

The logo for Freedom Bank features a dark blue vertical bar on the left side of the page. A thin gold horizontal line is positioned below the text 'FREEDOM BANK'. Two parallel gold curved lines sweep from the bottom left towards the top right, framing the text. The text 'FREEDOM BANK' is written in a dark blue, serif font with a thin gold underline.

FREEDOM BANK

Annual Report

2010

A solid gold horizontal bar spans the entire width of the page at the bottom.



# FREEDOM BANK

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# FREEDOM BANK

## MANAGEMENT DISCUSSION

We are very pleased to report that Freedom Bank of Virginia posted Net Income of \$2,433,514 in 2010. The audited results include income of \$1,821,514, before Income Taxes and a \$612,000 tax benefit derived from a tax loss carry forward. Quarterly Net Income for the 4 quarters in 2010 was \$362,253 in the 1<sup>st</sup> quarter, \$457,498 in the 2<sup>nd</sup> quarter, \$561,600 in the 3<sup>rd</sup> quarter, and \$1,052,163, including the tax benefit, in the 4<sup>th</sup> quarter. Freedom Bank has posted profits in each of the preceding seven quarters, after taking a \$3,810,744 Provision for Loan Losses in the 1<sup>st</sup> quarter, 2009.

Interest Income totaled \$9,155,929 in 2010, compared to \$8,199,336 in 2009. Interest Expense was \$2,197,618 in 2010, compared to \$2,879,159 in 2009. The combination of these two factors, a \$956,593 increase in interest income and a \$681,542 decrease in interest expense combined to increase net interest income by \$1,638,135. The principal driver of higher interest income was increased loans outstanding, but the principal driver of lower interest expense was a decreased interest rate on deposits.

The Provision for Possible Loan Losses improved significantly with \$200,000 recorded for the year ending December 31, 2010, compared to \$4,435,744 for the year ending December 31, 2009. The large Provision taken in the 1<sup>st</sup> quarter, 2009 overshadowed the net operating profit for the remainder of the year. The Bank was profitable each of the remaining quarters of 2009 and each quarter in 2010. The 2009 Provision reflected deteriorating conditions in the economy and heightened concerns about borrower's credit worthiness. By 2010, the Bank witnessed lower loan delinquencies and non-performing loans and was able to decrease the amount of Provision for Possible Loan Losses. The Bank had no foreclosures in 2010.

Other Income in 2010 totaled \$548,428, compared to \$572,448 in 2009. The Bank did not have any gain on sale of real estate in 2010, compared to \$462,621 in 2009. The Bank did not hold any OREO property in 2010.

Total Operating Expense was \$5,485,225 as of December 31, 2010, compared to \$5,550,037 as of December 31, 2009. A decrease in legal and professional fees by 85% from 2009 to 2010 was the key performance improvement factor.

For the year ended December 31, 2010, the Bank's Net Income per Share was \$1.03, compared to a Net Loss per Share of \$1.54 for the year ended December 31, 2009.

### Financial Condition

Cash, Federal Funds Sold and Investment Securities are primary and secondary sources of liquidity to meet obligations as they come due and are sources of funds for growth of loans outstanding. As of December 31, 2010, these assets totaled \$28,425,469. Liquid assets were 16.6% of Total Assets. On December 31, 2009, the Bank held \$20,863,589 in Cash, Federal Funds and Investment Securities, 13.3% of Total Assets. The Bank owned \$615,600 of Federal Reserve Bank Stock at December 31, 2010, compared to \$556,400 at the end of 2009. These assets do not produce as much income as loans; however, liquidity is paramount in a time of economic uncertainty.

Loans Receivable ended 2010, at \$141,067,476, compared to \$135,400,086 at the end of 2009. The 4.2% increase in loans outstanding was underscored by extraordinary repayments of previously originated loans. In general, many borrowers managed their own liquidity and market risk by reducing debt and as a result, it was very difficult to grow the loans outstanding.

Other Assets including Premises and Equipment, Accrued Interest, Other Receivables, Other Assets, and Deferred Tax Asset totaled \$2,976,926 as of December 31, 2010, compared to \$2,369,485 as of December 31, 2009.

Total Deposits increased to \$149,122,963 on December 31 2010, up from \$137,431,805 on December 31, 2009. The \$11.7 million deposit increase included \$6.7 million in Time Deposits and \$5.0 million in Transaction Account Deposits. During 2010, the Bank achieved the goal of reducing its level of non-core deposits by replacing them with local, core deposits.

Total Stockholder's Equity at December 31, 2010 was \$21,575,018, compared to \$19,059,028 on December 31, 2009, an increase of 13.20%. Book value per share was \$9.15 at December 31, 2010. The Bank retained 100% of its Net Income, including the tax benefit described earlier.

Capital remains strong with all capital ratios remaining above the "Well Capitalized" regulatory definitions. As of December 31, 2010, Tier 1 Leverage Ratio was 12.35%, more than double the ratio considered by regulators to be "Well Capitalized". Tier 1 Risk Based Capital Ratio was 14.85%, more than 8% higher than the regulatory guidelines and the Tier 2 Risk Based Capital Ratio was 16.05%, well above the 10% regulatory position.

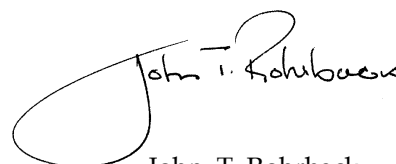
During 2010, a management succession plan was prepared for the Board to address the growth and attrition needs of the Bank. The Plan identified successors for key manager positions when internal candidates were available and positions which would require external recruiting if vacated. It also addressed job specialization which may require dividing some officer's responsibilities into separate positions and the training needs of internal candidates for succession to greater responsibilities. The Plan was activated on September 1, 2010 when President and CEO John T. Rohrback divided his responsibilities and named Craig S. Underhill to the responsibility of President.

Since its founding in 2001, Freedom Bank utilized the services of Fidelity Information Services (FIS) as the Bank's main data processor. The Bank used a software application called "Premier". Premier was the core system for all of our deposit and loan functions. FIS operated the Premier application under a license from the software owner. In May, 2010, FIS was notified that its license to operate Premier would not be renewed and it could not offer the software to its clients after the license expiration date. In order to minimize the impact of this change, the Bank contracted with nationally recognized, Fiserv, to provide the Bank's data processing. By moving the Bank's data processing to Fiserv, we utilized the same core operating system as used previously and minimized the impact of the change from one data processor to another. This change entailed a "migration" process from FIS to Fiserv that was carried out with great care and advance planning. Upon completion of the migration, many of our customers commented that they did not realize the change had taken place. Our customers have access to their account information at any time, any place. Our "eBanking" services which include online banking, remote capture, e-statements and bill pay make banking a breeze and give our customers a greater control over their finances.

The Board of Directors and management are very gratified to report these results to our shareholders.



Richard C. Litman  
Chairman of the Board



John T. Rohrback  
CEO

# THOMPSON, GREENSPON & CO., P.C.

Certified Public Accountants  
Management Consultants

## INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholders  
The Freedom Bank of Virginia  
Vienna, Virginia

We have audited the accompanying balance sheets of The Freedom Bank of Virginia as of December 31, 2010 and 2009, and the related statements of operations, changes in stockholders' equity and cash flows for the years then ended. 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 auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe 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 The Freedom Bank of Virginia as of December 31, 2010 and 2009, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.



