u>	<u>\$ 8,025,088</u>	<u>\$ 49,887,089</u>	<u>\$ 40,083,693</u>	<u>\$ 1,305,242</u>	<u>\$ -</u>	<u>\$ 106,379,554</u>
Ending balance: individually evaluated for impairment	<u>\$ 629,456</u>	<u>\$ 3,347,030</u>	<u>\$ 2,761,956</u>	<u>\$ 1,991,085</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8,729,527</u>
Ending balance: collectively evaluated for impairment	<u>\$ 6,448,986</u>	<u>\$ 4,678,058</u>	<u>\$ 47,125,133</u>	<u>\$ 38,092,608</u>	<u>\$ 1,305,242</u>	<u>\$ -</u>	<u>\$ 97,650,027</u>

Notes to Financial Statements

Note 5. Loans (continued)

The following table lists the loan grades utilized by the Bank that serve as credit quality indicators. Each of the loan grades include high and low factors associated with their classification that are utilized to calculate the aggregate ranges of the allowance for loan losses. The total balance does not include loans secured by deposits or the undisbursed portion of construction loans in process for loans graded Pass.

Credit Risk Profile by Internally Assigned Grades

	Commercial & Agricultural	Real Estate Construction & Development	Real Estate Mortgage Nonresidential	Real Estate Mortgage Residential - Prime	Consumer
Pass	\$ 4,792,906	\$ 4,408,553	\$ 42,243,650	\$ 36,819,245	\$ 1,288,429
Special Mention	1,630,927	270,047	4,882,144	1,155,417	12,930
Substandard	510,730	3,236,803	2,761,295	2,109,031	3,452
Doubtful	143,879	109,685	-	-	431
Total	<u>\$ 7,078,442</u>	<u>\$ 8,025,088</u>	<u>\$ 49,887,089</u>	<u>\$ 40,083,693</u>	<u>\$ 1,305,242</u>

The internally assigned grades are defined as follows:

Special Mention – are potentially weak credits. Assets rated special mention are currently protected but potentially weak. These assets constitute an undue and unwarranted credit risk, but not to the point of justifying a classification of substandard. Loans in this category have potential weaknesses, which may, if not corrected weaken the asset, or inadequately protect the Bank's credit position at some future date.

Substandard – Assets classified substandard have well-defined weakness(es) in the credit that jeopardize the repayment of all principal and interest in accordance with the contractual terms of the credit. Substandard assets are generally well secured and any loss potential is minimal. Assets with loss potential less than 35% of principal should be classified substandard.

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. The possibility of loss is extremely high, but because of certain factors that may work to the advantage and strengthening of the asset, its classification as an estimated loss is deferred until its more exact status may be determined.

The following table presents an age analysis of past due status of loans by category.

	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans Receivable	Past Due 90 Days or More and Still Accruing
Commercial and agricultural	\$ -	\$ -	\$ 143,866	\$ 143,866	\$ 6,934,576	\$ 7,078,442	\$ -
Real estate construction and land development	1,000,000	-	-	1,000,000	7,025,088	8,025,088	-
Real estate mortgage loans						-	
Nonresidential	155,206	-	1,207,620	1,362,826	48,524,263	49,887,089	-
Residential	245,438	-	418,796	664,234	39,419,459	40,083,693	-
Consumer loans	-	-	-	-	1,305,242	1,305,242	-
Total loans	<u>\$ 1,400,644</u>	<u>\$ -</u>	<u>\$ 1,770,282</u>	<u>\$ 3,170,926</u>	<u>\$ 103,208,628</u>	<u>\$ 106,379,554</u>	<u>\$ -</u>

Notes to Financial Statements

Note 5. Loans (continued)

Impaired Loans

A loan is considered impaired when it is probable that the Bank will be unable to collect contractual principal and interest payments in accordance with the original or modified terms of the loan agreement. Impaired loans are measured based on the estimated fair value of the collateral less estimated cost to sell if the loan is considered collateral dependent.

The categories of non-accrual loans and impaired loans overlap, although they are not considered coextensive. The Bank considers all circumstances regarding the loan and borrower on an individual basis when determining whether an impaired loan should be placed on non-accrual status, such as the financial strength of the borrower, the estimated collateral value, reasons for the delay, payment record, the amount past due and the number of days past due.

