

TRI COUNTY FINANCIAL CORP /MD/
Form 10-K
March 07, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2010

OR

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

For the transition period from _____ to _____

Commission File No. 0-18279

TRI-COUNTY FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of
incorporation or organization)

52-1652138
(I.R.S. Employer
Identification No.)

3035 Leonardtown Road, Waldorf, Maryland
(Address of principal executive offices)

20601
(Zip Code)

Registrant's telephone number, including area code: (301) 645-5601

Securities registered pursuant to Section 12(b) of the Act: None

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

Common Stock, par value \$0.01 per share
(Title of Class)

Indicate by check mark whether 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 Section 15(d) of the Act. Yes ☐ No ☒

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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 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 ☐

Smaller reporting company ☒

(Do not check if a smaller reporting company)

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

The aggregate market value of voting stock held by non-affiliates of the registrant was approximately \$23.8 million based on the closing price (\$11.25 per share) at which the common stock was sold on the last business day of the Company's most recently completed second fiscal quarter. For purposes of this calculation only, the shares held by directors, executive officers and the Company's Employee Stock Ownership Plan of the registrant are deemed to be shares held by affiliates.

Number of shares of common stock outstanding as of March 4, 2011: 3,022,848

DOCUMENTS INCORPORATED BY REFERENCE

1. Portions of the Annual Report to Stockholders for the year ended December 31, 2010. (Part II)
2. Portions of the Proxy Statement for the 2011 Annual Meeting of Stockholders. (Part III)

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PART I

This report contains certain “forward-looking statements” within the meaning of the federal securities laws. These statements are not historical facts, rather statements based on Tri-County Financial Corporation’s current expectations regarding its business strategies, intended results and future performance. Forward-looking statements are preceded by terms such as “expects,” “believes,” “anticipates,” “intends” and similar expressions.

Management’s ability to predict results or the effect of future plans or strategies is inherently uncertain. Factors that could affect actual results include interest rate trends, the general economic climate in the market area in which Tri-County Financial Corporation operates, as well as nationwide, Tri-County Financial Corporation’s ability to control costs and expenses, competitive products and pricing, loan delinquency rates and changes in federal and state legislation and regulation. These factors should be considered in evaluating the forward-looking statements and undue reliance should not be placed on such statements. Tri-County Financial Corporation assumes no obligation to update any forward-looking statement after the date of the statements or to reflect the occurrence of anticipated or unanticipated events.

Item 1. Business

Tri-County Financial Corporation (the “Company”) is a bank holding company organized in 1989 under the laws of the State of Maryland. It owns all the outstanding shares of capital stock of Community Bank of Tri-County (the “Bank”), a Maryland-chartered commercial bank. The Bank was originally organized in 1950 as Tri-County Building and Loan Association of Waldorf, a mutual savings and loan association, and in 1986 converted to a federal stock savings bank and adopted the name Tri-County Federal Savings Bank. In 1997, the Bank converted to a Maryland-chartered commercial bank and adopted its current name. The Company engages in no significant activity other than holding the stock of the Bank and operating the business of the Bank. Accordingly, the information set forth in this report, including financial statements and related data, relates primarily to the Bank and its subsidiaries.

The Bank serves the Southern Maryland counties of Charles, Calvert and St. Mary’s, (the “Tri-County area”) through its main office and nine branches located in Waldorf, Bryans Road, Dunkirk, Leonardtown, La Plata, Lusby, Charlotte Hall, Prince Frederick and Lexington Park, Maryland. The Bank operates fifteen automated teller machines (“ATMs”) including five stand-alone locations in the Tri-County area. The Bank offers telephone and internet banking services. The Bank is engaged in the commercial and retail banking business as authorized by the banking statutes of the State of Maryland and applicable federal regulations, including the acceptance of deposits, and the origination of loans to individuals, associations, partnerships and corporations. The Bank’s real estate financing consists of residential first and second mortgage loans, home equity lines of credit and commercial mortgage loans. Commercial lending consists of both secured and unsecured loans. The Bank is a member of the Federal Reserve and Federal Home Loan Bank (the “FHLB”) system and its deposits are insured up to applicable limits by the Deposit Insurance Fund administered by the Federal Deposit Insurance Corporation (the “FDIC”).

The Company’s executive offices are located at 3035 Leonardtown Road, Waldorf, Maryland. Its telephone number is (301) 645-5601.

Available Information

The Company’s Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, current reports on Form 8-K, and any amendments to such reports filed pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, are made available free of charge on its website, www.cbtc.com, as soon as reasonably practicable after such reports are electronically filed with the Securities and Exchange Commission. Information on the website should not be considered a part of this Form 10-K.

Market Area

The Bank considers its principal lending and deposit market area to consist of the Tri-County area. These counties have experienced significant population growth during the past decade due to their proximity to the growing Washington, DC and Baltimore metropolitan areas. Southern Maryland is generally considered to have more affordable housing than many other Washington and Baltimore area suburbs. In addition, the area has experienced rapid growth in the last decade in businesses and federal facilities located in the area. Major federal facilities include the Patuxent Naval Air Station in St. Mary's County. The Patuxent Naval Air Station has undergone significant expansion in the last several years and is projected to continue to expand for several more years.

In the last several years, residential housing and population growth in the Tri-County area has been constrained by certain government policies designed to limit growth. Growth has also been dampened as the demand for new housing in the Tri-County area has fallen as the overall housing market has fallen. Future regulatory events may adversely affect the Bank's loan growth.

Competition

The Bank faces strong competition in the attraction of deposits and in the origination of loans. Its most direct competition for deposits and loans comes from other banks, savings and loan associations, and federal and state credit unions located in its primary market area. There are currently 14 FDIC-insured depository institutions operating in the Tri-County area including subsidiaries of several regional and super-regional bank holding companies. According to statistics compiled by the FDIC, the Bank was ranked third in deposit market share in the Tri-County area as of June 30, 2010, the latest date for which such data is available. The Bank faces additional significant competition for investors' funds from mutual funds, brokerage firms, and other financial institutions. The Bank competes for loans by providing competitive rates, flexibility of terms, and service. It competes for deposits by offering depositors a wide variety of account types, convenient office locations and competitive rates. Other services offered include tax-deferred retirement programs, brokerage services, cash management services and safe deposit boxes. The Bank has used direct mail, billboard and newspaper advertising to increase its market share of deposits, loans and other services in its market area. It provides ongoing training for its staff in an attempt to ensure high-quality service.

Lending Activities

General. The Bank offers a wide variety of real estate, consumer and commercial loans. The Bank's lending activities include residential and commercial real estate loans, construction loans, land acquisition and development loans, equipment financing and commercial and consumer loans. Most of the Bank's customers are residents of, or businesses located in, the Tri-County area. The Bank's primary market for commercial loans consists of small and medium-sized businesses located in Southern Maryland. The Bank believes that this market is responsive to the Bank's ability to provide personal service and flexibility. The Bank attracts customers for its consumer lending products based upon its ability to offer service, flexibility, and competitive pricing, as well as by leveraging other banking relationships such as soliciting deposit customers for loans.

Commercial Real Estate and Other Non-Residential Real Estate Loans. The permanent financing of commercial and other improved real estate projects, including office buildings, retail locations, churches, and other special purpose buildings is the largest single component of the Bank's loan portfolio. Commercial real estate loans amounted to \$336.3 million, or 50.7% of the loan portfolio, at December 31, 2010. This was an increase in both absolute size and as a percentage of the loan portfolio from the previous year. The commercial real estate and residential first mortgage loan portfolios increased as a percentage of total loans during 2010. The primary security on a commercial real estate loan is the real property and the leases that produce income for the real property. The Bank generally limits its exposure to a single borrower to 15% of the Bank's capital and participates with other lenders on larger

projects. Loans secured by commercial real estate are generally limited to 80% of the lower of the appraised value or sales price and have an initial contractual loan payment period ranging from three to 20 years. Virtually all of the Bank's commercial real estate loans are secured by real estate located in the Bank's primary market area. At December 31, 2010, the largest outstanding commercial real estate loan was a \$7.4 million loan, which is secured by an office building. This loan was performing according to its terms at December 31, 2010.

Loans secured by commercial real estate are larger and involve greater risks than one-to-four family residential mortgage loans. Because payments on loans secured by such properties are often dependent on the successful operation or management of the properties, repayment of such loans may be subject to a greater extent to adverse conditions in the real estate market or the economy. As a result of the greater emphasis that the Bank places on commercial real estate loans, the Bank is increasingly exposed to the risks posed by this type of lending. To monitor cash flows on income properties, the Bank requires borrowers and loan guarantors, if any, to provide annual financial statements on multi-family or commercial real estate loans. In reaching a decision on whether to make a multi-family or commercial real estate loan, the Bank considers the net operating income of the property, the borrower's expertise, credit history and profitability, and the value of the underlying property. Environmental surveys are generally required for commercial real estate loans over \$250,000.

Residential First Mortgage Loans. Residential first mortgage loans made by the Bank are generally long-term loans, amortized on a monthly basis, with principal and interest due each month. The initial contractual loan payment period for residential loans typically ranges from ten to 30 years. The Bank's experience indicates that real estate loans remain outstanding for significantly shorter time periods than their contractual terms. Borrowers may refinance or prepay loans at their option, without penalty. The Bank originates both fixed-rate and adjustable-rate residential first mortgages.

The Bank offers fixed-rate residential first mortgages on a variety of terms including loan periods from ten to 30 years and bi-weekly payment loans. Total fixed-rate loan products in our residential first mortgage portfolio amounted to \$122.4 million as of December 31, 2010. Fixed-rate loans may be packaged and sold to investors or retained in the Bank's loan portfolio. Depending on market conditions, the Bank may elect to retain the right to service the loans sold for a payment based upon a percentage (generally 0.25% of the outstanding loan balance). These servicing rights may be sold to other qualified servicers. As of December 31, 2010, the Bank serviced \$43.3 million in residential mortgage loans for others.

The Bank also offers mortgages that are adjustable on a one-, three- and five-year basis generally with limitations on upward adjustments of two percentage points per repricing period and six percentage points over the life of the loan. The Bank primarily markets adjustable-rate loans with rate adjustments based upon a United States Treasury Bill Index. As of December 31, 2010, the Bank had \$13.6 million in adjustable-rate residential mortgage loans. The retention of adjustable-rate mortgage loans in the Bank's loan portfolio helps reduce the negative effects of increases in interest rates on the Bank's net interest income. Under certain conditions, however, the annual and lifetime limitations on interest rate adjustments may limit the increases in interest rates on these loans. There are also unquantifiable credit risks resulting from potential increased costs to the borrower as a result of repricing of adjustable-rate mortgage loans. During periods of rising interest rates, the risk of default on adjustable-rate mortgage loans may increase due to the upward adjustment of interest cost to the borrower. In addition, the initial interest rate on adjustable-rate loans is generally lower than that on a fixed-rate loan of similar credit quality and size.