Fairfax, Virginia  
March 28, 2011

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## BALANCE SHEETS

DECEMBER 31, 2010 AND 2009

2010

2009

**ASSETS**

Cash and Due from banks	\$ 3,441,325	\$ 1,375,127
Federal Funds sold	17,212,000	10,824,000
Securities Available-for-Sale	5,767,655	4,631,602
Securities Held-to-maturity	2,004,489	4,032,860
Federal Reserve Bank Stock, at cost	615,600	556,400
Loans Receivable	141,067,476	135,400,086
Allowance for Possible Loan Losses	(1,735,353)	(1,907,853)
Net Loans	139,332,123	133,492,233
Bank Premises and Equipment, net	315,774	429,828
Accrued interest receivable	517,293	483,510
Deferred Tax Asset	612,000	-
Other assets	1,531,859	1,456,147
<b>Total Assets</b>	<b>\$ 171,350,118</b>	<b>\$ 157,281,707</b>

**LIABILITIES AND STOCKHOLDERS' EQUITY****Liabilities**

## Demand deposits

Non-interest bearing

\$ 29,797,798 \$ 27,796,586

Interest bearing

19,039,135 16,257,975

Savings deposits

830,262 660,759

Time deposits

99,455,768 92,716,485

Total Deposits

149,122,963 137,431,805

Other accrued expenses

580,902 699,778

Accrued interest payable

71,235 91,096

Total Liabilities

149,775,100 138,222,679

**Stockholders' Equity**

Common stock, \$5 par value, 5,000,000 shares authorized:

2,357,361 shares issued and outstanding, 2010 &amp; 2009

11,786,805 11,786,805

Additional paid-in capital

16,042,863 16,002,413

Accumulated other comprehensive income

86,159 44,133

Retained earnings (deficit)

(6,340,809) (8,774,323)

Total Stockholders' Equity

21,575,018 19,059,028

**Total Liabilities and Stockholders' Equity****\$ 171,350,118 \$ 157,281,707**

**THE FREEDOM BANK OF VIRGINIA**

**STATEMENTS OF OPERATIONS**

YEARS ENDED DECEMBER 31, 2010 AND 2009

2010

2009

**Interest Income**

Interest and fees on loans	\$ 8,730,192	\$ 7,655,791
Interest on investment securities	379,702	518,444
Interest on Federal Funds sold	46,035	25,101
	9,155,929	8,199,336

**Interest Expense**

Interest on deposits	2,197,618	2,879,159
	6,958,311	5,320,177

**Provision for Possible Loan Losses**

	200,000	4,435,744
	6,758,311	884,433

Net Interest Income after

Provision for Possible Loan Losses

**Other Income**

Service charges and other income	548,428	572,448
Gain on sale of other real estate owned	-	462,621
	548,428	1,035,069

**Operating Expenses**

Officers and employee compensation and benefits	3,156,155	2,848,087
Occupancy expense	544,326	503,075
Equipment and depreciation expense	234,641	230,639
Insurance expense	332,217	276,562
Professional fees	101,590	701,280
Data and item processing	525,559	466,695
Business development	109,202	69,271
Franchises tax	202,136	220,144
Other operating expenses	279,399	234,284
	5,485,225	5,550,037

Income (Loss) before Income Taxes

**Income Tax (Benefit) Expense**

	(612,000)	-
	-	-

**Net Income (Loss)**

	\$ 2,433,514	\$ (3,630,535)
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**Net Income (Loss) Per Common Share**

	\$ 1.03	\$ (1.54)
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**Net Income (Loss) Per Diluted Share**

	\$ 1.03	\$ (1.54)
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*The Notes to Financial Statements are an integral part of these statements.*

**STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
**YEARS ENDED DECEMBER 31, 2010 AND 2009**

	Shares of Common Stock	Common Stock	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Deficit)	Retained Earnings (Deficit)	Total Stockholders' Equity
Balance, December 31, 2008	2,357,361	\$ 11,786,805	\$ 16,002,413	\$ 59,894	\$ (5,143,788)	\$ 22,705,324
Comprehensive Income (Loss):						
Net Loss	-	-	-	-	(3,630,535)	(3,630,535)
Change in unrealized gain (loss) on securities available- for-sale, net of tax of \$8,486	-	-	-	(15,761)	-	(15,761)
Total Comprehensive Income (Loss)						(3,646,296)
Balance, December 31, 2009	2,357,361	11,786,805	16,002,413	44,133	(8,774,323)	19,059,028
Comprehensive Income (Loss):						
Net Income	-	-	-	-	2,433,514	2,433,514
Change in unrealized gain (loss) on securities available- for-sale, net of tax of \$22,629	-	-	-	42,026	-	42,026
Total Comprehensive Income						2,475,540
Stock based compensation	-	-	40,450	-	-	40,450
Balance, December 31, 2010	<u>2,357,361</u>	<u>\$ 11,786,805</u>	<u>\$ 16,042,863</u>	<u>\$ 86,159</u>	<u>\$ (6,340,809)</u>	<u>\$ 21,575,018</u>

## STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2010 AND 2009

2010

2009

**Cash Flows from Operating Activities**

Net Income (loss)	\$ 2,433,514	\$ (3,630,535)
Noncash items included in net income (loss)		
Depreciation and amortization	155,620	166,947
Provision for possible loan losses	200,000	4,435,744
Net amortization of securities	42,347	27,848
Stock-based compensation expense	40,450	-
Gain on other real estate	-	(462,621)
Deferred income tax benefit	(612,000)	-
(Increase) Decrease in		
Accrued interest receivable	(33,783)	(64,965)
Other assets	(75,712)	(1,194,773)
Increase (Decrease) in		
Other accrued expenses	(141,505)	316,849
Accrued interest payable	(19,861)	(112,073)
Net Cash Provided (Used) by Operating Activities	<u>1,989,070</u>	<u>(517,579)</u>

**Cash Flows from Investing Activities**

Federal Funds sold, net	(6,388,000)	663,000
Loan originations, net	(6,039,890)	(19,826,199)
Purchase of available-for-sale securities	(2,327,573)	(3,935,363)
Maturities, calls and paydowns of securities available-for-sale	1,209,575	1,836,526
Paydowns of held-to-maturity securities	2,032,624	3,092,694
Purchase of Federal Reserve Bank Stock	(59,200)	(10,800)
Acquisition of bank equipment	(41,566)	(61,127)
Proceeds from sale of other real estate	-	2,250,833
Proceeds from redemption of Federal Reserve Bank Stock	-	167,200
Net Cash Used by Investing Activities	<u>(11,614,030)</u>	<u>(15,823,236)</u>

**Cash Flows from Financing Activities**

Increase in deposits, net	<u>11,691,158</u>	<u>16,531,342</u>
Net Cash Provided by Financing Activities	<u>11,691,158</u>	<u>16,531,342</u>

**Net Increase in Cash and Due from Banks**

2,066,198 190,527

**Cash and Due from Banks, beginning of year**1,375,127 1,184,600**Cash and Due from Banks, end of year**\$ 3,441,325 \$ 1,375,127**Noncash Investing Activity**

Unrealized gain (loss) on securities available-for-sale, net	<u>\$ 42,026</u>	<u>\$ (15,761)</u>
Transfer of loans to other real estate owned	<u>\$ -</u>	<u>\$ 1,082,883</u>

**Supplemental Information**

Cash paid during the year for interest	<u>\$ 2,217,479</u>	<u>\$ 2,991,232</u>
Cash paid during the year for income taxes	<u>\$ -</u>	<u>\$ -</u>

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

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2010 AND 2009

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**1. NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accounting and reporting policies of The Freedom Bank of Virginia (the Bank) conform to generally accepted accounting principles (GAAP) and reflect practices of the banking industry. The policies are summarized below.

**Nature of Operations**

The Freedom Bank of Virginia is a state chartered bank and a member of the Federal Reserve and is subject to the rules and regulations of the Virginia State Banking Commission, the Federal Reserve and the Federal Deposit Insurance Corporation (FDIC). The Bank provides banking services at its branch offices in Vienna and Fairfax, Virginia, and serves customers primarily in the Northern Virginia area. The Bank was in organization during the period January 27, 2000 through July 22, 2001, and opened for business on July 23, 2001.

**Use of Estimates**

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

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

**Securities**

Debt securities are classified as held-to-maturity when the Bank has the positive intent and ability to hold the securities to maturity. Securities held-to-maturity are carried at amortized cost.