At December 31, 2010 and 2009 there were no loans past due 90 days or more which were still accruing interest. Impaired loans of \$8,729,527 at December 31, 2010 consisted of non-accrual loans of \$4,223,871 and \$4,505,656 of loans still accruing interest. At December 31, 2010, impaired loans of \$1,753,711 had specific reserves of \$393,286. There was \$6,975,816 of impaired loans without specific reserves at December 31, 2010. Impaired loans of \$5,815,918 at December 31, 2009 consisted of non-accrual loans of \$2,510,527 and \$3,305,391 of loans still accruing interest. At December 31, 2009, impaired loans of \$5,007,603 had specific reserves of \$1,321,240. There was \$808,315 of impaired loans without specific reserves at December 31, 2009. The average recorded investment in impaired loans during the year ended December 31, 2010 was \$4,087,532.

The following table is a summary of information related to impaired loans as of December 31, 2010:

	<u>Recorded Investment</u>	<u>Unpaid Principal Balance</u>	<u>Related Allowance</u>	<u>Average Recorded Investment</u>	<u>Interest Income Recognized</u>
With no related allowance recorded:					
Commercial and agricultural	\$ 496,371	\$ 494,359	\$ -	\$ 34,995	\$ 1,921
Real estate construction and development	2,637,598	2,535,505	-	1,800,770	15,916
Real estate mortgage nonresidential	2,109,524	2,049,531	-	368,219	11,194
Real estate mortgage residential	1,914,447	1,896,421	-	449,275	33,676
With an related allowance recorded:					
Commercial and agricultural	\$ 169,820	\$ 135,097	\$ 60,097	\$ 192,676	\$ -
Real estate construction and development	830,834	811,525	199,048	345,215	6,635
Real estate mortgage nonresidential	853,443	712,425	133,550	796,181	2,070
Real estate mortgage residential	100,083	94,664	591	100,201	-
Total:					
Commercial and agricultural	\$ 666,191	\$ 629,456	\$ 60,097	\$ 227,671	\$ 1,921
Real estate construction and development	3,468,432	3,347,030	199,048	2,145,985	22,551
Real estate mortgage nonresidential	2,962,967	2,761,956	133,550	1,164,400	13,264
Real estate mortgage residential	2,014,530	1,991,085	591	549,476	33,676

Interest foregone on non-accrual loans was approximately \$372,256 and \$93,680 for the years ended December 31, 2010 and 2009, respectively.

Notes to Financial Statements

Note 6. Premises and Equipment

Components of property and equipment and total accumulated depreciation are as follows:

	December 31,	
	2010	2009
Land	\$ 893,789	\$ 890,429
Building	2,743,775	794,949
Construction-in-process	-	411,464
Leasehold improvements	2,774	7,751
Furniture and equipment	821,100	755,063
	<u>4,461,438</u>	<u>2,859,656</u>
Accumulated depreciation and amortization	(661,392)	(461,415)
Net premises and equipment	<u>\$ 3,800,046</u>	<u>\$ 2,398,241</u>

Depreciation expense for the years ended December 31, 2010 and 2009 was \$208,608 and \$158,520 respectively.

Lease expense totaled \$64,274 and \$75,446 for the years ended December 31, 2010 and 2009, respectively. The Bank has two leases - one for the full service branch in Clayton, North Carolina and one for the loan production office in Cary, North Carolina.

The Clayton office has a one year lease dated April 1, 2010. Under this lease, monthly lease expense will be \$1,300 through March 2011.

The Cary office has a two year and two month lease dated November 1, 2008. Monthly lease expense for November and December of 2008 was \$665. The monthly lease expense for January 2009 through December 2010 increased to \$3,798. The Bank exercised its option on this lease to renew for an additional one year term. Monthly lease expense under this lease will be \$3,798 through December 2011.

Pursuant to the terms of the non-cancelable lease agreements in effect at December 31, 2010, the schedule of future minimum rent payments is as follows:

2011	<u>\$ 49,476</u>
-------------	------------------

Note 7. Deposits

The aggregate amount of time deposits in denominations of one hundred thousand dollars or more at December 31, 2010 and 2009 was \$27,349,000 and \$30,087,000 respectively.

The Bank had \$74,485,849 in time deposits at December 31, 2010, which includes CD's and certain IRA's. Also included are \$20,881,000 in purchased deposits. At December 31, 2010, the scheduled maturities of time deposits are as follows:

2011	\$ 50,203,531
2012	11,351,543
2013	5,638,820
2014	2,002,706
2015	2,179,534
Thereafter	3,109,715
	<u>\$ 74,485,849</u>

On December 31, 2010, the aggregate amount of demand deposits that had been reclassified as overdrafts was \$1,081.