The Bank makes residential first mortgage loans of up to 97% of the appraised value or sales price of the property, whichever is less, to qualified owner-occupants upon the security of single-family homes. Non-owner occupied one-to four-family loans are generally permitted to a maximum 80% loan-to-value of the appraised value depending on the overall strength of the application. The Bank currently requires that substantially all residential first mortgage loans with loan-to-value ratios in excess of 80% carry private mortgage insurance to lower the Bank's exposure to approximately 80% of the value of the property. In certain cases, the borrower may elect to borrow amounts in excess of 80% loan-to-value in the form of a second mortgage. The second mortgage will generally have a higher interest rate and shorter repayment period than the first mortgage on the same property.

All improved real estate that serves as security for a loan made by the Bank must be insured, in the amount and by such companies as may be approved by the Bank, against fire, vandalism, malicious mischief and other hazards. Such

insurance must be maintained through the entire term of the loan and in an amount not less than that amount necessary to pay the Bank's indebtedness in full.

Construction and Land Development Loans. The Bank offers construction loans to individuals and building contractors for the construction of one-to-four family dwellings. Construction loans totaled \$17.4 million at December 31, 2010. Loans to individuals primarily consist of construction/permanent loans, which have fixed rates, payable monthly for the construction period and are followed by a 30-year, fixed or adjustable-rate permanent loan. The Bank also provides construction financing to home builders. Generally, these loans are secured by the real estate under construction as well as by guarantees of the principals involved. Draws are made upon satisfactory completion of predefined stages of construction. The Bank will typically lend up to the lower of 80% of the appraised value or the contract purchase price of the homes to be constructed.

In addition, the Bank offers loans to acquire and develop land, as well as loans on undeveloped, subdivided lots for home building by individuals. Land acquisition and development loans totaled \$25.1 million at December 31, 2010. Bank policy requires that zoning and permits must be in place prior to making development loans. The Bank will typically lend up to the lower of 75% of the appraised value or cost.

The Bank's ability to originate all types of residential construction and development loans is heavily dependent on the continued demand for single-family housing construction in the Bank's market areas. As demand for newly constructed housing has fallen, the Bank's investment in these loans has slowed and the net portfolio decreased \$20.0 million from \$62.5 million at December 31, 2009 to \$42.5 million at December 31, 2010. Additionally, construction and land development loans as a percentage of the total loan portfolio fell from 10.0% at December 31, 2009 to 6.4% at December 31, 2010. If the demand for new houses in the Bank's market areas continues to decline, this portion of its loan portfolio may also decline. In addition, a continued decline in demand for new housing might adversely affect the ability of borrowers to repay these loans. The Bank may not be able to grow its construction lending activities in the event of a continued decline. Construction and land development loans have been particularly affected by recent economic factors that have slowed absorption of finished lots and homes.

Construction and land development loans are inherently riskier than providing financing on owner-occupied real estate. The Bank's risk of loss is affected by the accuracy of the initial estimate of the market value of the completed project as well as the accuracy of the cost estimates made to complete the project. In addition, the volatility of the real estate market has made it increasingly difficult to ensure that the valuation of land associated with these loans is accurate. During the construction phase, a number of factors could result in delays and cost overruns. If the estimate of construction costs proves to be inaccurate, the Bank may be required to advance funds beyond the amount originally committed to permit completion of the development. If the estimate of value proves to be inaccurate, the Bank may be confronted, at or before the maturity of the loan, with a project having a value that is insufficient to assure full repayment. As a result of these factors, construction lending often involves the disbursement of substantial funds with repayment dependent, in part, on the success of the project rather than the ability of the borrower or guarantor to repay principal and interest. If the Bank forecloses on a project, there can be no assurance that the Bank will be able to recover all of the unpaid balance of, and accrued interest on, the loan as well as related foreclosure and holding costs.

Home Equity and Second Mortgage Loans. The Bank maintains a portfolio of home equity and second mortgage loans. Home equity loans, which totaled \$19.0 million at December 31, 2010, are generally made in the form of lines of credit with minimum amounts of \$5,000, have terms of up to 20 years, variable rates priced at prime or some margin above prime, and require an 80% or 90% loan-to-value ratio (including any prior liens), depending on the specific loan program. Second mortgage loans, which totaled \$5.4 million at December 31, 2010, are fixed and variable-rate loans that have original terms between five and 15 years. Loan-to-value ratios of up to 80% or 95% are allowed depending on the specific loan program.

These products contain a higher risk of default than residential first mortgages as in the event of foreclosure, the first mortgage would need to be paid off prior to collection of the second mortgage. This risk has been heightened as the market value of residential property has declined. The Bank is monitoring the property values which secure its second mortgages and is lowering credit availability where prudent. The Bank believes that its policies and procedures are sufficient to mitigate the additional risk posed by these loans at the current time.

Commercial Loans. The Bank offers commercial loans to its business customers. The Bank offers a variety of commercial loan products including term loans and lines of credit. Such loans are generally made for terms of five years or less. The Bank offers both fixed-rate and adjustable-rate loans under these product lines. While commercial loans remain an important class of the Bank's loan portfolio at 15.77% of total loans, the commercial loan portfolio decreased by \$4.1 million from \$108.7 million at December 31, 2009 to \$104.6 million at December 31, 2010. When making commercial business loans, the Bank considers the financial condition of the borrower, the borrower's payment history of both corporate and personal debt, the projected cash flows of the business, the viability of the industry in which the consumer operates, the value of the collateral, and the borrower's ability to service the debt from income. These loans are primarily secured by equipment, real property, accounts receivable, or other security as determined by the Bank. The higher interest rates and shorter loan terms available on commercial lending make these products attractive to the Bank. Commercial business loans, however, entail greater risk than residential mortgage loans. Unlike residential mortgage loans, which generally are made on the basis of the borrower's ability to make repayment from his or her employment or other income and which are secured by real property whose value tends to be more easily ascertainable, commercial loans are made on the basis of the borrower's ability to make repayment from the cash flows of the borrower's business. As a result, the availability of funds for the repayment of commercial loans may depend substantially on the success of the business itself. In the case of business failure, collateral would need to be liquidated to provide repayment for the loan. In many cases, the highly specialized nature of collateral equipment would make full recovery from the sale of collateral problematic. The Bank attempts to control these risks by establishing guidelines that provide for loans with low loan-to-value ratios. At December 31, 2010, the largest outstanding commercial loan was \$9.5 million, which was secured by commercial real estate, cash and investments. This loan was performing according to its terms at December 31, 2010.

Consumer Loans. The Bank has developed a number of programs to serve the needs of its customers with primary emphasis upon loans secured by automobiles, boats, recreational vehicles and trucks. The Bank also makes home improvement loans and offers both secured and unsecured personal lines of credit. Consumer loans totaled \$1.3 million at December 31, 2010. The higher interest rates and shorter loan terms available on consumer lending make these products attractive to the Bank. Consumer loans entail greater risk than residential mortgage loans, particularly in the case of consumer loans, which are unsecured or secured by rapidly depreciating assets such as automobiles. In such cases, any repossessed collateral may not provide an adequate source of repayment of the outstanding loan balance. Further collection efforts may be hampered by the borrower's lack of current income or other assets. In addition, consumer loan collections are dependent on the borrower's continuing financial stability and thus are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws including federal and state bankruptcy and insolvency laws, may limit the amount that can be recovered on such loans. Such loans may also give rise to claims and defenses by a consumer loan borrower against an assignee such as the Bank, and a borrower may be able to assert against such assignee claims and defenses that it has against the seller of the underlying collateral.

Commercial Equipment Loans. The Bank also maintains a commercial equipment financing portfolio. Commercial equipment loans totaled \$18.0 million, or 2.7% of the total loan portfolio, at December 31, 2010. These loans consist primarily of fixed-rate, short-term loans collateralized by customers' equipment including trucks, cars, construction equipment, and other more specialized equipment. When making commercial equipment loans, the Bank considers the same factors it considers when underwriting a commercial business loan. The higher interest rates and shorter loan terms available on commercial equipment lending make these products attractive to the Bank. These loans entail greater risk than loans such as residential mortgage loans. Unlike residential mortgage loans, which generally are made on the basis of the borrower's ability to make repayment from his or her employment or other income and which are secured by real property whose value tends to be more easily ascertainable, commercial loans are of higher risk and typically are made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business. As a result, the availability of funds for the repayment of commercial loans may depend substantially on the success of the business itself. In the case of business failure, collateral would need to be liquidated to provide

repayment for the loan. In many cases, the highly specialized nature of collateral equipment would make full recovery from the sale of collateral problematic. The Bank attempts to control these risks by establishing guidelines that provide for over collateralization of the loans.

Loan Portfolio Analysis. Set forth below is selected data relating to the composition of the Bank's loan portfolio by type of loan on the dates indicated.

	At December 31, 2010			2009			2008			2007			2006		
	Amount	%		Amount	%		Amount	%		Amount	%		Amount	%	
(Dollars in Thousands)															
Real Estate															
Loans															
Commercial	\$336,300	50.72	%	\$292,988	46.88	%	\$236,410	43.11	%	\$190,484	41.55	%	\$181,933	42.63	%
Residential															
first															
mortgage	136,048	20.52	%	116,226	18.59	%	104,607	19.07	%	90,932	19.83	%	80,781	18.93	%
Construction															
and land															
development	42,504	6.41	%	62,509	10.00	%	57,565	10.50	%	50,577	11.03	%	41,715	9.77	%
Home equity															
and second															
mortgage	24,380	3.68	%	25,133	4.02	%	25,412	4.63	%	24,650	5.38	%	24,572	5.76	%
Commercial															
loans	104,566	15.77	%	108,658	17.38	%	101,936	18.59	%	75,247	16.41	%	76,651	17.96	%
Consumer															
loans	1,273	0.19	%	1,608	0.26	%	2,046	0.37	%	2,465	0.54	%	2,813	0.66	%
Commercial															
equipment	17,984	2.71	%	17,917	2.87	%	20,458	3.73	%	24,113	5.26	%	18,288	4.29	%
Total loans	663,055	100.00	%	625,039	100.00	%	548,434	100.00	%	458,468	100.00	%	426,754	100.00	%
Less:															
Deferred															
loan fees	936			975			311			371			490		
Loan loss															
reserve	7,669			7,471			5,146			4,482			3,784		
Loans															
receivable,															
net	\$654,450			\$616,593			\$542,977			\$453,614			\$422,480		

Loan Originations, Purchases and Sales. The Bank solicits loan applications through marketing by commercial and residential mortgage loan officers, its branch network, and referrals from customers. Loans are processed and approved according to guidelines deemed appropriate for each product type. Loan requirements such as income verification, collateral appraisal, and credit reports vary by loan type. Loan processing functions are generally centralized except for small consumer loans.