Debt securities not classified as held-to-maturity or trading securities are classified as available-for-sale. Securities available-for-sale are carried at fair value with unrealized gains and losses reported in other comprehensive income. Realized gains (losses) on securities available-for-sale are included in other income (expense) and, when applicable, are reported as a reclassification adjustment, net of tax, in other comprehensive income.

The amortization of premiums and accretion of discounts are recognized in interest income using methods approximating the interest method over the period to maturity. Declines in the fair value of individual held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary result in write-downs of the individual securities to their fair value. The related write-downs are included in earnings as realized losses. Gains and losses on sales of securities are recorded on the trade date and are determined using the specific-identification method.

Federal Reserve stock is considered a restricted investment security, is carried at cost and evaluated annually for impairment. The stock is required in order to be a member of the Federal Reserve.

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2009 AND 2008

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**Loans and Loan Fees**

Loans that management has the intent and ability to hold for the foreseeable future, or until maturity or pay-off, generally are stated at the principal amount outstanding, less the allowance for loan losses and net deferred loan fees. Interest on loans is generally computed using the simple interest method.

Loan origination and commitment fees, as well as certain direct origination costs, are deferred and amortized as a yield adjustment over the lives of the related loans using the interest method. Amortization of deferred loan fees is discontinued when a loan is placed on non-accrual status.

The accrual of interest on mortgage and commercial loans is discontinued at the time the loan is 90 days delinquent unless the credit is well secured and in process of collection. Other personal loans are typically charged off no later than 180 days past due. In all cases, loans are placed on non-accrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

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

**Loans Held for Sale**

Loans held for sale consist primarily of residential mortgage loans, which are secured by one-to-four family residential real estate. Loans held for sale are carried at the lower of aggregate cost, net of purchase discounts or premiums, deferred fees, and deferred origination costs, or fair value. The Bank determines the fair value of loans held for sale using current secondary market prices for loans with similar coupons, maturities and credit quality. The fair value of mortgage loans is subject to change primarily due to changes in market interest rates. Loans held for sale totaled approximately \$993,000 and \$390,000 as of December 31, 2010 and 2009, respectively, and are included in loans receivable in the financial statements.

**Allowance for Loan Losses**

The allowance for loan losses is maintained at a level that, in management's judgment, is adequate to absorb credit losses inherent in the loan portfolio. The amount of the allowance is based on management's evaluation of the collectability of the loan portfolio, including the nature of the portfolio, credit concentrations, trends in historical loss experience, specific impaired loans, economic conditions, and other risks inherent in the portfolio.

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. Allowances for impaired loans are generally determined based on collateral values or the present value of estimated cash flows. Although management uses available information to recognize losses on loans, because of uncertainties associated with local economic conditions, collateral values, and future cash flows on impaired loans, it is reasonably possible that a material change could occur in the allowance for loan losses in the near term. However, the amount of the change that is reasonably possible cannot be estimated. The allowance is increased by a provision for loan losses, which is charged to expense and reduced by charge-offs, net of recoveries. Changes in the allowance relating to impaired loans are charged or credited to the provision for loan losses. Past due status is determined based on contractual terms.

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2010 AND 2009

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**Bank Premises and Equipment**

Bank premises and equipment are stated at cost, less accumulated depreciation and amortization. Leasehold improvements are amortized over the shorter of the asset life or lease term using the straight-line method. Furniture and equipment are depreciated over estimated useful lives of three to seven years using the straight-line method. The Bank depreciates premises and equipment using accelerated methods for income tax reporting.

Expenditures for maintenance, repairs and improvements that do not materially extend the useful lives of bank premises and equipment are charged to earnings. When bank premises or equipment is sold or otherwise disposed of, the cost and related accumulated depreciation or amortization are removed from the accounts, and the effect is reflected in current earnings.

Leases that meet certain specified criteria are accounted for as capital assets and liabilities, and those not meeting the criteria are accounted for as operating leases.

**Other Real Estate Owned**

Real estate properties acquired through or in lieu of loan foreclosures are initially recorded at the fair value less estimated selling cost at the date of foreclosure. Any write-downs based on the asset's fair value at the date of acquisition are charged to the allowance for loan losses. After foreclosure, valuations are periodically performed by management and property held for sale is carried at the lower of the new cost basis or fair value less cost to sell. Impairment losses on property to be held and used are measured as the amount by which the carrying amount of a property exceeds its fair value. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. The portion of interest costs relating to development of real estate is capitalized. Valuations are periodically performed by management, and any subsequent write-downs are recorded as a charge to operations, if necessary, to reduce the carrying value of a property to the lower of its cost or fair value less cost to sell. The Bank owned no other real estate at December 31, 2010 and 2009.

**Other Assets**

Included in other assets is approximately \$933,000 and \$1,207,000 as of December 31, 2010 and 2009, respectively, of prepaid expense related to the required prepayment of the FDIC premium through the fourth quarter of 2012.

**Stockholders' Equity**

At December 31, 2010, warrants were outstanding and exercisable to purchase 232,089 shares of common stock at \$13.25 per share if exercised by January 15, 2015, and 44,899 shares of common stock at \$13.25 per share if exercised by February 16, 2015.

Comprehensive income (loss) represents all changes in equity that result from recognized transactions and other economic events of the period. Other comprehensive income (loss) refers to revenues, expenses, gains and losses that under accounting principles generally accepted in the United States of America are included in comprehensive income but excluded from net income, such as unrealized gains and losses on certain investments in debt and equity securities.

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2010 AND 2009

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**Income Taxes**

Income taxes are provided for the tax effects of the transactions reported in the financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the basis of the net operating losses carryforward and allowance for loan losses. The deferred tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred tax assets and liabilities are reflected at income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

Management has determined that recent profitability and projections of future taxable income will be adequate to absorb a portion of the Bank's net operating loss carryforward included in the deferred tax asset. Therefore, \$612,000 of the valuation allowance taken against the deferred tax asset was reversed in December 2010, resulting in the net tax benefit shown in the table in Note 8.

The Bank files an income tax return in the U.S. Federal jurisdiction. The Bank pays state franchise tax in lieu of state income taxes. Currently, the 2009, 2008 and 2007 income tax returns are open and subject to examination. The Bank is not currently under audit by any income tax jurisdictions.

The Bank has no uncertain tax positions that qualify for either recognition or disclosure in the financial statements, and no interest and penalties have been recorded in the accompanying financial statements related to uncertain tax positions.

**Earnings per Share (EPS)**

Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for the year. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Bank. The Bank does not have any contracts or options with a dilutive effect; therefore, basic EPS and diluted EPS are equal.

**Stock-Based Compensation**

The Bank recognizes the cost of employee services received in exchange for an award of equity instruments in the financial statements over the period the employee is required to perform the services in exchange for the award (presumptively the vesting period). The Bank also measures the cost of employee services received in exchange for an award based on the grant-date fair value of the award.

**Employment Contracts**

In August 2010, the Bank entered into an employment agreement with the Bank's current President. The agreement provides for a base salary, a performance bonus, annual adjustments to compensation and other benefits. The agreement has an initial term of 17 months and will be automatically renewed for successive 12 month terms until employment is terminated under specific conditions as provided in the agreement.

The Bank has also entered into employment agreements with certain other key employees. The agreements provide for base salary, performance bonuses and other benefits. The terms of the agreements range from one to two years with options to extend for additional one year periods until employment is terminated under specific conditions as provided in the agreements.

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2010 AND 2009

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**Statements of Cash Flows**

The Bank considers all cash and amounts due from depository institutions, excluding interest-bearing deposits in other banks and Federal funds sold, to be cash equivalents for purposes of the statements of cash flows. The Freedom Bank of Virginia periodically has bank deposits, including short-term investments, in excess of Federally insured limits.

**Off-Balance Sheet Credit Related Financial Instruments**

In the ordinary course of business, the Bank has entered into commitments to extend credit, including commitments under credit card arrangements, commercial letters of credit, and standby letters of credit. Such financial instruments are recorded when they are funded.