Notes to Financial Statements

Note 8. Borrowed Funds

Secured Borrowings

Secured borrowings represent the accounting for our \$250,000 investment in The Senior Housing Crime Prevention Foundation (as discussed in Note 4). If a transfer of assets in exchange for cash or other consideration (other than beneficial interests in the transferred assets) does not meet the criteria for a sale, the transferor and transferee shall account for the transfer as secured borrowing with pledge of collateral.

Short-term Debt

Short-term debt consists of Federal funds purchased. Federal funds purchased generally mature within one to seven days from the transaction date. The maximum outstanding balance in Federal funds purchased during 2010 and 2009 was \$3,445,000 and \$6,200,000 respectively. The weighted average cost of Federal funds purchased was 0.81% in 2010 and 0.87% in 2009. There were no Federal funds purchased at December 31, 2010 or at December 31, 2009.

Note 9. Earnings (Loss) Per Share

The following table presents the computation of earnings (loss) per share for the periods ended December 31, 2010 and 2009:

	Twelve Months Ended	
	December 31,	
	2010	2009
Net income (loss) available to common stockholders	<u>\$ 359,064</u>	<u>\$(1,950,677)</u>
Weighted average shares outstanding	<u>1,765,000</u>	<u>1,765,000</u>
Weighted average shares outstanding diluted	<u>1,765,000</u>	<u>1,765,000</u>
Basic income (loss) per share	<u>\$ 0.20</u>	<u>\$ (1.11)</u>
Diluted income (loss) per share	<u>\$ 0.20</u>	<u>\$ (1.11)</u>

In connection with its initial offering of common stock, the Bank issued a warrant to purchase for \$11 one share of common stock for each ten shares of common stock purchased, a total of 176,500 warrants. The warrants expire seven years from the conclusion of the common stock offering, August 21, 2006. The potential exchange of warrants for common stock is excluded from the computation of loss per share for the period ended December 31, 2009, as the assumed issuance of shares would reduce loss per share. In addition, the Bank has 263,759 and 266,759 options outstanding at December 31, 2009 and 2010 respectively, to purchase shares of the Bank's common stock. The potential effect of the exercise of these options is excluded from the computation of weighted average diluted shares for the period ended December 31, 2009 as the effect would be anti-dilutive. The effect of the warrants and options is excluded from the income per share calculation for the period ended December 31, 2010, as the exercise price exceeds the Bank's average stock price for the period.

Notes to Financial Statements

Note 10. Stock Based Compensation

The Bank has two stock-based compensation plans, which are described below. The compensation cost that has been charged against income for those plans was approximately \$88,881 and \$250,848 for the twelve-month periods ended December 31, 2010 and 2009 respectively. The fair value of each option award is estimated on the date of grant using the Black-Scholes option-pricing model. The risk-free interest rate is based on the U.S. Treasury rate for the expected life at the time of grant. Volatility is based on the volatilities of our trading history. The expected life is based on the average life of the options of 10 years and the weighted average graded vesting period of 1.59 years, and forfeitures are considered immaterial. Compensation expense is determined using the grant date fair value as determined by the Black-Scholes model over the service period.

On March 6, 2007, the Bank adopted a qualified incentive stock option plan which reserves 176,500 shares for purchase by eligible employees. Options granted under this plan vest at the rate of 25% at the date of grant and an additional 25% at each anniversary date for the next three years, expire not more than ten years from the date of grant, and are exercisable at not less than the fair market value of the stock at the date of the grant.

On March 6, 2007, the Bank also adopted a non-qualified stock option plan which reserves 176,500 shares for purchase by non-employee directors. Options granted under this plan vest at the rate of 25% at the date of grant and an additional 25% at anniversary date for the next three years, and are exercisable at not less than the fair market value of the stock at the date of the grant. The life of such options shall not extend more than ten years from the date of the grant.

On March 23, 2010, the Bank issued 7,000 qualified options to selected employees with a weighted average grant date fair value of \$1.39 per option. In August 2010, an employee resigned from the Bank and forfeited 4,000 options. There was no other stock compensation activity during 2010. There were no options granted, issued or forfeited during 2009.

The following table illustrates the assumptions for the Black-Scholes model used in determining the fair value of options granted to employees for the year ended December 31, 2010.