Loan Approvals, Procedures and Authority. Loan approval authority is established by Board policy and delegated as deemed necessary and appropriate. Loan approval authorities vary by individual with the Chief Executive Officer having approval authority up to \$1.25 million, the President \$1.0 million, the Chief Lending Officer \$1.0 million, the Chief Credit Officer \$1.0 million and the Chief Operating Officer \$1.0 million. The individual lending authority of the other lenders is set by management and based on their individual abilities. The loan approval authorities of the Chief Executive Officer, the President, the Chief Lending Officer, the Chief Credit Officer, the Chief Operating Officer and the Senior Credit Officer may be combined and a minimum of at least three of the five need to be present in an officers' loan committee to approve loans up to \$2.0 million. In cases where time is of the essence, the officers' loan committee consisting of any three members may unanimously approve loans to relationships in excess of the \$2.0 million up to the Bank's in house lending limit with a later ratification by the Board Credit Review Committee. A loan committee consisting of at least three members of the Board (the "Credit Review Committee") ratifies all commercial real estate loans and approves or renews all loans to relationships that exceed \$2.0 million, except for those noted above that exceed the \$2.0 million limit in certain cases. Depending on the loan and collateral type, conditions for protecting the Bank's collateral are specified in the loan documents. Typically these conditions might include requirements to maintain hazard and title insurance and to pay property taxes.

Depending on market conditions, mortgage loans may be originated primarily with the intent to sell to third parties such as Fannie Mae or Freddie Mac. Mortgage loans in the amount of \$14.2 million were sold by the Bank in 2010. To comply with internal and regulatory limits on loans to one borrower, the Bank may sell portions of commercial and commercial real estate loans to other lenders. The Bank sold no participations in 2010. The Bank also buys loans, portions of loans, or participation certificates from other lenders. The Bank only purchases loans or portions of loans after reviewing loan documents, underwriting support, and other procedures, as necessary. The Bank did not purchase any participations in 2010. Purchased participation loans are subject to the same regulatory and internal policy requirements as other loans in the Bank's portfolio.

Loans to One Borrower. Under Maryland law, the maximum amount that the Bank is permitted to lend to any one borrower and his or her related interests may generally not exceed 10% of the Bank's unimpaired capital and surplus, which is defined to include the Bank's capital, surplus, retained earnings and 50% of its reserve for possible loan losses. Under this authority, the Bank would have been permitted to lend up to \$8.5 million to any one borrower at December 31, 2010. By interpretive ruling of the Commissioner of Financial Regulation, Maryland banks have the option of lending up to the amount that would be permissible for a national bank, which is generally 15% of unimpaired capital and surplus (defined to include a bank's total capital for regulatory capital purposes plus any loan loss allowances not included in regulatory capital). Under this formula, the Bank would have been permitted to lend up to \$13.3 million to any one borrower at December 31, 2010. At December 31, 2010, the largest amount outstanding to any one borrower and his or her related interests was \$8.9 million.

Loan Commitments. The Bank does not normally negotiate standby commitments for the construction and purchase of real estate. Conventional loan commitments are granted for a one-month period. The Bank's outstanding commitments to originate loans at December 31, 2010 were approximately \$18.6 million, excluding undisbursed portions of loans in process. It has been the Bank's experience that few commitments expire unfunded.

Maturity of Loan Portfolio. The following table sets forth certain information at December 31, 2010 regarding the dollar amount of loans maturing in the Bank's portfolio based on their contractual terms to maturity. Demand loans, loans having no stated schedule of repayments and no stated maturity, and overdrafts are reported as due in one year or less.

	Due within one year after December 31, 2010 (Dollars in Thousands)	Due after one year through five years from December 31, 2010	Due more than five years from December 31, 2010
Real Estate Loans			
Commercial	\$ 34,487	\$ 54,695	\$ 247,118
Residential first mortgage	30,537	59,380	46,132
Construction and land development	42,317	187	-
Home equity and second mortgage	5,423	13,081	5,876
Commercial loans	104,566	-	-
Consumer loans	777	442	54
Commercial equipment	5,481	9,313	3,190
Total loans	\$ 223,588	\$ 137,098	\$ 302,370

The following table sets forth the dollar amount of all loans due after one year from December 31, 2010, which have predetermined interest rates and have floating or adjustable interest rates.

	Fixed Rates (Dollars in Thousands)	Floating or Adjustable Rates	Total
Real Estate Loans			
Commercial	\$ 42,296	\$ 259,517	\$ 301,813
Residential first mortgage	94,816	10,696	105,512
Construction and land development	-	187	187
Home equity and second mortgage	2,561	16,396	18,957
Commercial loans	-	-	-
Consumer loans	496	-	496
Commercial equipment	11,455	1,048	12,503
	\$ 151,624	\$ 287,844	\$ 439,468

Delinquencies. The Bank's collection procedures provide that when a loan is 15 days delinquent, the borrower is contacted by mail and payment is requested. If the delinquency continues, subsequent efforts will be made to contact the delinquent borrower and obtain payment. If these efforts prove unsuccessful, the Bank will pursue appropriate legal action including repossession of the collateral and other actions as deemed necessary. In certain instances, the Bank will attempt to modify the loan or grant a limited moratorium on loan payments to enable the borrower to reorganize his financial affairs.

Impairment. A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay,

the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price or the fair value of the collateral if the loan is collateral dependent.

Loan loss reserves of \$2.0 million relate to impaired loans at December 31, 2010.

Non-Performing Assets and Asset Classification. The Bank's non-performing assets include foreclosed real estate and non-accrual loans. Troubled debt restructured loans ("TDRs") are only considered non-performing assets if they are not accruing interest or are not performing in accordance with the terms of their restructured agreements.

Foreclosed Real Estate. Real estate acquired by the Bank as a result of foreclosure or by deed in lieu of foreclosure is classified as foreclosed real estate until such time as it is sold. When such property is acquired, it is recorded at its fair market value. Subsequent to foreclosure, the property is carried at the lower of cost or fair value less selling costs. Additional write-downs as well as carrying expenses of the foreclosed properties are charged to expenses in the current period. The Bank had foreclosed real estate with a carrying value of approximately \$10.5 million at December 31, 2010.

Non-accrual Loans. Loans are reviewed on a regular basis and are placed on non-accrual status when, in the opinion of management, the collection of additional interest is doubtful. 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 the process of collection. Consumer loans are typically charged-off no later than 90 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. Non-accrual loans are evaluated for impairment on a loan by loan basis in accordance with the Company's impairment methodology.

All interest accrued but not collected from 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 principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Troubled Debt Restructured Loans. The Company considers all TDRs to be impaired and defines TDRs as loans whose terms have been modified to provide for a reduction of either interest or principal because of deterioration in the financial condition of the borrower. A loan extended or renewed at a stated interest rate equal to the current interest rate for new debt with similar risk is not considered a TDR. Once an obligation has been classified as a TDR it continues to be considered a TDR until paid in full or until the loan returns to performing status and yields a market interest rate equal to the current interest rate for new debt with similar risk. TDRs are evaluated by management on a regular basis utilizing the Company's risk grading matrix and must have a passing loan grade to be removed as a TDR. TDRs are evaluated for impairment on a loan by loan basis in accordance with the Company's impairment methodology. The Company does not participate in any specific government or Company sponsored loan modification programs. All restructured loan agreements are individual contracts negotiated with a borrower.

The following table sets forth information with respect to the Bank's foreclosed real estate, non-accrual loans and troubled debt restructured loans ("TDRs"). The table includes a breakdown between non-performing and impaired loans.

	2010	2009	At December 31,		2007	2006
			2008			
	(Dollars in Thousands)					
Foreclosed real estate	\$ 10,469	\$ 923	\$ -	\$ -	\$ 461	
Non-performing loans						
Non-accrual loans with impairment	\$ 4,506	\$ 8,947	\$ 1,743	\$ -	\$ -	
Non-accrual loans with no impairment	8,715	10,340	3,193	414	1,046	
TDRs not performing according to terms	297	-	-	-	-	
Total non-performing loans	\$ 13,518	\$ 19,287	\$ 4,936	\$ 414	\$ 1,046	
Total non-performing assets	\$ 23,987	\$ 20,210	\$ 4,936	\$ 414	\$ 1,507	
Impaired loans						
Non-accrual loans with impairment	\$ 4,506	\$ 8,947	\$ 1,743	\$ -	\$ -	
TDRs not performing according to terms	297	-	-	-	-	
TDRs performing according to terms	16,585	11,601	-	755	-	
Total impaired loans	\$ 21,388	\$ 20,548	\$ 1,743	\$ 755	\$ -	
Non-performing loans to total loans	2.04 %	3.09 %	0.90 %	0.09 %	0.25 %	
Allowance for loan losses to nonperforming loans	56.73 %	38.74 %	104.25 %	1082.61 %	361.76 %	
Nonperforming assets to total assets	2.71 %	2.48 %	0.69 %	0.07 %	0.26 %	
Nonperforming assets and TDRs to total assets	4.58 %	3.90 %	0.69 %	0.20 %	0.26 %	

The largest concentration of non-performing loans is in the commercial real estate portfolio. Foreclosed real estate has grown as the Bank continues to resolve problem loans. Two construction and land development properties represent 86% of the foreclosed real estate balance and are the primary factor in the current year increase in nonperforming assets from 2.48% to 2.71%. Other loan types have also been affected by the economic conditions in our local and national markets. At December 31, 2010, the Bank had 32 non-performing loans of which \$10.5 million or 78% of the Bank's non-performing loan balances represent six customer relationships. The Bank's non-performing loans are predominantly collateralized. Management continues to monitor these loans and is working to resolve these loans in a manner which will, in our opinion, preserve the most value for the Company. The below schedule provides the details by loan portfolio of non-performing loans for the dates indicated.