**Subsequent Events**

The date to which events occurring after December 31, 2009, the date of the most recent balance sheet, have been evaluated for possible adjustment to the financial statements or disclosure is March 4, 2010, which is the date on which the financial statements were issued.

**Adoption of New Accounting Standards**

Accounting Standards Update (ASU) 2009-16, *Accounting for Transfers of Financial Assets*, provides guidance to improve the relevance, representational faithfulness, and comparability of the information that an entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. ASU 2009-16 was effective for transfers on or after January 1, 2010.

ASU 2010-06, *Fair Value Measurements and Disclosures, Improving Disclosures about Fair Value Measurements* provides amendments that clarify existing disclosures and requires certain new disclosures. The update is effective for interim and annual reporting periods beginning after December 15, 2009, except for disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years.

The above recently adopted accounting standards did not have a material impact on the Bank's financial statements.

**Adoption of New Accounting Standards**

ASU 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses* expands disclosures to require an entity to disaggregate by portfolio segment or class certain existing disclosures and provide certain new disclosures about its financing receivables and related allowance for credit losses. The disclosures are effective for annual reporting periods ending on or after December 15, 2011.

The adoption of the new standard is not expected to have a material impact on the Bank's financial statements.

NOTES TO FINANCIAL STATEMENTS  
YEARS ENDED DECEMBER 31, 2010 AND 2009

2. RESTRICTION OF CASH AND DUE FROM BANKS

The Bank is required to maintain reserve funds in cash or on deposit with the Federal Reserve. The required reserve at December 31, 2010 and 2009 was \$622,000 and \$606,000, respectively.

3. SECURITIES AVAILABLE-FOR-SALE AND HELD-TO-MATURITY

The amortized cost and fair values of securities as shown in the balance sheets of the Bank are as follows:

	Amortized Costs	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2010				
<u>Available-for-sale</u>				
U.S. Government and				
Agency securities	\$ 1,000,000	\$ 77,624	\$ -	\$ 1,077,624
Corporate securities	1,097,819	46,833	(2,716)	1,141,936
Mortgage backed securities	3,537,284	35,466	(24,655)	3,548,095
Total Available-for-sale	<u>5,635,103</u>	<u>159,923</u>	<u>(27,371)</u>	<u>5,767,655</u>
<u>Held-to-maturity</u>				
Mortgage backed securities	<u>2,004,489</u>	<u>51,915</u>	<u>-</u>	<u>2,056,404</u>
Total Investment Securities	<u>\$ 7,639,592</u>	<u>\$ 211,838</u>	<u>\$ (27,371)</u>	<u>\$ 7,824,059</u>
December 31, 2009				
<u>Available-for-sale</u>				
U.S. Government and				
Agency securities	\$ 1,000,000	\$ 62,870	\$ -	\$ 1,062,870
Corporate securities	1,587,528	56,006		1,643,534
Mortgage backed securities	1,976,176	-	(50,978)	1,925,198
Total Available-for-sale	<u>4,563,704</u>	<u>118,876</u>	<u>(50,978)</u>	<u>4,631,602</u>
<u>Held-to-maturity</u>				
Mortgage backed securities	<u>4,032,860</u>	<u>96,122</u>	<u>-</u>	<u>4,128,982</u>
Total Investment Securities	<u>\$ 8,596,564</u>	<u>\$ 214,998</u>	<u>\$ (50,978)</u>	<u>\$ 8,760,584</u>

The amortized cost and estimated fair value of debt securities at December 31, 2010, by contractual maturity, are as follows:

	Available-for-sale		Held-to-maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Amounts maturing in:				
1 year or less	\$ -	\$ -	\$ -	\$ -
After 1 year - 5 years	1,847,819	1,972,276	-	-
After 5 years - 10 years	-	-	-	-
After 10 years	250,000	247,284	-	-
	<u>2,097,819</u>	<u>2,219,560</u>	<u>-</u>	<u>-</u>
Mortgage backed securities	3,537,284	3,548,095	2,004,489	2,056,404
	<u>\$ 5,635,103</u>	<u>\$ 5,767,655</u>	<u>\$ 2,004,489</u>	<u>\$ 2,056,404</u>

**NOTES TO FINANCIAL STATEMENTS**  
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Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

At December 31, 2010 and 2009, U.S. Government obligations with a carrying value of \$4,426,044 and \$4,626,677, respectively, were pledged to secure public deposits and for other purposes required or permitted by law.

Information pertaining to securities with gross unrealized losses at December 31, 2010, aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
<u>Available-for-sale</u>				
Mortgage backed securities	\$ 24,655	\$ 1,999,125	\$ -	\$ -
Corporate securities	\$ 2,716	\$ 247,284	\$ -	\$ -
<u>Held-to-maturity</u>				
Mortgage backed securities	\$ -	\$ -	\$ -	\$ -

Management evaluates securities for other-than-temporary impairment on at least 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 the 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.

At December 31, 2010, three debt securities with an unrealized loss depreciated one percent from the Bank amortized cost basis. The securities are secured by mortgage loans or are corporate bonds. These unrealized losses relate principally to current interest rates for similar types of securities. In analyzing an issuer's financial condition, management considers whether the securities are issued by the Federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. As management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available-for-sale, management feels that the unrealized losses on the securities are not deemed to be other-than-temporary.

NOTES TO FINANCIAL STATEMENTS  
YEARS ENDED DECEMBER 31, 2010 AND 2009

#### 4. LOANS RECEIVABLE

Loans receivable include the following:

	2010	2009
Commercial	\$ 32,103,239	\$ 36,190,011
Consumer and other	2,107,038	2,948,806
Loans held for sale	992,551	390,300
Real estate	106,177,212	96,152,302
Subtotal	<u>141,380,040</u>	<u>135,681,419</u>
Deferred loan fees	(312,564)	(281,333)
Totals	<u>\$ 141,067,476</u>	<u>\$ 135,400,086</u>

An analysis of the allowance for possible loan losses is as follows:

	2010	2009
Balance, beginning of period	\$ 1,907,853	\$ 2,276,824
Provision for loan losses	200,000	4,435,744
Loans charged to reserve	(682,061)	(4,969,969)
Recoveries credited to reserve	309,561	165,254
Totals	<u>\$ 1,735,353</u>	<u>\$ 1,907,853</u>

At December 31, 2010 and 2009, the total recorded investment in loans on nonaccrual amounted to approximately \$2,299,000 and \$4,271,000, respectively. There were no loans past due 90 days or more and still accruing interest at December 31, 2010. At December 31, 2010 and 2009, the total recorded investment in impaired loans, all of which had allowances determined in accordance with GAAP, amounted to approximately \$2,299,000 and \$4,314,000, respectively. The average recorded investment in impaired loans amounted to approximately \$3,306,000 and \$4,758,000 for the years ended December 31, 2010 and 2009, respectively. There is no specific allowance for impaired loans at December 31, 2010. The allowance for loan losses related to impaired loans amounted to approximately \$278,000 at December 31, 2009. Interest income on impaired loans of approximately \$2,000 and \$95,000 was recognized for cash payments received in 2010 and 2009, respectively. No additional funds are committed to be advanced in connection with the impaired loans.

The Bank has entered into transactions with certain directors, executive officers, significant stockholders and their affiliates. 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 same 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. The aggregate amount of loans outstanding to such related parties was \$3,636,656 and \$5,181,156 at December 31, 2010 and 2009, respectively. New loans made to such related parties including loans held by new directors, amounted to \$1,354,811 and \$3,204,473 and payments amounted to \$2,899,311 and \$1,527,198 at December 31, 2010 and 2009, respectively.