	<u>2010</u>
Expected volatility	27%
Expected dividends	0.00%
Expected term	5-6 years
Risk-free rate	2.70%

A summary of option activity under the stock option plans for the years ended December 31, 2009 and 2010 is presented below:

	<u>Options Available</u>	<u>Options Outstanding</u>	<u>Weighted Average Exercise Price</u>
<i>Balance at December 31, 2008</i>	89,241	263,759	\$ 11.00
Authorized	-	-	-
Granted	-	-	-
Forfeited	-	-	-
<i>Balance at December 31, 2009</i>	89,241	263,759	\$ 11.00
Authorized	-	-	-
Granted	(7,000)	7,000	8.99
Forfeited	4,000	(4,000)	10.00
<i>Balance at December 31, 2010</i>	86,241	266,759	\$ 10.96

Notes to Financial Statements

Note 10. Stock Based Compensation (continued)

The following table sets forth the exercise prices, the number of options outstanding and the number of options exercisable at December 31, 2010:

Range of Exercise Prices	Number of Options Outstanding	Weighted Average Exercise Price	Weighted Average Contractual Life Remaining (Years)	Number of Options Exercisable	Weighted Average Exercise Price	Weighted Average Contractual Life Remaining (Years)
\$8.99 - \$11.00	266,759	\$ 10.96	6.51	258,259	\$ 10.99	6.44

The following table sets forth information pertaining to the Bank's exercisable options and options expected to vest:

	Twelve Months Ended December 31, 2010
Incentive and non-qualified stock options:	
Fair value of options granted during period expected to vest	\$ 5,471
Aggregate intrinsic value of exercisable and non-vested options expected to vest	\$ -
Number of non-vested options expected to vest	8,500
Weighted average price of non-vested options expected to vest	\$ 10.11
Weighted average remaining life of non-vested options expected to vest	8.49
Intrinsic value of non-vested options expected to vest	\$ -
Intrinsic value of forfeited options	\$ -

As of December 31, 2010, there was \$16,569 of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under the Bank's stock option plans. That cost is expected to be recognized over a weighted-average period of 1.06 years. The total fair value of shares vested during the year ended December 31, 2010, was \$262,202.

Note 11. Benefit Plans

The Bank maintains a profit sharing plan (the "Plan") pursuant to Section 401(k) of the Internal Revenue Code. The plan covers substantially all employees who are 18 years of age and who have completed six months of service. Participants may contribute up to 50 percent of their salary to the Plan, subject to limits imposed under the Internal Revenue Code. The Bank matches 100 percent of the first three percent of a participant's compensation and 50 percent of the excess, subject to an overall limitation of five percent of compensation. For the periods ended December 31, 2010 and 2009, the Bank contributed \$55,575 and \$55,295 respectively. The Bank's contributions vest immediately.

Notes to Financial Statements

Note 12. Income Taxes

Operating Loss Carryforwards

The Bank has a loss carryforward of approximately \$1.2 million for federal and state income tax purposes that may be used to offset future taxable income. If not previously utilized, the federal and state loss carryforward will begin to expire in 2026 and 2021, respectively.

Current and Deferred Income Tax Components

The components of income tax expense for the years ended December 31, 2010 and 2009 are as follows:

	<u>2010</u>	<u>2009</u>
Current	\$ -	\$ -
Deferred	201,125	(676,009)
Deferred tax asset valuation allowance change	(201,125)	676,009
	<u>\$ -</u>	<u>\$ -</u>

Rate Reconciliation

A reconciliation of income tax expense (benefit) computed at the statutory federal income tax rate to income tax expense included in the statement of operations for the years ended December 31, 2010 and 2009 is as follows:

	<u>2010</u>	<u>2009</u>
Tax at statutory federal rate	\$ 122,082	\$ (663,230)
State tax, net of federal benefit	25,423	(71,328)
Stock compensation expense	21,341	49,776
Other	32,279	8,773
Deferred tax asset valuation allowance change	(201,125)	676,009
	<u>\$ -</u>	<u>\$ -</u>

Notes to Financial Statements

Note 12. Income Taxes (continued)

The significant components of net deferred tax assets at December 31, 2010 and 2009 are as follows:

	<u>2010</u>	<u>2009</u>
<i>Deferred tax assets</i>		
Allowance for loan losses	\$ 506,991	\$ 959,035
Net operating losses	424,665	276,784
Pre-opening expenses	173,457	189,718
Stock compensation expense	216,497	206,429
Depreciation	42,231	30,569
Deferred loan costs	5,227	10,341
OREO Write Down	-	386
Non Accrual Interest	143,520	36,117
Contributions	8,309	8,157
Deferred tax asset	<u>1,520,897</u>	<u>1,717,536</u>
<i>Deferred tax liabilities</i>		
Prepaid expenses	(25,318)	(24,144)
Deferred loan fees	-	-
Accretion of bond discount	(13,616)	(10,304)
Deferred tax liability	<u>(38,934)</u>	<u>(34,448)</u>
Deferred tax asset valuation allowance	<u>(1,481,963)</u>	<u>(1,683,088)</u>
Net deferred tax asset (liability)	<u>\$ -</u>	<u>\$ -</u>

The change in the deferred tax valuation allowance was (\$201,125) in 2010 and \$676,009 in 2009.

Deferred tax assets represent the future tax benefit of deductible differences and, if it is more likely than not that a tax asset will not be realized, a valuation allowance is required to reduce the recorded deferred tax assets to net realizable value. As of December 31, 2010 and 2009, in consideration of the lack of an established earnings history, management has provided a valuation allowance of 100% to reflect its net realizable value.

The Bank has analyzed the tax positions taken or expected to be taken in its tax returns and concluded it has no liability related to uncertain tax positions. Tax returns for the years of 2007, 2008 and 2009 remain subject to examination by both federal and state tax authorities.

Note 13. Commitments and Contingencies

Stockholders' Equity

During the Bank's initial sale of shares, one warrant to purchase an additional share of the Bank's common stock was included with each 10 shares purchased. At December 31, 2010, 176,500 such warrants were outstanding.

Litigation

In the normal course of business the Bank may be involved in various legal proceedings. The Bank was not involved in any litigation at December 31, 2010.

Financial Instruments with Off-balance sheet Risk

The Bank is party to financial instruments with off-balance-sheet risk in the normal course of business to meet financing needs of its customers. These financial instruments include commitments to extend credit and standby

Notes to Financial Statements

Note 13. Commitments and Contingencies (continued)

letters of credit. These instruments involve, to varying degrees, credit risk in excess of the amount recognized in the balance sheet.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as for on-balance sheet instruments. A summary of the Bank's commitments at December 31, 2010 and 2009 is as follows:

	<u>December 31, 2010</u>	<u>December 31, 2009</u>
Financial instruments whose contract amounts represent credit risk		
Unfunded commitments to extend credit	\$ 14,909,388	\$ 19,711,536
Standby letters of credit	94,303	104,908
	<u>\$ 15,003,691</u>	<u>\$ 19,816,444</u>

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 of the party. Collateral held varies, but may include accounts receivable, inventory, property and equipment, residential real estate 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. Those guarantees are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Collateral held varies as specified above and is required in instances which the Bank deems necessary.

Concentrations of Credit risk

Substantially all of the Bank's loans and commitments to extend credit have been granted to customers in the Bank's market area and such customers are generally depositors of the Bank. The concentrations of credit by type of loan are set forth in Note 5. The distribution of commitments to extend credit approximates the distribution of loans outstanding. The Bank's primary focus is toward consumer and small business transactions.

The Bank from time to time may have cash and cash equivalents on deposit with financial institutions that exceed federally-insured limits.

Other Commitments

The Bank has entered into employment agreements with certain officers covering duties, salary, benefits, and provisions for termination and Bank obligations in the event of merger or acquisition.

Notes to Financial Statements

Note 14. Regulatory Restrictions

Dividends

The Bank, as a North Carolina banking corporation, may pay dividends only out of undivided profits (retained earnings) as determined pursuant to North Carolina General Statutes Section 53-87. However, regulatory authorities may limit payment of dividends by any bank when it is determined that such a limitation is in the public interest and is necessary to ensure financial soundness of the bank.

Capital Requirements

The Bank is subject to various regulatory capital requirements administered by federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory (and possibly additional discretionary) actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. 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 Bank to maintain minimum amounts and ratios (set forth in the table below) of total Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets, as all those terms are defined in the applicable regulations. As of December 31, 2010 and 2009, the Bank met all capital adequacy requirements to which it was subject.

As of December 31, 2010, the most recent notification from the Federal Deposit Insurance Corporation categorized the Bank as well capitalized. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the following table. There are no conditions or events since the notification that management believes have changed the Bank's category.