	2010	2009	At December 31,		2007	2006
			2008			

(Dollars in Thousands)

Loans accounted for on a nonaccrual basis:

Real Estate Loans

Commercial	\$ 8,243	\$ 6,367	\$ 1,208	\$ -	\$ 390
Residential first mortgage	1,747	339	-	274	273
Construction and land development	984	9,504	1,840	-	-
Home equity and second mortgage	233	-	-	-	-
Commercial loans	2,262	2,192	903	60	303
Consumer loans	1	23	148	80	80
Commercial equipment	48	862	837	-	-
Total	\$ 13,518	\$ 19,287	\$ 4,936	\$ 414	\$ 1,046

During the years ended December 31, 2010 and December 31, 2009, gross interest income of \$875,170 and \$1.3 million, respectively, would have been recorded on loans accounted for on a non-accrual basis if the loans had been current throughout the period. During 2010 and 2009, the Company recognized \$204,000 and \$268,000 in interest on these loans.

At December 31, 2010, the Bank had 19 troubled debt restructured loans of which \$16.6 million or 98.2% were performing according to the terms of their restructured agreements. During 2010, the Company recognized \$720,570 in interest on these loans. At December 31, 2010, the only non-performing TDR was a commercial real estate loan in the amount of \$297,000 was a non-performing non-accrual loan. Management continues to monitor these loans and is working to resolve these loans in a manner which will, in our opinion, preserve the most value for the Company. The below schedule provides the details by loan portfolio of TDRs for the dates indicated.

	2010	2009	At December 31,		2006
			2008	2007	
	(Dollars in Thousands)				
Real Estate Loans					
Commercial	\$6,848	\$6,706	\$-	\$755	\$-
Residential first mortgage	929	394	-	-	-
Commercial loans	8,834	4,441	-	-	-
Commercial equipment	271	60	-	-	-
Total	\$16,882	\$11,601	\$-	\$755	\$-

The following table sets forth an analysis of activity in the Bank's allowance for loan losses for the periods indicated.

	2010	2009	At December 31,		2006
			2008	2007	
	(Dollars in Thousands)				
Balance at beginning of period	\$7,471	\$5,146	\$4,482	\$3,784	\$3,383
Charge-offs:					
Real Estate Loans					
Commercial	526	-	-	29	-
Residential first mortgages	63	-	-	-	-
Construction and land development	2,249	187	287	-	-
Home equity and second mortgage	71	98	-	-	-
Commercial loans	569	608	202	73	-
Consumer loans	10	32	67	56	8
Commercial equipment	256	223	83	-	-
Total Charge-offs:	3,744	1,148	639	158	8
Recoveries:					
Construction and land development	1	-	-	-	-
Consumer loans	7	-	2	2	3
Total Recoveries	8	-	2	2	3
Net charge-offs	3,736	1,148	637	156	5
Provision for Possible Loan Losses	3,934	3,473	1,301	855	406
Balance at End of Period	\$7,669	\$7,471	\$5,146	\$4,482	\$3,784
Allowance for loan losses to total loans	1.16	% 1.20	% 0.94	% 0.98	% 0.89
Net charge-offs to average loans	0.61	% 0.20	% 0.13	% 0.04	% 0.00

The following table allocates the allowance for loan losses by loan category at the dates indicated. The allocation of the allowance to each category is not necessarily indicative of future losses and does not restrict the use of the allowance to absorb losses in any category.

	2010			2009			At December 31, 2008			2007			2006		
	Amount	Percent of Loans in Each Category to Total Loans		Amount	Percent of Loans in Each Category to Total Loans		Amount	Percent of Loans in Each Category to Total Loans		Amount	Percent of Loans in Each Category to Total Loans		Amount	Percent of Loans in Each Category to Total Loans	
(Dollars in Thousands)															
Real Estate Loans															
Commercial	\$3,314	50.72 %		\$2,660	46.88 %		\$2,009	43.11 %		\$1,739	41.55 %		\$1,479	42.63 %	
Residential first mortgage	204	20.52 %		128	18.59 %		105	19.07 %		266	19.83 %		97	18.93 %	
Construction and land development	1,267	6.41 %		1,696	10.00 %		1,295	10.50 %		1,125	11.03 %		662	9.77 %	
Home equity and second mortgage	98	3.68 %		131	4.02 %		102	4.63 %		98	5.38 %		104	5.76 %	
Commercial loans	2,551	15.77 %		2,110	17.38 %		1,248	18.59 %		930	16.41 %		1,135	17.96 %	
Consumer loans	32	0.19 %		64	0.26 %		43	0.37 %		96	0.54 %		126	0.66 %	
Commercial equipment	203	2.71 %		682	2.87 %		344	3.73 %		228	5.26 %		181	4.29 %	
Total allowance for loan losses	\$7,669	100.00 %		\$7,471	100.00 %		\$5,146	100.00 %		\$4,482	100.00 %		\$3,784	100.00 %	

The Bank closely monitors the payment activity of all its loans. The Bank periodically reviews the adequacy of the allowance for loan losses based on an analysis of the size and composition of the loan portfolio, the Bank's historical loss experience, including trends in non-performing and classified loans and charge-offs, economic conditions in the Bank's market area, and a review of selected individual loans. Loan losses are charged off against the allowance when individual loans are deemed uncollectible. Subsequent recoveries, if any, are credited to the allowance. The Bank believes it has established its existing allowance for loan losses in accordance with accounting principles generally accepted in the United States of America and is in compliance with appropriate regulatory guidelines. However, the establishment of the level of the allowance for loan losses is highly subjective and dependent on incomplete information as to the ultimate disposition of loans. Accordingly, there can be no assurance that actual losses may not vary from the amounts estimated or that the Bank's regulators will not require the Bank to significantly increase or decrease its allowance for loan losses, thereby affecting the Bank's financial condition and earnings. For a more complete discussion of the allowance for loan losses, see the section captioned "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies" in the Company's 2010 Annual Report to Stockholders.

Investment Activities

The Bank maintains a portfolio of investment securities to provide liquidity as well as a source of earnings. The Bank's investment securities portfolio consists primarily of mortgage-backed and other securities issued by U.S. government-sponsored enterprises ("GSEs"), including Freddie Mac and Fannie Mae. The Bank also has smaller holdings of privately issued mortgage-backed securities, U.S. Treasury obligations, and other equity and debt securities. As a member of the Federal Reserve and FHLB system, the Bank is required to maintain investments in the Federal Reserve Bank as a condition of membership and the Federal Home Loan Bank based upon levels of borrowings.

The following table sets forth the carrying value of the Company's investment securities portfolio and FHLB of Atlanta and Federal Reserve Bank stock at the dates indicated. At December 31, 2010, 2009, and 2008, their estimated fair value was \$168 million, \$148 million, and \$124 million, respectively.

	At December 31, (Dollars in Thousands)		
	2010	2009	2008
Asset-backed securities:			
Freddie Mac and Fannie Mae	\$ 144,861	\$ 121,510	\$ 93,049
Other	12,463	19,006	25,150
Total asset-backed securities	157,324	140,516	118,199
Corporate equity securities	37	39	157
Bond mutual funds	3,820	3,654	3,560
Treasury bills	753	-	1,000
Other Investments	-	5	17
Total investment securities	161,934	144,214	122,933
FHLB and Federal Reserve Bank stock	6,316	6,936	6,453
Total investment securities and FHLB and Federal Reserve Bank stock	\$ 168,250	\$ 151,150	\$ 129,386

The maturities and weighted average yields for investment securities available for sale (AFS) and held to maturity (HTM) at December 31, 2010 are shown below.

	One Year or Less		After One		After Five		After Ten Years	
	Amortized	Average	Amortized	Average	Amortized	Average	Amortized	Average
	Cost	Yield	Cost	Yield	Cost	Yield	Cost	Yield
(Dollars in Thousands)								
AFS Investment securities:								
Corporate equity securities	\$ 37	0.00 %	\$ -	0.00 %	\$ -	0.00 %	\$ -	0.00 %
Asset-backed securities	11,468	2.14 %	12,904	2.41 %	4,327	2.41 %	1,629	2.17 %
Mutual funds	3,697	3.41 %	-	0.00 %	-	0.00 %	-	0.00 %
Total AFS investment securities	\$ 15,202	2.44 %	\$ 12,904	2.41 %	\$ 4,327	2.41 %	\$ 1,629	2.17 %
HTM Investment securities:								
Asset-backed securities	\$ 36,223	2.66 %	\$ 61,310	2.75 %	\$ 21,990	2.63 %	\$ 6,712	2.29 %
Treasury bills	753	0.36 %	-	0.00 %	-	0.00 %	-	0.00 %
Other investments	-	0.00 %	-	0.00 %	-	0.00 %	-	0.00 %
Total HTM investment securities	\$ 36,976	2.61 %	\$ 61,310	2.75 %	\$ 21,990	2.63 %	\$ 6,712	2.29 %

The Bank's investment policy provides that securities that will be held for indefinite periods of time, including securities that will be used as part of the Bank's asset/liability management strategy and that may be sold in response to changes in interest rates, prepayments and similar factors, are classified as available for sale and accounted for at fair value. Management's intent is to hold securities reported at amortized cost to maturity. Certain of the Company's asset-backed securities are issued by private issuers (defined as an issuer that is not a government or a government-sponsored entity). The Company had no investments in any private issuer's securities that aggregate to more than 10% of the Company's equity.

Deposits and Other Sources of Funds

General. The funds needed by the Bank to make loans are primarily generated by deposit accounts solicited from the communities surrounding its main office and nine branches in the Southern Maryland area. Total deposits were \$724.6 million as of December 31, 2010. The Bank uses borrowings and other sources to supplement funding from deposits.

Deposits. The Bank's deposit products include savings, money market, demand deposit, IRA, SEP, Christmas clubs, and time deposit accounts. Variations in service charges, terms and interest rates are used to target specific markets. Ancillary products and services for deposit customers include safe deposit boxes, travelers checks, night depositories, automated clearinghouse transactions, wire transfers, ATMs, and online and telephone banking. The Bank is a member of ACCEL/Exchange, Cirrus, Maestro and Star ATM networks. The Bank has occasionally used deposit brokers to obtain funds. At December 31, 2010, the Bank had \$25.0 million in deposits from brokers compared to \$20.0 million at December 31, 2009. In addition the Bank utilizes the Certificate of Deposit Account Registry Service (CDARS) to provide existing customers with additional access to FDIC insurance. At December 31, 2010, the Bank maintained CDARS deposits of \$35.2 million compared to \$39.1 million at December 31, 2009.

The following table sets forth for the periods indicated the average balances outstanding and average interest rates for each major category of deposits.