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2010 AND 2009

**5. BANK PREMISES AND EQUIPMENT**

Bank premises and equipment include the following:

	2010	2009
Furniture and equipment	\$ 1,077,548	\$ 1,064,625
Leasehold improvements	130,959	130,959
Software	300,562	300,562
Total Cost	1,509,069	1,496,146
Less accumulated depreciation	(1,193,295)	(1,066,318)
Net Bank Premises and Equipment	<u>\$ 315,774</u>	<u>\$ 429,828</u>

Depreciation of bank premises and equipment charged to expense amounted to \$155,620 and \$166,947 in 2010 and 2009, respectively.

**6. DEPOSITS**

Time deposits in denominations of \$100,000 or more totaled \$61,346,589 and \$59,202,651 at December 31, 2010 and 2009, respectively.

At December 31, 2010, the following are time deposits maturing in years ending December 31:

2011	\$ 67,709,760
2012	28,286,768
2013	1,160,979
2014	739,933
2015 and thereafter	1,558,328
	<u>\$ 99,455,768</u>

The Bank held related party deposits of approximately \$4,894,000 and \$4,602,000 at December 31, 2010 and 2009, respectively.

**7. BORROWINGS**

At December 31, 2010, the Bank had \$2,100,000 available under a line of credit Fed Funds facility to be used for temporary, short-term needs with borrowing not to exceed seven consecutive business days. There were no borrowings on this line at December 31, 2010 and 2009.

At December 31, 2010, the Bank had an additional \$2,000,000 available under a line of credit Fed Funds facility to be used for temporary, short-term needs with borrowings not to exceed 30 consecutive calendar days. There were no borrowings on this line at December 31, 2010 and 2009.

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2010 AND 2009

**8. INCOME TAXES**

Significant components of deferred income tax assets and liabilities are as follows at December 31:

Deferred Source	2010	2009
Net operating loss carryforward	\$ 1,043,000	\$ 1,784,000
Loan loss reserve	1,033,000	1,104,000
Other	-	12,000
Unearned loan fees	106,000	96,000
Depreciation	(22,000)	(26,000)
Gross deferred tax assets	2,160,000	2,970,000
Valuation Allowance	(1,548,000)	(2,970,000)
Net deferred tax asset	<u>\$ 612,000</u>	<u>\$ -</u>

The Bank has net operating losses carried forward of approximately \$3,068,000 at December 31, 2010, which start to expire in 2022.

The provision for income taxes consists of the following at December 31:

	2010	2009
Current tax expense	\$ -	\$ -
Deferred tax expense	810,000	-
Change in valuation allowance	(1,422,000)	-
	<u>\$ (612,000)</u>	<u>\$ -</u>

The following is a reconciliation of the federal statutory income tax rate to the effective tax rate as a percent of pre-tax income for the years ended December 31:

	2010	2009
Federal statutory rate	34 %	34 %
Permanent differences	1	-
Change in valuation allowance	(69)	-
Effective tax rate	<u>(34) %</u>	<u>34 %</u>

**9. CAPITAL REQUIREMENTS**

The Bank is subject to various regulatory capital requirements administered by the Federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the 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 their assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification under the prompt corrective action guidelines 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 of total risk-based capital and Tier 1 capital to risk-weighted assets (as defined in the regulations), and Tier 1 capital to adjusted total assets (as defined).

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2010 AND 2009

Management believes, as of December 31, 2010, that the Bank meets all the capital adequacy requirements to which it is subject.

As of December 31, 2010, the Bank was categorized as well capitalized under the regulatory framework for prompt corrective action. To remain categorized as well as capitalized, the Bank will have to maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as disclosed in the following table. There are no conditions or events since the most recent notification that management believes have changed the Bank's prompt corrective action category.

The Bank's actual capital amounts and ratios as of December 31, 2010 and 2009 are as follows:

	Actual		For Capital Adequacy Purposes		Minimum to be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2010:						
Total Capital (to Risk Weighted Assets)	\$ 21,575,018	14.91%	\$ 11,575,760	8.00%	\$ 14,469,700	10.00%
Tier 1 Capital (to Risk Weighted Assets)	\$ 21,488,859	14.85%	\$ 5,787,880	4.00%	\$ 8,681,820	6.00%
Tier 1 Capital (to Average Assets)	\$ 21,488,859	12.49%	\$ 6,880,367	4.00%	\$ 8,600,459	5.00%
December 31, 2009:						
Total Capital (to Risk Weighted Assets)	\$ 19,059,025	13.70%	\$ 11,129,360	8.00%	\$ 13,911,700	10.00%
Tier 1 Capital (to Risk Weighted Assets)	\$ 19,014,892	13.67%	\$ 5,564,680	4.00%	\$ 8,347,020	6.00%
Tier 1 Capital (to Average Assets)	\$ 19,014,892	12.67%	\$ 6,002,702	4.00%	\$ 7,503,377	5.00%

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2010 AND 2009

**10. STOCK OPTION PLAN**

In 2007, the Bank established the 2007 stock option and equity plan (the Plan) for executives, other employees, officers, directors, and consultants. Shares under the Plan may be granted at not less than 100 percent of the fair market value at the grant date. The authorized and granted options under the Plan is as follows:

	<u>Authorized</u>	<u>Granted</u>
2007 Plan	250,000	149,400

The stock options shall not be exercisable more than ten years after the date such option is granted. The granted stock option and equity plan shares are vested as of January 1, 2009. Shares vest when granted subsequent to January 1, 2009.

The following summarizes the option activity under the Stock Option Plan:

	Number of Shares	Option Price Per Share	Weighted Average Exercise Price
Outstanding, December 31, 2008	99,400	\$ 14.65	\$ 14.65
Grants	-	-	-
Exercised	-	-	-
Canceled or expired	-	-	-
Outstanding, December 31, 2009	99,400	14.65	-
Grants	50,000	8.83	8.83
Exercised	-	-	-
Canceled or expired	-	-	-
Outstanding, December 31, 2010	<u>149,400</u>	<u>\$ 12.70</u>	\$ 12.70

The weighted average fair value of options granted during the year ended December 31, 2010 was \$1.23. The weighted average remaining contractual life of options outstanding as of December 31, 2010 is 7.8 years.

Stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense on a straight-line basis over the requisite service period, which is the vesting period. The Bank uses the Black-Scholes option pricing model to determine the fair value of stock options. The fair value of the stock based payment awards is affected by the price of our stock and a number of financial assumptions and variables. These variables include the risk free interest rate, expected dividend rate, expected stock price volatility and the expected life of the options. The following assumptions were used: a risk free interest rate of 3.25 percent, an estimated dividend yield of zero percent, an expected holding period of 10 years and volatility of 5.0 percent.

The expected volatility is based on the historical volatility of peer institutions. The risk-free interest rate is the implied yield available on U.S. Treasury bonds with a remaining term equal to the expected term of the options granted. The expected life is based on the average of the contracted life and vesting schedule for the options granted. The dividend yield assumption is based on expected dividend payouts.

**NOTES TO FINANCIAL STATEMENTS**  
**YEARS ENDED DECEMBER 31, 2010 AND 2009**

In 2009 the Bank approved a compensation plan for the Board of Directors starting in 2010. The plan provided for payments to directors for attending regularly scheduled meetings of the Board of Directors as well as subcommittee meetings during 2010. The plan required payment to be made in the form of Bank stock to be accrued in 2010 and paid out in the first quarter of 2011.

For the year ended December 31, 2010, the Bank recognized stock-based compensation expense of \$40,450. No compensation expense was recognized for the year ended December 31, 2009.

**11. OPERATING LEASES**

In December 2010, the Bank exercised its second five-year option for the branch facility located at 502 Maple Avenue in Vienna, Virginia. The agreement provides for a term of five years ending December 2015. The total base annual lease payments for the second year of the extension are \$66,774, increasing a maximum of five percent per annum, thereafter. The lease agreement includes approximately 1,862 square feet on the ground floor for the branch facility. The lease agreement includes additional rent payments based on a pro rata portion of annual taxes and common area maintenance charges.