The Bank's actual capital amounts and ratios are also presented in the table (dollars in thousands):

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
<i>December 31, 2010</i>						
Total Capital (to Risk-Weighted Assets)	\$ 17,202	16.1%	\$ 8,535	8.0%	\$ 10,669	10.0%
Tier 1 Capital (to Risk-Weighted Assets)	15,864	14.9%	4,268	4.0%	6,401	6.0%
Tier 1 Capital (to Average Assets)	15,864	11.2%	5,653	4.0%	7,066	5.0%
<i>December 31, 2009</i>						
Total Capital (to Risk-Weighted Assets)	\$ 16,900	15.0%	\$ 8,997	8.0%	\$ 11,247	10.0%
Tier 1 Capital (to Risk-Weighted Assets)	15,478	13.8%	4,499	4.0%	6,748	6.0%
Tier 1 Capital (to Average Assets)	15,478	11.3%	5,493	4.0%	6,866	5.0%

Notes to Financial Statements

Note 15. Transactions with Related Parties

The Bank has entered into transactions with its directors, significant shareholders and their affiliates (related parties). Such transactions were made in the ordinary course of business on substantially the same terms and conditions, including interest rates and collateral, as those prevailing at the time for comparable transactions with other customers, and did not in the opinion of management, involve more than normal credit risk or present other unfavorable features.

Aggregate loan transactions with related parties were as follows (in thousands):

	<u>2010</u>	<u>2009</u>
<i>Balance, beginning</i>	\$ 4,666	\$ 3,884
New loans and advances	891	2,167
Repayments	(1,146)	(1,385)
<i>Balance, ending</i>	<u>\$ 4,411</u>	<u>\$ 4,666</u>

The amount of deposits of related parties was \$2,896,410 at December 31, 2010 and \$2,746,478 at December 31, 2009.

ITEM 9 – CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

There were no changes in or disagreements with our accountants during the fiscal year ended December 31, 2010.

ITEM 9A – CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

At the end of the period covered by this report, the Bank carried out an evaluation, under the supervision and with the participation of the Bank's management, including the Bank's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Bank's disclosure controls and procedures pursuant to Securities Exchange Act Rule 13a-14.

Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Bank's disclosure controls and procedures were effective (1) to provide reasonable assurance that information required to be disclosed by the Bank in the reports filed or submitted by it under the Securities Exchange Act of 1934 was recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) to provide reasonable assurance that information required to be disclosed by the Bank in such reports is accumulated and communicated to the Bank's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow for timely decisions regarding required disclosure.

Management's Annual Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting for the Bank. The Bank's internal control over financial reporting is a process designed under the supervision of the Bank's Chief Executive Officer and Chief Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Bank's financial statements for external reporting purposes in accordance with U.S. generally accepted accounting principles. Management has made a comprehensive review, evaluation and assessment of the Bank's internal control over financial reporting as of December 31, 2010. In making its assessment of internal control over financial reporting, management used the criteria issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in "Internal Control – Integrated Framework". In accordance with Section 404 of the Sarbanes–Oxley Act of 2002, management makes the following assertions:

- Management has implemented a process to monitor and assess both the design and operating effectiveness of internal control over financial reporting.
- All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may be inadequate due to changes in conditions, or that the degree of compliance with policies or procedures may deteriorate.
- The Bank's management assessed the effectiveness of the Bank's internal control over financial reporting as of December 31, 2010. In making this assessment, it used criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in "Internal Control – Integrated Framework". Based on that assessment, we believe that, as of December 31, 2010, the Bank's internal control over financial reporting is effective based on those criteria.

This annual report does not include an attestation report of the Bank's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Bank's registered public accounting firm pursuant to an exemption from that requirement provided to smaller reporting companies such as the Bank.

Changes in Internal Control over Financial Reporting

Management of the Bank has evaluated, with the participation of the Bank's Chief Executive Officer and Chief Financial Officer, changes in the Bank's internal controls over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) of the Exchange Act) during the fourth quarter of 2010. In connection with such evaluation, the Bank has determined that there have been no changes in internal control over financial reporting during the fourth quarter that have materially affected or are reasonably likely to materially affect, the Bank's internal control over financial reporting.

ITEM 9B – OTHER INFORMATION

None.

PART III

ITEM 10 – DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Incorporated by reference from the discussion under the headings “Proposal 1: Election of Directors,” “Executive Compensation - Executive Officers,” “Director Relationships,” “Section 16(a) Beneficial Ownership Reporting Compliance” and “Meetings and Committees of the Board of Directors - Audit Committee” in the Registrant’s Proxy Statement for the 2011 Annual Meeting of Shareholders to be filed with the FDIC.