	For the Year Ended December 31, (Dollars in Thousands)					
	2010		2009		2008	
	Average Balance	Average Rate	Average Balance	Average Rate	Average Balance	Average Rate
Savings	\$ 30,355	0.41 %	\$ 28,486	0.16 %	\$ 26,434	0.59 %
Interest-bearing demand and money market accounts	161,494	0.94 %	142,513	1.02 %	132,522	1.75 %
Certificates of deposit	421,525	2.21 %	355,489	3.02 %	268,363	3.93 %
Total interest-bearing deposits	613,374		526,488		427,320	
Noninterest-bearing demand deposits	65,041		53,584		42,955	
	\$ 678,415	1.61 %	\$ 580,072	2.11 %	\$ 470,275	2.77 %

The following table indicates the amount of the Bank's certificates of deposit and other time deposits of \$100,000 or more and \$250,000 or more by time remaining until maturity as of December 31, 2010.

Maturity Period	\$100K or More Certificates of Deposit (In Thousands)	\$250K or More Certificates of Deposit (In Thousands)
Three months or less	\$ 59,417	\$ 19,965
Three through six months	38,090	13,668
Six through twelve months	48,442	10,931
Over twelve months	86,586	40,209
Total	\$ 232,535	\$ 84,773

Borrowings. Deposits are the primary source of funds for the Bank's lending and investment activities and for its general business purposes. The Bank uses advances from the FHLB of Atlanta to supplement the supply of funds it may lend and to meet deposit withdrawal requirements. Advances from the FHLB are secured by the Bank's stock in the FHLB, a portion of the Bank's loan portfolio, and certain investments. Generally, the Bank's ability to borrow from the FHLB of Atlanta is limited by its available collateral and also by an overall limitation of 40% of assets. Further, short-term credit facilities are available at the Federal Reserve Bank of Richmond and other commercial banks. Other short-term debt consists of notes payable to the U.S. Treasury on treasury, tax and loan accounts. Long-term debt consists of adjustable-rate advances with rates based upon LIBOR, fixed-rate advances, and convertible advances. The table below sets forth information about borrowings for the years indicated.

	At or for the Year Ended December 31, (Dollars in Thousands)		
	2010	2009	2008
Long-term debt			
Long-term debt outstanding at end of period	\$70,624	\$75,670	\$104,963
Weighted average rate on outstanding long-term debt at end of period	3.24 %	3.26 %	3.81 %

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Maximum outstanding long-term debt of any month end	70,666		100,692		104,998	
Average outstanding long-term debt, during period	70,823		94,745		102,112	
Approximate average rate paid on long-term debt during period	3.22	%	3.70	%	4.09	%
Short-term borrowings						
Short-term borrowings outstanding at end of period at end of period	\$816		\$13,081		\$1,522	
Weighted average rate on short-term borrowings at end of period	0.00	%	0.34	%	1.83	%
Maximum outstanding short-term borrowings at any month end during period	\$11,322		\$13,081		\$20,943	
Average outstanding short-term borrowings	2,973		1,421		4,355	
Approximate average rate paid on short-term borrowings	1.41	%	2.06	%	3.59	%

For more information regarding the Bank's borrowings, see Note 10 of Notes to Consolidated Financial Statements.

Subsidiary Activities

In April 1997, the Bank formed a wholly owned subsidiary, Community Mortgage Corporation of Tri-County, to offer mortgage banking, brokerage, and other services to the public. This corporation is currently inactive.

The Company has two direct subsidiaries other than the Bank. In July 2004, Tri-County Capital Trust I was established as a statutory trust under Delaware law as a wholly-owned subsidiary of the Company to issue trust preferred securities. Tri-County Capital Trust I issued \$7.0 million of trust preferred securities on July 22, 2004. In June 2005, Tri-County Capital Trust II was also established as a statutory trust under Delaware law as a wholly owned subsidiary of the Company to issue trust preferred securities. Tri-County Capital Trust II issued \$5.0 million of trust preferred securities on June 15, 2005.

SUPERVISION AND REGULATION

Regulation of the Company

General. The Company is a public company registered with the Securities and Exchange Commission (the “SEC”) and, as the sole stockholder of the Bank, it is a bank holding company and registered as such with the Board of Governors of the Federal Reserve System. Bank holding companies are subject to comprehensive regulation by the Federal Reserve Board under the Bank Holding Company Act of 1956, as amended (the “BHCA”), and the regulations of the Federal Reserve Board. As a public company the Company is required to file annual, quarterly and current reports with the SEC, and as a bank holding company, the Company is required to file with the Federal Reserve Board annual reports and such additional information as the Federal Reserve Board may require, and is subject to regular examinations by the Federal Reserve Board. The Federal Reserve Board also has extensive enforcement authority over bank holding companies, including, among other things, the ability to assess civil money penalties, to issue cease and desist or removal orders, and to require that a holding company divest subsidiaries (including its bank subsidiaries). In general, enforcement actions may be initiated for violations of law and regulations and unsafe or unsound practices. The following discussion summarizes certain of the regulations applicable to the Company but does not purport to be a complete description of such regulations and is qualified in its entirety by reference to the actual laws and regulations involved.

Under the BHCA, a bank holding company must obtain Federal Reserve Board approval before: (1) acquiring, directly or indirectly, ownership or control of any voting shares of another bank or bank holding company if, after such acquisition, it would own or control more than 5% of such shares (unless it already owns or controls the majority of such shares); (2) acquiring all or substantially all of the assets of another bank or bank holding company; or (3) merging or consolidating with another bank holding company. In evaluating such application, the Federal Reserve Board considers factors such as the financial condition and managerial resources of the companies involved, the convenience and needs of the communities to be served and competitive factors.

The Riegle-Neal Interstate Banking and Branching Efficiency of 1994 (the “Riegle-Neal Act”) authorizes the Federal Reserve Board to approve an application of a bank holding company meeting certain qualitative criteria to acquire control of, or acquire all or substantially all of the assets of, a bank located in a state other than such holding company’s home state, without regard to whether the transaction is prohibited by the laws of any state. Under Maryland law, a bank holding company is prohibited from acquiring control of any bank if the bank holding company would control more than 30% of the total deposits of all depository institutions in the State of Maryland unless waived by the Commissioner of Financial Regulation. Additionally, the federal banking agencies are authorized to approve interstate bank merger transactions without regard to whether such transaction is prohibited by the law of any state, unless the home state of one of the banks opted out of the Riegle-Neal Act by adopting a law after the date of enactment of the Riegle-Neal Act and prior to June 1, 1997, which applies equally to all out-of-state banks and expressly prohibits merger transactions involving out-of-state banks. The State of Maryland did not pass such a law during this period. The BHCA also prohibits a bank holding company, with certain exceptions, from acquiring direct or indirect ownership or control of more than 5% of the voting shares of any company that is not a bank or bank holding company, or from engaging directly or indirectly in activities other than those of banking, managing or controlling banks, or providing services for its subsidiaries. The principal exceptions to these prohibitions involve certain non-bank activities which, by statute or by Federal Reserve Board regulation or order, have been identified as activities closely related to the business of banking or managing or controlling banks. The list of activities permitted by the Federal Reserve Board includes, among other things, operating a savings institution, mortgage company, finance company, credit card company or factoring company; performing certain data processing operations; providing certain investment and financial advice; underwriting and acting as an insurance agent for certain types of credit related insurance; leasing property on a full-payout, non-operating basis; selling money orders, travelers’ checks and United States Savings Bonds; real estate and personal property appraising; providing tax planning and preparation

services; and, subject to certain limitations, providing securities brokerage services for customers.

Bank holding companies that are “well capitalized” and “well managed” and whose financial institution subsidiaries have satisfactory Community Reinvestment Act records can elect to become “financial holding companies,” which are permitted to engage in a broader range of financial activities than are permitted to bank holding companies. The Company has not opted to become a financial holding company. The Federal Reserve Board has the power to order a holding company or its subsidiaries to terminate any activity, or to terminate its ownership or control of any subsidiary, when it has reasonable cause to believe that the continuation of such activity or such ownership or control constitutes a serious risk to the financial safety, soundness or stability of any bank subsidiary of that holding company.

Federal law provides that no person (broadly defined to include business entities) may acquire “control” of a bank holding company or insured bank without the approval of the appropriate federal regulator, which in the Company’s (and Bank’s) case is the Federal Reserve Board. Control is defined to mean direct or indirect ownership, control of, or holding irrevocable proxies representing 25% or more of any class of voting stock, control in any manner of the election of a majority of the bank’s directors or a determination by the Federal Reserve Board that the acquirer has or would have the power to exercise a controlling influence over the management or policies of the institution. Acquisition of more than 10% of any class of stock creates a rebuttable presumption of control under certain circumstances that requires that a filing be made with the Federal Reserve Board unless the Federal Reserve Board determines that the presumption has been rebutted. Any company that seeks to acquire 25% or more of a class of a bank’s voting stock, or otherwise acquire control, must first receive the prior approval of the Federal Reserve Board under the Bank Holding Company Act and no existing bank holding company may acquire more than 5% of any class of a nonsubsidiary bank’s voting stock without prior Federal Reserve Board approval.

The Maryland Financial Institutions Code prohibits a bank holding company from acquiring more than 5% of any class of voting stock of a bank or bank holding company without the approval of the Commissioner of Financial Regulation, except as otherwise expressly permitted by federal law or in certain other limited situations. The Maryland Financial Institutions Code additionally prohibits any person from acquiring voting stock in a bank or bank holding company without 60 days prior notice to the Commissioner if such acquisition will give the person control of 25% or more of the voting stock of the bank or bank holding company or will affect the power to direct or to cause the direction of the policy or management of the bank or bank holding company. Any doubt whether the stock acquisition will affect the power to direct or cause the direction of policy or management shall be resolved in favor of reporting to the Commissioner. The Commissioner may deny approval of the acquisition if the Commissioner determines it to be anti-competitive or to threaten the safety or soundness of a banking institution. Voting stock acquired in violation of this statute may not be voted for five years.

Dividends. The Federal Reserve Board has the power to prohibit dividends by bank holding companies if their actions constitute unsafe or unsound practices. The Federal Reserve Board has issued a policy statement on the payment of cash dividends by bank holding companies, which expresses the Federal Reserve Board’s view that a bank holding company should pay cash dividends only to the extent that the company’s net income for the past year is sufficient to cover both the cash dividends and a rate of earnings retention that is consistent with the company’s capital needs, asset quality and overall financial condition. The Federal Reserve Board also indicated that it would be inappropriate for a bank holding company experiencing serious financial problems to borrow funds to pay dividends. Under the prompt corrective action regulations adopted by the Federal Reserve Board, the Federal Reserve Board may prohibit a bank holding company from paying any dividends if the holding company’s bank subsidiary is classified as “undercapitalized.” See “Regulation of the Bank – Capital Adequacy.” The Dodd-Frank Act codified the source of strength doctrine requiring bank holding companies to serve as a source of strength for their depository subsidiaries and required the issuance of implementing regulations.