In May 2008, the Bank entered into a lease for its loan operations on the second floor at 10555 Main Street, in Fairfax, Virginia. The agreement provides for an initial lease term of approximately three years commencing July 1, 2008 and ending July 31, 2011. Total base annual lease payments are \$162,608 for the first year, increasing three percent per annum, thereafter. The lease agreement is for 6,072 square feet. The lease provides the right to renew for two periods of three additional years with the base rent at the current market rate. The agreement includes additional rent payments based on a pro rata portion of annual taxes, common area maintenance charges, and utilities.

In October 2004, the Bank entered into a lease for its headquarters and an additional branch facility at 10555 Main Street in Fairfax, Virginia. The agreement provides for an initial lease term of 10 years commencing January 1, 2005 and ending December 31, 2014. Total base annual lease payments are \$168,056 for the first year, increasing a maximum of three percent per annum thereafter. The lease agreement is for 6,002 square feet. The agreement includes additional rent payments based on a pro rata portion of annual taxes, common area maintenance charges, and utilities.

The following are the future minimum lease payments at December 31, 2010:

<u>Years ending December 31:</u>	
2011	\$ 362,642
2012	284,681
2013	294,623
2014	304,934
Thereafter	81,164
	<u>\$ 1,328,044</u>

Rent expense amounted to \$448,441 and \$440,149 for the years ended December 31, 2010 and 2009, respectively.

NOTES TO FINANCIAL STATEMENTS  
YEARS ENDED DECEMBER 31, 2010 AND 2009

## 12. FAIR VALUE MEASUREMENTS

Fair value is the exit price that would be received to sell an asset or paid to transfer a liability. Fair value is a market-based measurement that should be determined using assumptions that market participants would use in pricing an asset or liability. A three-level hierarchy is used to prioritize the inputs used in measuring fair value. The levels within the hierarchy are described with Level 1 having the highest priority and Level 3 having the lowest. These levels are:

Level 1 – inputs are based upon unadjusted quoted prices for identical instruments traded in active markets.

Level 2 – inputs are 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 or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – inputs are generally unobservable and typically reflect management’s estimates of assumptions that market participants would use in pricing the asset or liability. Therefore, the fair values are determined using model-based techniques that include option pricing models, discounted cash flow models, and similar techniques.

The following describes the valuation techniques used by the Bank to measure certain financial assets and liabilities recorded at fair value on a recurring basis in the financial statements:

Securities available-for-sale: Securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are derived primarily from or corroborated by observable market data. Third party vendors compile prices from various sources and may determine the fair value of identical or similar securities by using pricing models that considers observable market data (Level 2).

The following table presents the balances of financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2010:

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<u>December 31, 2010</u>				
Available-for-sale securities	\$ 5,767,655	\$ 1,141,936	\$ 4,625,719	\$ -
<u>December 31, 2009</u>				
Available-for-sale securities	\$ 4,631,602	\$ 1,643,534	\$ 2,988,068	\$ -

**NOTES TO FINANCIAL STATEMENTS**  
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Certain financial assets are measured at fair value on a nonrecurring basis in accordance with GAAP. Adjustments to the fair value of these assets usually result from the application of lower-of-cost-or-market accounting or write-downs of individual assets.

The following describes the valuation techniques used by the Bank to measure certain financial assets recorded at fair value on a nonrecurring basis in the financial statements:

Impaired loans: Loans are designated as impaired when, in the judgment of management based on current information and events, it is probable that all amounts due according to the contractual terms of the loan agreement will not be collected. The measurement of loss associated with impaired loans can be based on either the observable market price of the loan or the fair value of the collateral. Fair value is measured based on the value of the collateral securing the loans. Collateral may be in the form of real estate or business assets including equipment, inventory and accounts receivable. The vast majority of the collateral is real estate. The value of real estate collateral is determined utilizing an income or market valuation approach based on an appraisal conducted by an independent, licensed appraiser outside of the Bank using observable market data (Level 2). However, if the collateral is a house or building in the process of construction, or if an appraisal of the real estate property is over two years old, then the fair value is considered Level 3. The value of business equipment is based upon an outside appraisal if deemed significant, or the net book value on the applicable business' financial statements if not considered significant using observable market data. Likewise, values for inventory and accounts receivables collateral are based on financial statement balances or aging reports (Level 3). Impaired loans allocated to the allowance for loan losses are measured at fair value on a nonrecurring basis. Any fair value adjustments are recorded in the period incurred as provision for loan losses on the statements of operations.

The following table summarizes the Bank's financial assets that were measured at fair value on a nonrecurring basis as of December 31:

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<u>December 31, 2010</u>				
Impaired loans	\$ -	\$ -	\$ -	\$ -
<u>December 31, 2009</u>				
Impaired loans	\$ 4,314,000	\$ -	\$ 4,036,000	\$ 278,000

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2010 AND 2009

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The following methods and assumptions were used by the Bank in estimating fair values of financial instruments as disclosed herein:

*Cash and cash equivalents:* The carrying amounts of cash and cash equivalents approximate their fair value.

*Securities available-for-sale:* Fair values for securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

*Interest bearing deposits at other financial institutions:* The carrying amounts of interest bearing deposits at other financial institutions payable on demand, consisting of money market deposits, approximate fair value. Fair value of fixed rate certificates of deposit is estimated based on discounted cash flow analyses using the remaining maturity of the underlying accounts and interest rates currently offered on certificates of deposit with similar original maturities.

*Loans receivable:* For variable-rate loans that reprice frequently and have no significant change in credit risk, fair values are based on carrying values. Fair values for certain mortgage loans (for example, one to four family residential), credit card loans and other consumer loans are based on quoted market prices of similar loans sold in conjunction with securitization transactions, adjusted for differences in loan characteristics. Fair values for business real estate and business loans are estimated using a discounted cash flow analyses, using interest rates currently being offered for loans with similar term to borrowers of similar credit quality. Fair values for impaired loans are estimated using discounted cash flows analyses or underlying collateral values, where applicable.

*Accrued interest:* The carrying amounts of accrued interest approximate fair value.

*Deposits:* The carrying amounts of deposit liabilities payable on demand, consisting of NOW accounts, money market deposits and saving deposits approximate fair value. Fair value of fixed-rate certificates of deposit is estimated based on discounted cash flow analyses using the remaining maturity of the underlying accounts and interest rates currently offered on certificates of deposit with similar original maturities.

*Off balance sheet financial instruments:* At December 31, 2010 and 2009, the fair values of loan commitments and standby letters of credit are immaterial. Therefore, they have not been included in the following table.

## NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2010 AND 2009

The estimated fair values of the Bank's financial instruments are as follows at December 31:

	2010		2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and due from banks	\$ 3,441,325	\$ 3,441,325	\$ 1,375,127	\$ 1,375,127
Federal Funds sold	17,212,000	17,212,000	10,824,000	10,824,000
Securities available-for-sale	5,767,655	5,767,655	4,631,602	4,631,602
Securities held-to-maturity	2,004,489	2,056,405	4,032,860	4,128,982
Loans receivable, net	139,332,123	141,351,184	133,492,233	139,303,835
Accrued interest receivable	517,293	517,293	483,510	483,510
Total financial assets	<u>\$ 168,274,885</u>	<u>\$ 170,345,862</u>	<u>\$ 154,839,332</u>	<u>\$ 160,747,056</u>
Financial liabilities:				
Non-Interest bearing deposits	\$ 29,797,798	\$ 29,797,798	\$ 27,796,586	\$ 27,796,586
Interest bearing deposits	19,869,397	19,869,397	16,918,734	16,918,734
Time Deposits	99,455,768	97,642,988	92,716,485	90,816,961
Accrued interest payable	71,235	71,235	91,096	91,096
Total financial liabilities	<u>\$ 149,194,198</u>	<u>\$ 147,381,418</u>	<u>\$ 137,522,901</u>	<u>\$ 135,623,377</u>

### 13. FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

In the normal course of business, the Bank has outstanding commitments and contingent liabilities, such as commitments to extend credit and standby letters of credit, which are not included in the accompanying financial statements. The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual or notional amount of those instruments. The Bank uses the same credit policies in making such commitments as it does for instruments that are included in the balance sheet.