The Registrant has adopted a Code of Ethics that applies, among others, to its principal executive officer and principal financial officer. The Code of Ethics is available at <http://www.patriotstatebank.com>.

ITEM 11 – EXECUTIVE COMPENSATION

Incorporated by reference from the discussion under the headings “Executive Compensation”, and “Director Compensation” in the Registrant’s Proxy Statement for the 2011 Annual Meeting of Shareholders to be filed with the FDIC.

ITEM 12 – SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Incorporated by reference from the discussion under the heading “Beneficial Ownership of Voting Securities” in the Registrant’s Proxy Statement for the 2011 Annual Meeting of Shareholders to be filed with the FDIC.

Stock Option Plans

Set forth below is certain information regarding the Registrant’s various stock option plans.

EQUITY COMPENSATION PLAN INFORMATION

<u>Plan Category</u>	<u>Number of securities to be issued upon exercise of outstanding options, warrants, and rights</u> (a)	<u>Weighted-average exercise price of outstanding options, warrants, and rights</u> (b)	<u>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))</u> (c)
Equity compensation plans approved by security holders	266,759	\$ 10.96	86,241
Equity compensation plans not approved by security holders	-	-	-
Total	266,759	\$ 10.96	86,241

See additional information in Note 10 under the heading "Stock Based Compensation" in Item 8 of this annual report.

ITEM 13 – CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Incorporated by reference from the discussion under the headings “Director Independence” and “Indebtedness of and Transactions with Management” in the Registrant’s Proxy Statement for the 2011 Annual Meeting of Shareholders to be filed with the FDIC.

ITEM 14 – PRINCIPAL ACCOUNTANT FEES AND SERVICES

Incorporated by reference from the discussion under the heading “Proposal 2: Ratification of Independent Registered Public Accounting Firm” and “Audit Committee Report” in the Registrant’s Proxy Statement for the 2011 Annual Meeting of Shareholders to be filed with the FDIC.

ITEM 15 – EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) List of Documents Filed as Part of this Report

- (1) **Financial Statements.** The following financial statements are filed as a part of this report:

Report of Independent Registered Public Accounting Firm

Balance Sheets at December 31, 2010 and 2009

Statements of Operations for the periods ended December 31, 2010 and 2009

Statements of Changes in Stockholders' Equity for the periods ended December 31, 2010
and 2009

Statements of Cash Flows for the periods ended December 31, 2010 and 2009

Notes to Financial Statements

- (2) **Financial Statement Schedules.** All schedules for which provision is made in the applicable accounting regulations of the Securities and Exchange Commission are omitted because of the absence of conditions under which they are required or because the required information is included in the financial statements and related notes thereto.

- (3) **Exhibits.** The following exhibits are filed as part of this report:

3.1 Articles of Incorporation of Registrant (incorporated by reference from Exhibit 2.1 of Registrant's Form 10-SB dated April 27, 2007).

3.2 Bylaws of Registrant (incorporated by reference from Exhibit 3.2 of Registrant's Form 10-K for the fiscal year ended December 31, 2007).

4 Specimen of Stock Certificate (incorporated by reference from Exhibit 3.1 of Registrant's Form 10-SB dated April 27, 2007).

10.1 2007 Incentive Stock Option Plan including a form Incentive Stock Option Agreement (incorporated by reference from Exhibit 6.3 of Registrant's Form 10-SB dated April 27, 2007). *

10.2 2007 Nonstatutory Stock Option Plan including a form Nonstatutory Stock Option Agreement (incorporated by reference from Exhibit 6.4 of Registrant's Form 10-SB dated April 27, 2007). *

10.3 Employment Agreement dated August 21, 2006 with M. Gregg Strickland (incorporated by reference from Exhibit 10.3 of Registrant's Form 10-K for the fiscal year ended December 31, 2007). *

10.4 Employment Agreement dated August 21, 2006 with W. David Bell (incorporated by reference from Exhibit 10.4 of Registrant's Form 10-K for the fiscal year ended December 31, 2007). *

14 Code of Ethics (incorporated by reference from Exhibit 14 of Registrant's Form 10-K for the fiscal year ended December 31, 2007).