Stock Repurchases. As a bank holding company, the Company is required to give the Federal Reserve Board prior written notice of any purchase or redemption of its outstanding equity securities if the gross consideration for the purchase or redemption, when combined with the net consideration paid for all such purchases or redemptions during

the preceding 12 months, is equal to 10% or more of the Company's consolidated net worth. The Federal Reserve Board may disapprove such a purchase or redemption. This requirement does not apply to bank holding companies that are "well capitalized," "well-managed" and are not the subject of any unresolved supervisory issues.

Capital Requirements. The Federal Reserve Board has adopted guidelines regarding the capital adequacy of bank holding companies, which require bank holding companies to maintain on a consolidated basis, specified minimum ratios of capital to total assets and capital to risk-weighted assets. These requirements, which generally apply to bank holding companies with consolidated assets of \$500 million or more, are substantially similar to, but somewhat more generous than, those applicable to the Bank. See “– Regulation of the Bank – Capital Adequacy.” The Dodd-Frank Act required the Federal Reserve Board to adopt consolidated capital requirements for holding companies that are equally as stringent as those applicable to the depository institution subsidiaries. That means that certain instruments that had previously been includable in Tier 1 capital for bank holding companies, such as trust preferred securities, will no longer be eligible for inclusion. The revised capital requirements are subject to certain grandfathering and transition rules. The Company is currently considered a grandfathered institution under these rules.

Regulation of the Bank

General. The Bank is a Maryland commercial bank and its deposit accounts are insured by the Deposit Insurance Fund of the Federal Deposit Insurance Corporation. The Bank is a member of the Federal Reserve and FHLB systems. The Bank is subject to supervision, examination and regulation by Commissioner of Financial Regulation of the State of Maryland (the “Commissioner”) and the Federal Reserve Board and to Maryland and federal statutory and regulatory provisions governing such matters as capital standards, mergers, and establishment of branch offices. The Federal Deposit Insurance Corporation, as deposit insurer, has certain secondary examination and supervisory authority. The Bank is required to file reports with the Commissioner and the Federal Reserve Board concerning its activities and financial condition and is required to obtain regulatory approvals prior to entering into certain transactions, including mergers with, or acquisitions of, other depository institutions.

As an institution with federally insured deposits, the Bank is subject to various operational regulations promulgated by the Federal Reserve Board, including Regulation B (Equal Credit Opportunity), Regulation D (Reserve Requirements), Regulation E (Electronic Fund Transfers), Regulation P (Privacy), Regulation W (Transactions Between Member Banks and Their Affiliates), Regulation Z (Truth in Lending), Regulation CC (Availability of Funds and Collection of Checks) and Regulation DD (Truth in Savings).

The Dodd-Frank Act provides for the establishment of the Consumer Financial Protection Bureau as an independent bureau of the Federal Reserve Board. The Consumer Financial Protection Bureau will assume responsibility for implementing federal consumer financial protection and fair lending laws and regulations, a function currently handled by federal bank regulatory agencies.

The system of regulation and supervision applicable to the Bank establishes a comprehensive framework for the operations of the Bank and gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities. Changes in the regulatory framework could have a material effect on the Bank and its respective operations that in turn, could have a material effect on the Company. The following discussion summarizes certain regulations applicable to the Bank but does not purport to be a complete description of such regulations and is qualified in its entirety by reference to the actual laws and regulations involved.

Capital Adequacy. The Federal Reserve Board has established guidelines with respect to the maintenance of appropriate levels of capital by bank holding companies and state member banks, respectively. The regulations impose two sets of capital adequacy requirements: minimum leverage rules, which require bank holding companies and member banks to maintain a specified minimum ratio of capital-to-total assets, and risk-based capital rules, which require the maintenance of specified minimum ratios of capital to “risk-weighted” assets.

The regulations of the Federal Reserve Board require bank holding companies and state member banks, respectively, to maintain a minimum leverage ratio of “Tier 1 capital” (as defined in the risk-based capital guidelines discussed in the

following paragraphs) to total assets of 3.0%. Although setting a minimum 3.0% leverage ratio, the capital regulations state that only the strongest bank holding companies and banks, with composite examination ratings of 1 under the rating system used by the federal bank regulators, would be permitted to operate at or near such minimum level of capital. All other bank holding companies and banks are expected to maintain a leverage ratio of at least 4.0%. Any bank or bank holding company experiencing or anticipating significant growth would be expected to maintain capital well above the minimum levels. In addition, the Federal Reserve Board has indicated that whenever appropriate, and in particular when a bank holding company is undertaking expansion, seeking to engage in new activities, or otherwise facing unusual or abnormal risks, it will consider, on a case-by-case basis, the level of an organization's ratio of tangible Tier 1 capital (after deducting all intangibles) to total assets in making an overall assessment of capital.

The risk-based capital rules of the Federal Reserve Board require bank holding companies and state member banks, respectively, to maintain minimum regulatory capital levels based upon a weighting of their assets and off-balance sheet obligations according to risk. Risk-based capital is composed of two elements: Tier 1 capital and Tier 2 capital. Tier 1 capital consists primarily of common stockholders' equity, certain perpetual preferred stock (which must be noncumulative in the case of banks), and minority interests in the equity accounts of consolidated subsidiaries; less all intangible assets, except for certain servicing assets, purchased credit card relationships, deferred tax assets and credit enhancing interest-only strips. Tier 2 capital elements include, subject to certain limitations, the allowance for losses on loans and leases; perpetual preferred stock that does not qualify as Tier 1 capital and long-term preferred stock with an original maturity of at least 20 years from issuance; hybrid capital instruments, including perpetual debt and mandatory convertible securities, subordinated debt and intermediate-term preferred stock and up to 45% of unrealized gains on available for sale equity securities with readily determinable market values.

The risk-based capital regulations assign balance sheet assets and credit equivalent amounts of off-balance sheet obligations to one of four broad risk categories based principally on the degree of credit risk associated with the obligor. The assets and off-balance sheet items in the four risk categories are weighted at 0%, 20%, 50% and 100%. These computations result in the total risk-weighted assets. The risk-based capital regulations require all banks and bank holding companies to maintain a minimum ratio of total capital (Tier 1 capital plus Tier 2 capital) to total risk-weighted assets of 8%, with at least 4% as Tier 1 capital. For the purpose of calculating these ratios: (i) Tier 2 capital is limited to no more than 100% of Tier 1 capital; and (ii) the aggregate amount of certain types of Tier 2 capital is limited. In addition, the risk-based capital regulations limit the allowance for loan losses includable as capital to 1.25% of total risk-weighted assets.

Federal Reserve Board regulations and guidelines additionally specify that state member banks with significant exposure to declines in the economic value of their capital due to changes in interest rates may be required to maintain higher risk-based capital ratios.

The Federal Reserve Board has issued regulations that classify state member banks by capital levels and which authorize the Federal Reserve Board to take various prompt corrective actions to resolve the problems of any bank that fails to satisfy the capital standards. Under such regulations, a well capitalized bank is one that is not subject to any regulatory order or directive to meet any specific capital level and has or exceeds the following capital levels: a total risk-based capital ratio of 10%, a Tier 1 risk-based capital ratio of 6%, and a leverage ratio of 5%. An adequately capitalized bank is one that does not qualify as well capitalized but meets or exceeds the following capital requirements: a total risk-based capital ratio of 8%, a Tier 1 risk-based capital ratio of 4%, and a leverage ratio of either (1) 4% or (2) 3% if the bank has the highest composite examination rating. A bank not meeting these criteria is treated as undercapitalized, significantly undercapitalized, or critically undercapitalized depending on the extent to which the bank's capital levels are below these standards. A state member bank that falls within any of the three undercapitalized categories established by the prompt corrective action regulation will be subject to regulatory sanctions. As of December 31, 2010, the Bank was well capitalized as defined by the Federal Reserve Board's regulations.

Branching. Maryland law provides that, with the approval of the Commissioner, Maryland banks may establish branches within the State of Maryland without geographic restriction and may establish branches in other states by any means permitted by the laws of such state or by federal law. The Riegle-Neal Act authorizes the Federal Reserve Board to approve interstate branching by merger by state member banks in any state that did not opt out and de novo in states that specifically allow for such branching. These regulations include guidelines to ensure that interstate branches operated by an out-of-state bank in a host state are reasonably helping to meet the credit needs of the communities which they serve.

Dividend Limitations. Pursuant to the Maryland Financial Institutions Code, Maryland banks may only pay dividends from undivided profits or, with the prior approval of the Commissioner, their surplus in excess of 100% of required capital stock. The Maryland Financial Institutions Code further restricts the payment of dividends by prohibiting a Maryland bank from declaring a dividend on its shares of common stock until its surplus fund equals the amount of required capital stock or, if the surplus fund does not equal the amount of capital stock, in an amount in excess of 90% of net earnings.

Without the approval of the Federal Reserve Board, a state member bank may not declare or pay a dividend if the total of all dividends declared during the year exceeds its net income during the current calendar year and retained net income for the prior two years. The Bank is further prohibited from making a capital distribution if it would be thereafter undercapitalized within the meaning of the prompt corrective action regulations discussed above. In addition, the Bank may not make a capital distribution that would reduce its net worth below the amount required to maintain the liquidation account established for the benefit of its depositors at the time of its conversion to stock form.

Insurance of Deposit Accounts. The Bank's deposits are insured up to applicable limits by the Deposit Insurance Fund of the Federal Deposit Insurance Corporation. Under the Federal Deposit Insurance Corporation's existing assessment system, insured institutions are assigned to one of four categories based on supervisory evaluations, regulatory capital levels and certain other factors. An institution's assessment rate depends upon the category to which it is assigned and certain potential adjustments established by Federal Deposit Insurance Corporation regulations. Currently, the applicable initial base assessment rates range from 12 to 45 basis points, and total base assessment rates can range from 7 to 77.5 basis points after adjustments. The Federal Deposit Insurance Corporation may adjust the scale uniformly from one quarter to the next, except that no adjustment can deviate more than three basis points from the base scale without notice and comment. On February 7, 2011, the Federal Deposit Insurance Corporation issued a final rule regarding the risk-based deposit insurance assessment system that better reflects the risks to the Deposit Insurance Fund. Under the final rule effective April 1, 2011 new initial base assessment rates will range from 5 to 35 basis points, and total base assessment rates will range from 2.5 to 45 basis points after adjustments. No institution may pay a dividend if in default of the federal deposit insurance assessment.