Financial instruments whose contract amount represents credit risk were as follows:

	2010	2009
Commitments to extend credit	\$ 42,092,564	\$ 30,513,443
Standby letters of credit	\$ 416,202	\$ 148,202

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation. Collateral held varies, but may include accounts receivable, inventory, property and equipment, and income-producing commercial properties.

**NOTES TO FINANCIAL STATEMENTS**  
YEARS ENDED DECEMBER 31, 2010 AND 2009

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

The Bank has not been required to perform on any financial guarantees during the past two years. The Bank has not incurred any losses on its commitments in either 2010 or 2009.

**14. RESTRICTION ON DIVIDENDS**

The Bank is subject to certain restrictions on the amount of dividends that it may pay without prior regulatory approval. At December 31, 2010 and 2009, capital was not available for payment of dividends.

**15. PROFIT SHARING PLAN**

Effective July 1, 2002, the Bank adopted a contributory 401(k) savings plan covering substantially all employees. The Plan allows eligible employees to contribute up to 25 percent of their compensation. The Board of Directors may elect to approve to match a portion of each employee's contribution. The Bank elected to make a discretionary contribution of \$68,904 for the year ended December 31, 2010. No contributions were made by the Bank for the year ended December 31, 2009.

**16. LEGAL CONTINGENCIES**

In 2007, The Freedom Bank of Virginia made a loan to a borrower and sold a participation in the loan to Monarch Bank. The loan matured on March 1, 2009, and was not repaid. The participation agreement provided that the Bank would exercise normal mortgage lending practices in administering the loan. There was a disagreement between the two banks on how best to collect and service the loan. Monarch Bank filed an action against the Bank on June 3, 2009 in the Circuit Court of the City of Chesapeake, Virginia, alleging that the Bank failed to properly service and collect the loan. Monarch Bank sought \$2.19 million in actual damages, plus \$350,000 in punitive damages as well as attorney's fees and costs. The two parties entered into a Settlement and Mutual Release Agreement for the case dated May 3, 2010. The Bank agreed to repurchase Monarch Bank's remaining portion of the loan and Monarch Bank agreed it was not entitled to any future recoveries in the loan. Both parties agreed to release one another from any liability related to the loan.

Various legal claims can arise from time to time in the normal course of business which, in the opinion of management, will have no material effect on the Bank's financial statements.

BOARD OF DIRECTORS AND SENIOR MANAGEMENT

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BOARD OF DIRECTORS

**Richard C. Litman**

*Chairman of the Board*

**Cynthia Carter Atwater**

*Corporate Secretary*

**William G. Dukas**

*Vice Chairman*

**John T. Rohrback**

*Chief Executive Officer*

**G. Thomas Collins, Jr.**

**Dr. Terry L. Collins**

**H. Jason Gold**

**Norman P. Horn**

**Dr. David C. Karlgaard**

**Michael A. Miranda**

**Dr. Alvin E. Nashman**

SENIOR MANAGEMENT

**Craig S. Underhill**

*President*

**John T. Rohrback**

*Chief Executive Officer*

**Robert D. Willey, Jr.**

*Executive Vice President, Commercial Lending*

**Deborah A. Free**

*Senior Vice President  
& Branch Administration Officer*

**Karin M. Johns**

*Executive Vice President  
& Chief Financial Officer*

**Kimberly J. Ryman**

*Senior Vice President  
& Senior Administration & Information Officer*

**Christine A. Gorman**

*Senior Vice President  
& Assistant Corporate Secretary*

DIRECTORS EMERITUS & ADVISORY BOARD

WITH DEEPEST APPRECIATION FOR THE  
DIRECTORS WHO PREVIOUSLY SERVED

**James N. Newsome**

*Founding Chairman & CEO*  
2000 - 2003  
Director Emeritus

**George C. Dukas**

*Director*  
2002 - 2005  
Director Emeritus

**Russell E. Sherman**

*Founding Director*  
2000 - 2007  
In Memoriam

**John F. Carman**

*Founding Director / Vice Chairman*  
2000 - 2006  
In Memoriam

**Michael A. Falke**

*Founding Director*  
2000 - 2002

**Harry N. Snyder, O.D.**

*Founding Director*  
2000 - 2007  
Director Emeritus

**Richard L. Hall**

*Founding Director / President & COO*  
2000 - 2003  
In Memoriam

**Timothy P. Hecht**

*Director*  
2005 - 2007  
Director Emeritus

**James F. Steffey**

*Founding Director*  
2000 - 2007  
Director Emeritus

**Irving Bernstein**

*Founding Director*  
2000 - 2007  
Director Emeritus

**George Z. Kontzias**

*Director*  
2002 - 2006  
Director Emeritus

**C. Stephen Templeton**

*Founding Director*  
2000 - 2002  
Director Emeritus

**Charles M. Wright**

*Founding Director*  
2000 - 2002  
Director Emeritus

ADVISORY BOARD

Arlene Lyles Pripeton, *Chairman*

Darren Bernstein  
Irving Bernstein  
William C. Bogart  
Louis M. Cocks, Jr.  
Jimmy B. Contristan  
John R. Herbert  
Timothy P. Hecht  
Michael J. Kurka  
David C. Knapp

Michael A. Magnotti  
Donald J. Mayer  
Owen Michael McCall  
Stephen W. McCarthy  
Usama H. Misleh  
Ali R. Oskuie  
Thomas J. Riley  
Harry N. Snyder, O.D.

James F. Steffey  
Michael J. Sullivan  
C. Stephen Templeton  
Thomas J. Tracy  
Stephen M. Turner  
Robert G. Williams  
Charles M. Wright  
Theodore A. Yiannarakis