31.1 Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) (filed herewith)

31.2 Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) (filed herewith)

ITEM 15 – EXHIBITS AND FINANCIAL STATEMENT SCHEDULES (continued)

32.1 Certification by the Chief Executive Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)

32.2 Certification by the Chief Financial Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)

* Management contract or compensatory plan or arrangement

- (b) **Exhibits.** The exhibits required by Item 601 of Regulation S-K are either filed as part of this report or incorporated by reference herein.
- (c) **Financial Statements and Schedules Excluded from Annual Report.** There are no other financial statements and financial statement schedules which were excluded from the annual report to shareholders pursuant to Rule 14a-3(b) which are required to be included herein

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.

PATRIOT STATE BANK

Registrant

By: /s/ M. Gregg Strickland
M. Gregg Strickland
President & CEO

Date: March 28, 2011

Pursuant to the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

<u>/s/ D. Trent Weaver</u> D. Trent Weaver, Chairman	March 28, 2011
<u>/s/ W. David Bell</u> W. David Bell, Director, Executive Vice President	March 28, 2011
<u>/s/ Ronald T. Conner</u> Ronald T. Conner, Director	March 28, 2011
<u>/s/ Randy L. Dickens</u> Randy L. Dickens, Director	March 28, 2011
<u>/s/ Dennis E. Duke</u> Dennis E. Duke, Director	March 28, 2011
<u>/s/ Warren E. Gintis, DVM</u> Warren E. Gintis, DVM, Director	March 28, 2011
<u>/s/ Mike P. Hamby, DDS</u> Mike P. Hamby, DDS, Director	March 28, 2011
<u>/s/ Dwain K. Lanier</u> Dwain K. Lanier, Director	March 28, 2011
<u>/s/ David W. Ball</u> David W. Ball, Director	March 28, 2011
<u>/s/ Anita M. Pace</u> Anita M. Pace, Principal Financial Officer and Principal Accounting Officer	March 28, 2011
<u>/s/ M. Gregg Strickland</u> M. Gregg Strickland, Director, President & CEO	March 28, 2011

EXHIBIT INDEX

<u>Exhibit Number</u>	<u>Exhibit</u>	<u>Page Number</u>
3.1	Articles of Incorporation	*
3.2	Bylaws	*
4	Specimen of Stock Certificate	*
10.1	2007 Incentive Stock Option Plan including a form Incentive Stock Option Agreement	*
10.2	2007 Nonstatutory Stock Option including a form Nonstatutory Stock Option Agreement	*
10.3	Employment Agreement dated August 21, 2007 with M. Gregg Strickland	*
10.4	Employment Agreement dated August 21, 2007 with W. David Bell	*
14	Code of Ethics	*
31.1	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a)	Filed herewith
31.2	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a)	Filed herewith
32.1	Certification by the Chief Executive Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith
32.2	Certification by the Chief Financial Officer pursuant to 18 U.S.C. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith

* Incorporated by reference

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER

Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, M. Gregg Strickland, certify that:

- (1) I have reviewed this annual report on Form 10-K of Patriot State Bank, a North Carolina bank (the "Registrant");
- (2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
- (4) The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (the Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and
- (5) The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Date: March 28, 2011

/s/ M. Gregg Strickland
M. Gregg Strickland
President and Chief Executive Officer

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER

Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Anita M. Pace, certify that:

- (1) I have reviewed this annual report on Form 10-K of Patriot State Bank, a North Carolina bank (the "Registrant");
- (2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
- (4) The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (the Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and
- (5) The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Date: March 28, 2011

/s/ Anita M. Pace
Anita M. Pace
Chief Financial Officer

Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

The undersigned hereby certifies that, to his or her knowledge, (i) the Form 10-K filed by Patriot State Bank (the "Issuer") for the year ended December 31, 2010, fully complies with the requirements of Section 13 (a) or 15 (d) of the Securities Exchange Act of 1934 and (ii) the information contained in that report fairly presents, in all material respects, the financial condition and results of operations of the Issuer on the dates and for the periods presented therein.

Date: March 28, 2011

/s/ M. Gregg Strickland
M. Gregg Strickland
President and Chief Executive Officer

Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

The undersigned hereby certifies that, to his or her knowledge, (i) the Form 10-K filed by Patriot State Bank (the "Issuer") for the year ended December 31, 2010, fully complies with the requirements of Section 13 (a) or 15 (d) of the Securities Exchange Act of 1934 and (ii) the information contained in that report fairly presents, in all material respects, the financial condition and results of operations of the Issuer on the dates and for the periods presented therein.

Date: March 28, 2011

/s/ Anita M. Pace _____
Anita M. Pace
Chief Financial Officer