The Federal Deposit Insurance Corporation imposed on all insured institutions a special emergency assessment of five basis points of total assets minus Tier 1 capital, as of June 30, 2009 (capped at ten basis points of an institution's deposit assessment base), to cover losses to the Deposit Insurance Fund. That special assessment was collected on September 30, 2009. In lieu of further special assessments, the Federal Deposit Insurance Corporation required insured institutions to prepay estimated quarterly risk-based assessments for the fourth quarter of 2009 through the fourth quarter of 2012. The estimated assessments, which include an assumed annual assessment base increase of 5%, were recorded as a prepaid expense asset as of December 30, 2009. As of December 31, 2009, and each quarter thereafter, a charge to earnings is recorded for each regular assessment with an offsetting credit to the prepaid asset.

Because of the recent difficult economic conditions, deposit insurance per account owner had been temporarily raised to \$250,000 for all types of accounts. That level was made permanent by the Dodd-Frank Act. In addition, the Federal Deposit Insurance Corporation adopted an optional Temporary Liquidity Guarantee Program ("TLGP") under which, for a fee, noninterest-bearing transaction accounts would receive unlimited insurance coverage until June 30, 2010, subsequently extended to December 31, 2010. The Dodd-Frank Act extended the unlimited coverage of certain noninterest-bearing transaction accounts until December 31, 2012 without providing an opt out.

In addition to the assessment for deposit insurance, institutions are required to make payments on bonds issued in the late 1980s by the Financing Corporation to recapitalize a predecessor deposit insurance fund. This payment is established quarterly and during the four quarters ended December 31, 2010 averaged 1.04 basis points of assessable deposits.

The Federal Deposit Insurance Corporation has authority to increase insurance assessments. In addition, the Dodd-Frank Act requires that the Federal Deposit Insurance Corporation amend its assessment system to base it on total assets less tangible equity rather than deposits. 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 Federal Deposit Insurance Corporation upon a finding that the 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 Federal Deposit Insurance Corporation. The management of the Bank does not know of any practice, condition or violation that might lead to termination of deposit insurance.

Safety and Soundness Guidelines. Each federal banking agency was required to establish safety and soundness standards for the depository institutions under its authority. The interagency guidelines require depository institutions to maintain internal controls and information systems and internal audit systems that are appropriate for the size, nature and scope of the institution's business. The guidelines also establish certain basic standards for loan documentation, credit underwriting, interest rate risk exposure and asset growth. The guidelines further provide that depository institutions should maintain safeguards to prevent the payment of compensation, fees and benefits that are excessive or that could lead to material financial loss, and should take into account factors such as compensation practices at comparable institutions. If the appropriate federal banking agency determines that a depository institution is not in compliance with the safety and soundness guidelines, it may require the institution to submit an acceptable plan to achieve compliance with the guidelines. Failure to submit or implement a compliance plan may subject the institution to regulatory sanctions. Management believes that the Bank meets all the standards adopted in the interagency guidelines.

Reserve Requirements. Under Federal Reserve Board regulations, the Bank currently must maintain average daily reserves equal to 3% on aggregate transaction, plus 10% on the remainder. The first \$10.7 million of transaction accounts are exempt. This percentage is subject to adjustment by the Federal Reserve Board. Because required reserves must be maintained in the form of vault cash or in a noninterest-bearing account at a Federal Reserve Bank, the effect of the reserve requirement is to reduce the amount of the institution's interest-earning assets. At December 31, 2010, the Bank met applicable Federal Reserve Board reserve requirements.

Federal Home Loan Bank System. The Bank is a member of the Federal Home Loan Bank System, which consists of 12 regional Federal Home Loan Banks governed and regulated by the Federal Housing Finance Board ("FHFB"). As a member, the Bank is required to purchase and hold stock in the FHLB of Atlanta. As of December 31, 2010, the Bank held \$5.2 million of stock in the FHLB of Atlanta and was in compliance with the above requirement.

Transactions with Affiliates. A state member bank or its subsidiaries may not engage in "covered transactions" with any one affiliate in an amount greater than 10% of such bank's capital stock and surplus, and for all such transactions with all affiliates a state member bank is limited to an amount equal to 20% of capital stock and surplus. All such transactions must also be on terms substantially the same, or at least as favorable, to the bank or subsidiary as those provided to a non-affiliate. The term "covered transaction" includes the making of loans, purchase of assets, issuance of a guarantee and similar types of transactions. Certain covered transactions, such as loans to affiliates, must meet specified collateral requirements. The BHCA further prohibits a depository institution from extending credit to or offering any other services, or fixing or varying the consideration for such extension of credit or service, on the condition that the customer obtain some additional service from the institution or certain of its affiliates or not obtain services of a competitor of the institution, subject to certain limited exceptions. At December 31, 2010, we had no transactions with affiliates.

Loans to Directors, Executive Officers and Principal Stockholders. Loans to directors, executive officers and principal stockholders of a state member bank must be made on substantially the same terms as those prevailing for comparable transactions with persons who are not executive officers, directors, principal stockholders or employees of the bank unless the loan is made pursuant to a compensation or benefit plan that is widely available to employees and does not favor insiders. Loans to any executive officer, director and principal stockholder together with all other outstanding loans to such person and affiliated interests generally may not exceed 15% of the Bank's unimpaired capital and surplus and all loans to such persons may not exceed the institution's unimpaired capital and unimpaired surplus. Loans to directors, executive officers and principal stockholders, and their respective affiliates, in excess of the greater of \$25,000 or 5% of capital and surplus, or any loans cumulatively aggregating \$500,000 or more, must be approved in advance by a majority of the board of directors of the bank with any "interested" director not participating in the voting. State member banks are prohibited from paying the overdrafts of any of their executive officers or directors unless payment is made pursuant to a written, pre-authorized interest-bearing extension of credit plan that

specifies a method of repayment or transfer of funds from another account at the bank. In addition, loans to executive officers may not be made on terms more favorable than those afforded other borrowers and are restricted as to type, amount and terms of credit.

Enforcement. The Commissioner has extensive enforcement authority over Maryland banks. Such authority includes the ability to issue cease and desist orders and civil money penalties and to remove directors or officers. The Commissioner may also take possession of a Maryland bank whose capital is impaired and seek to have a receiver appointed by a court.

The Federal Reserve Board has primary federal enforcement responsibility over state banks under its jurisdiction, including the authority to bring enforcement action against all “institution-related parties,” including stockholders, and any attorneys, appraisers and accountants who knowingly or recklessly participate in wrongful action likely to have an adverse effect on an institution. Formal enforcement action may range from the issuance of capital directive or a cease and desist order for the removal of officers and/or directors, receivership, conservatorship or termination of deposit insurance. Civil money penalties cover a wide range of violations and actions, and range up to \$25,000 per day or even up to \$1 million per day (in the most egregious cases). Criminal penalties for most financial institution crimes include fines of up to \$1 million and imprisonment for up to 30 years.

Regulatory Restructuring Legislation. On July 21, 2010, President Obama signed into law the Dodd-Frank Act, which is legislation that restructures the regulation of depository institutions. In addition to creating the Consumer Financial Protection Bureau, the Dodd-Frank Act, among other things, requires changes in the way that institutions are assessed for deposit insurance, authorizes the payment of interest on business checking accounts, mandates the imposition of consolidated capital requirements on holding companies that are less stringent than those applicable to the subsidiary institution, requires that originators of securitized loans retain a percentage of the risk for the transferred loans, requires the Federal Reserve Board to regulate pricing of certain debit card interchange fees, reduces the federal preemption afforded to national banks and federal savings associations and contains a number of reforms related to mortgage origination. Many of the provisions of the Dodd-Frank Act contain delayed effective dates and require the issuance of regulations. Consequently, it will be some time before their impact on operations can be assessed by management. However, there is a significant possibility that the Dodd-Frank Act will, at a minimum, result in an increased regulatory burden and higher compliance, operating, and possibly, interest expense costs for the Company and the Bank.

Personnel

As of December 31, 2010, the Bank had 131 full-time employees and 11 part-time employees. The employees are not represented by a collective bargaining agreement. The Bank believes its employee relations are good.

Executive Officers of the Registrant

The executive officers of the Company are as follows:

Michael L. Middleton (63 years old) is Chairman, President and Chief Executive Officer of the Company and Chairman and Chief Executive Officer of the Bank. Mr. Middleton joined the Bank in 1973 and served in various management positions until 1979 when he became President of the Bank until April 1, 2010. Mr. Middleton is a Certified Public Accountant and holds a Masters of Business Administration. From 1996 to 2004, Mr. Middleton served on the Board of Directors of the Federal Home Loan Bank of Atlanta, serving as Chairman of the Board in 2004. Mr. Middleton served on the Board of Directors of the Federal Reserve Bank, Baltimore Branch, from 2004 to 2009. He is Vice Chairman of the Maryland Bankers Association, a trustee for the College of Southern Maryland, Chairman of the Board of the Energetics Technology Center and serves on the Federal Reserve's Community Depository Institutions Advisory Council. He also serves on several philanthropic and civic boards.

William J. Pasenelli (52 years old) is Executive Vice President and Chief Financial Officer of the Company and President and Chief Financial Officer of the Bank. Mr. Pasenelli joined the Bank as Chief Financial Officer in April 2000 and was named President in 2010. Before joining the Bank, Mr. Pasenelli had been Chief Financial Officer of Acacia Federal Savings Bank, Annandale, Virginia, since 1987. Mr. Pasenelli is a member of the American Institute of Certified Public Accountants, the Greater Washington Society of Certified Public Accountants and other civic groups.

Gregory C. Cockerham (56 years old) joined the Bank in 1988. He serves as the Bank's Executive Vice President – Chief Lending Officer. Prior to joining the Company he was retail Vice President of Maryland National Bank. Mr. Cockerham serves as Chairman of the College of Southern Maryland Foundation and the Maryland Title Center. He is a Paul Harris Fellow with the Rotary Club of Charles County and serves on various civic boards in Charles County.

James M. Burke (42 years old) joined the Bank in 2006. He serves as the Bank's Executive Vice President – Chief Credit Officer. Before his appointment as Executive Vice President in 2007, he served as the Bank's Senior Credit Officer. Prior to joining the Bank, Mr. Burke served as Executive Vice President of Mercantile Southern Maryland Bank. Mr. Burke has almost 20 years of banking experience. Mr. Burke is the former Chairman of the Board of Directors of Civista Medical Center and is active in other civic groups.