OFFICERS & STAFF

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COMMERCIAL LENDING

**Craig S. Underhill**

*President*

cunderhill@freedombankva.com

**Jeremiah D. Behan**

*SVP & Real Estate Lending Officer*

jbehan@freedombankva.com

**Paula A. Newsome**

*VP & Relationship Management Officer*

pnewsome@freedombankva.com

**Robert D. Willey, Jr.**

*EVP, Commercial Lending*

bwilley@freedombankva.com

**Michael J. Underwood**

*SVP & Relationship Management Officer*

munderwood@freedombankva.com

**Gregory L. Montgomery**

*SVP & Government Contracting Officer*

gmontgomery@freedombankva.com

**Sally T. Siveroni**

*VP & Portfolio Management Officer*

ssiveroni@freedombankva.com

**Ashley Reese**

*Portfolio Manager*

areese@freedombankva.com

LOAN ADMINISTRATION

**Kimberly J. Ryman**

*SVP & Senior Administration & Information Officer*

kdawson@freedombankva.com

**Kevin P. Mullins**

*AVP & Loan Administration Officer*

kmullins@freedombankva.com

**Alicia G. Bez**

*Loan Clerk*

abez@freedombankva.com

**Connie L. Maness**

*Loan Document Specialist*

cmaness@freedombankva.com

**Brenda Croft**

*Loan Document Specialist*

bcroft@freedombankva.com

MORTGAGE LOAN

**George J. Decker**

*VP & Mortgage Loan Originator*

gdecker@freedombankva.com

**Allison Leigh Carey**

*Mortgage Loan Processor*

lcarey@freedombankva.com

**Fredric V. Wilson**

*Mortgage Loan Originator*

fwilson@freedombankva.com

**William T. Rogers**

*Mortgage Loan Originator*

brogers@freedombankva.com

OPERATIONS

**Jeri L. Leddon**

*AVP & Operations Officer*

jleddon@freedombankva.com

**Karin M. Johns**

*EVP & Chief Financial Officer*

kjohns@freedombankva.com

**Thyda Price**

*VP & BSA Risk Management Officer*

tprice@freedombankva.com

OFFICERS & STAFF

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**BRANCHES**

**Deborah A. Free**

*SVP & Branch Administration Officer*  
dafree@freedombankva.com

**Veronika Cavero**

*Assistant Branch Manager - Fairfax*  
vcavero@freedombankva.com

**Trilce Castillo**

*Branch Administrative Assistant - Fairfax*  
t1fairfax@freedombankva.com

**Elizabeth Brown**

*Drive-Thru Teller - Fairfax*  
t2fairfax@freedombankva.com

**Fares Hakim**

*Branch Officer - Vienna*  
fhakim@freedombankva.com

**Hilda Alvarez**

*Branch Administrative Assistant - Vienna*  
halvarez@freedombankva.com

**Janet Gaffney**

*Teller - Vienna*  
t1vienna@freedombankva.com

**Harsha Patel**

*Teller - Vienna*  
t3vienna@freedombankva.com

**HUMAN RESOURCES, MARKETING AND INVESTOR RELATIONS OFFICER**

**Christine A. Gorman**

*SVP & Assistant Corporate Secretary*  
cgorman@freedombankva.com

**COMMERCIAL ACCOUNT SERVICES**

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**TRANSACTION ACCOUNTS**

Business Checking  
 Not-For-Profit Organization Checking  
 Business / Corporate Analysis Account  
 Business Interest Checking

**SAVINGS ACCOUNTS, INVESTMENT & FIDUCIARY SERVICES**

Business Money Market  
 Business Savings  
 Certificates of Deposit  
 CDAR'S (Certificate of Deposit Account Registry Service®)  
 Trustee Accounts

**CASH MANAGEMENT SERVICES**

Concentration Accounts  
 Lockbox Accounts  
 Merchant Accounts  
 Repurchase Agreement Accounts  
 Sweep Accounts  
 Sweep Account into a Collateralized Repurchase Agreement Accounts  
 Target Balance Accounts  
 Zero Balance Accounts  
 Wire Transfers

**CREDIT SERVICES**

Commercial Term Loans  
 Commercial Line of Credit  
 Commercial Revolving Line of Credit  
 Commercial Letters of Credit  
 Commercial Real Estate Mortgages  
 Commercial Construction Loans  
 Small Business Administration (SBA) Loans

**MANAGING ACCOUNTS & FUNDS**

24 Hour Depository  
 24 Hour Telephone Banking  
 ACH Transactions & File Transfers  
 American Express Travelers Cheques/Gift Cards  
 ATM  
 Bank by Mail  
 Cashier's Checks  
 Corporate Credit Card - MasterCard  
 Corporate Debit Card  
 Electronic Check Processing & Deposit Program  
 E-Statements  
 Freedom Direct Online Banking  
 Lock Box Service  
 Merchant Credit Card Services  
 Notary Services  
 Safe Deposit Boxes

**PERSONAL ACCOUNT SERVICES**

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**TRANSACTION ACCOUNTS**

Freedom Ba\$ic (Free) Checking  
Freedom Interest Checking

**SAVINGS ACCOUNTS & INVESTMENT & FIDUCIARY SERVICES**

Personal Money Market Checking  
Regular Savings  
Senior or Student or Minor Savings  
Certificates of Deposit  
CDAR'S (Certificate of Deposit Account Registry Service®)

**INDIVIDUAL RETIREMENT ACCOUNTS**

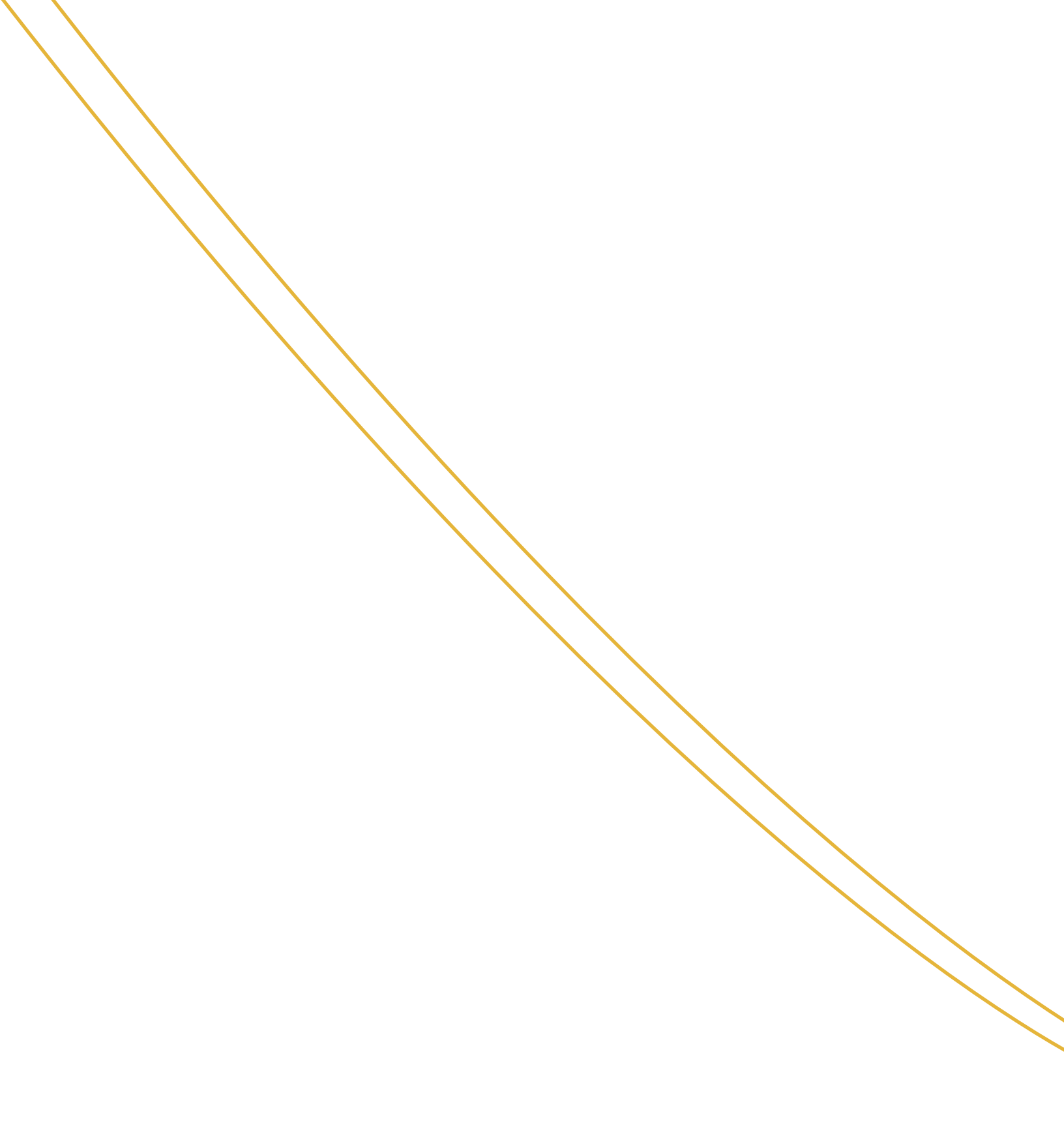
Traditional  
Roth  
Coverdell (formerly Education IRA)  
Simplified Employee Pensions (SEPS)

**CREDIT SERVICES**

Auto Loans  
Boat & RV loans  
Personal Loans  
Overdraft Protection  
Home Equity Loans & Lines of Credit  
Mortgages

**MANAGING ACCOUNTS & FUNDS**

24 Hour Depository  
24 Hour Telephone Banking  
ACH Transactions/Direct Deposit  
ATM  
American Express Travelers Cheques/Gift Cards  
Bank by Mail  
Cashier's Checks  
Credit Cards - Visa & MasterCard  
Debit Check Card  
E-Statements  
Identity Theft Protection  
Notary Services  
Online Banking with Bill Payment  
Safe Deposit Boxes  
U. S. Savings Bonds  
Wire Transfers



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