James F. DiMisa (51 years old) joined the Bank in 2006. He serves as Executive Vice President- Chief Operating Officer. Prior to joining the Bank, Mr. DiMisa served as Executive Vice President of Mercantile Southern Maryland Bank. Mr. DiMisa has over 30 years of banking experience. Mr. DiMisa is Chairman of the Board of Trustees for the Maryland Bankers School and a member of several other civic and professional groups. Mr. DiMisa is a Stonier Graduate School of Banking graduate and holds a Masters of Business Administration.

Item 1A. Risk Factors

An investment in shares of our common stock involves various risks. Our business, financial condition and results of operations could be harmed by any of the following risks or by other risks that have not been identified or that we may believe are immaterial or unlikely. The value or market price of our common stock could decline due to any of these risks, and you may lose all or part of your investment. The risks discussed below also include forward-looking statements, and our actual results may differ substantially from those discussed in these forward-looking statements.

Our provision for loan losses increased during the past year and we may be required to make further increases in our provision for loan losses and to charge-off additional loans in the future, especially due to our level of non-performing assets. Further, our allowance for loan losses may prove to be insufficient to absorb losses in our loan portfolio.

For 2010, we recorded a provision for loan losses of \$3.9 million. We also recorded net loan charge-offs of \$3.7 million. Our non-performing assets, including troubled debt restructures, increased in 2010 from \$31.8 million, or 3.9% of total assets, at December 31, 2009 to \$40.6 million, or 4.58% of total assets, at December 31, 2010. The increase was primarily due to the weakened economy and the softening real estate market. If the economy and/or the real estate market continue to weaken, we may be required to add further reserves to our allowance for loan losses for these assets as the value of the collateral may be insufficient to pay any remaining net loan balance, which could have a negative effect on our results of operations. Like all financial institutions, we maintain an allowance for loan losses to provide for loans in our portfolio that may not be repaid in their entirety. We believe that our allowance for loan losses is maintained at a level adequate to absorb probable losses inherent in our loan portfolio as of the corresponding balance sheet date. However, our allowance for loan losses may not be sufficient to cover actual loan losses, and future provisions for loan losses could materially adversely affect our operating results.

In evaluating the adequacy of our allowance for loan losses, we consider numerous quantitative factors, including our historical charge-off experience, growth of our loan portfolio, changes in the composition of our loan portfolio and the volume of delinquent and classified loans, troubled debt restructures and foreclosed real estate. In addition, we use information about specific borrower situations, including their financial position and estimated collateral values, to estimate the risk and amount of loss for those borrowers. Finally, we also consider many qualitative factors, including general and economic business conditions, anticipated duration of the current business cycle, current general market collateral valuations, trends apparent in any of the factors we take into account and other matters, which are, by nature, more subjective and fluid. Our estimates of the risk of loss and amount of loss on any loan are complicated by the significant uncertainties surrounding our borrowers' abilities to successfully execute their business models through changing economic environments, competitive challenges and other factors. Because of the degree of uncertainty and susceptibility of these factors to change, our actual losses may vary from our current estimates.

Our regulators, as an integral part of their examination process, periodically review our allowance for loan losses and may require us to increase our allowance for loan losses by recognizing additional provisions for loan losses charged to expense, or to decrease our allowance for loan losses by recognizing loan charge-offs. Any such additional provisions for loan losses or charge-offs, as required by these regulatory agencies, could have a material adverse effect on our financial condition and results of operations.

Changes in interest rates could reduce our net interest income and earnings.

Our largest component of earnings is net interest income, which could be negatively affected by changes in interest rates. The Company's balance sheet is sensitive to changes in market and competitive interest rates. Changing interest rates impact customer actions and may limit the options available to the Company to maximize earnings or increase the costs to minimize risk. We do not have control over market interest rates and the Company's focus to mitigate potential earnings risk centers on controlling the composition of our asset and liability holdings.

Our net interest income is the interest we earn on loans and investment less the interest we pay on our deposits and borrowings. Our net interest margin is the difference between the yield we earn on our assets and the interest rate we pay for deposits and our other sources of funding. Changes in interest rates—up or down—could adversely affect our net interest margin and, as a result, our net interest income. Although the yield we earn on our assets and our funding costs tend to move in the same direction in response to changes in interest rates, one can rise or fall faster than the other, causing our net interest margin to expand or contract. Our liabilities tend to be shorter in duration than our assets, so they may adjust faster in response to changes in interest rates. As a result, when interest rates rise, our funding costs may rise faster than the yield we earn on our assets, causing our net interest margin to contract until the yield catches up. Changes in the slope of the “yield curve”—or the spread between short-term and long-term interest rates—could also reduce our net interest margin. Normally, the yield curve is upward sloping, meaning short-term rates are lower than long-term rates. Because our liabilities tend to be shorter in duration than our assets, when the yield curve flattens or inverts, we could experience pressure on our net interest margin as our cost of funds increases relative to the yield we can earn on our assets.

Our increased emphasis on commercial and construction lending may expose us to increased lending risks.

At December 31, 2010, our loan portfolio consisted of \$336.3 million, or 50.7%, of commercial real estate loans, \$104.6 million, or 15.8%, of commercial business loans and \$18.0 million, or 2.7%, of commercial equipment loans. We intend to maintain our emphasis on these types of loans. These types of loans generally expose a lender to greater risk of non-payment and loss than one- to four-family residential mortgage loans because repayment of the loans often depends on the successful operation of the property and the income stream of the borrowers. Such loans typically involve larger loan balances to single borrowers or groups of related borrowers compared to one- to four-family residential mortgage loans. Commercial business and equipment loans expose us to additional risks since they typically are made on the basis of the borrower’s ability to make repayments from the cash flows of the borrower’s business and are secured by non-real estate collateral that may depreciate over time. In addition, since such loans generally entail greater risk than one- to four-family residential mortgage loans, we may need to increase our allowance for loan losses in the future to account for the likely increase in probable incurred credit losses associated with the growth of such loans. Also, many of our commercial borrowers have more than one loan outstanding with us. Consequently, an adverse development with respect to one loan or one credit relationship can expose us to a significantly greater risk of loss compared to an adverse development with respect to a one- to four-family residential mortgage loan.

The economic recession could result in increases in our level of non-performing loans and/or reduce demand for our products and services, which would lead to lower revenue, higher loan losses and lower earnings.

Our business activities and earnings are affected by general business conditions in the United States and in our local market area. These conditions include short-term and long-term interest rates, inflation, unemployment levels, monetary supply, consumer confidence and spending, fluctuations in both debt and equity capital markets, and the strength of the economy in the United States generally and in our market area in particular. The national economy has recently experienced a recession, with rising unemployment levels, declines in real estate values and an erosion in consumer confidence. Dramatic declines in the U.S. housing market over the past few years, with falling home prices and increasing foreclosures, have negatively affected the performance of mortgage loans and resulted in significant write-downs of asset values by many financial institutions, including the Bank. A prolonged or more severe economic downturn, continued elevated levels of unemployment, further declines in the values of real estate, or other events that affect household and/or corporate incomes could further impair the ability of our borrowers to repay their loans in accordance with their terms. Nearly all of our loans are secured by real estate or made to businesses in southern Maryland. As a result of this concentration, a prolonged or more severe downturn in the local economy could result in significant increases in nonperforming loans, which would negatively impact our interest income and result in higher provisions for loan losses, which would hurt our earnings. Continuation of the economic downturn could also result

in reduced demand for credit or fee-based products and services, which would hurt our revenues.

The unseasoned nature of our commercial loan portfolio may result in changes in estimating collectability, which may lead to additional provisions or charge-offs, which could hurt our profits.

Our commercial real estate, commercial business and commercial equipment loans increased \$100.0 million, or 27.9%, from \$358.8 million at December 31, 2008 to \$458.8 million at December 31, 2010. A large portion of our commercial loan portfolio is unseasoned and does not provide us with a significant payment history pattern from which to judge future collectability, especially in this period of continued declining and unfavorable economic conditions. As a result, it may be difficult to predict the future performance of this part of our loan portfolio. These loans may have delinquency or charge-off levels above our historical experience, which could adversely affect our future performance. Further, these types of loans generally have larger balances and involve a greater risk than one- to four-family residential mortgage loans. Accordingly, if we make any errors in judgment in the collectability of our commercial loans, any resulting charge-offs may be larger on a per loan basis than those incurred historically with our residential mortgage loan or consumer loan portfolios.

Our asset valuation may include methodologies, estimations and assumptions that are subject to differing interpretations and could result in changes to asset valuations that may materially adversely affect our results of operations or financial condition.

We must use estimates, assumptions, and judgments when financial assets and liabilities are measured and reported at fair value. Assets and liabilities carried at fair value inherently result in a higher degree of financial statement volatility. Fair values and the information used to record valuation adjustments for certain assets and liabilities are based on quoted market prices and/or other observable inputs provided by independent third-party sources, when available. When such third-party information is not available, we estimate fair value primarily by using cash flows and other financial modeling techniques utilizing assumptions such as credit quality, liquidity, interest rates and other relevant inputs. Changes in underlying factors, assumptions, or estimates in any of these areas could materially impact our future financial condition and results of operations.

During periods of market disruption, including periods of significantly rising or high interest rates, rapidly widening credit spreads or illiquidity, it may be difficult to value certain of our assets if trading becomes less frequent and/or market data becomes less observable. There may be certain asset classes that were in active markets with significant observable data that become illiquid due to the current financial environment. In such cases, certain asset valuations may require more subjectivity and management judgment. As such, valuations may include inputs and assumptions that are less observable or require greater estimation. Further, rapidly changing and unprecedented credit and equity market conditions could materially impact the valuation of assets as reported within our consolidated financial statements, and the period-to-period changes in value could vary significantly. Decreases in value may have a material adverse effect on our results of operations or financial condition.

Our inability to retain deposits as they become due may cause us to rely more heavily on wholesale funding strategies, which could increase our expenses and adversely affect our operating margins and profitability.

A large percentage of our certificates of deposit have maturities of less than one year. The Bank has marketing and pricing initiatives to retain these certificates of deposit when they mature, however, there can be no guarantee that we will retain the deposits necessary to continue to fund asset growth at reasonable prices. If we are not able to maintain sufficient deposits, we will have to rely more heavily on wholesale strategies to fund our asset growth, which historically are more expensive than retail sources of funding. If we are required to rely more heavily on more expensive funding sources to support future growth, our revenues may not increase proportionately to cover our costs. In this case, our operating margins and profitability would be adversely affected.

Our continued pace of growth may require us to raise additional capital in the future, which will be dilutive to existing shareholders and could dilute our per share book value.

We are required by regulatory authorities to maintain adequate levels of capital to support our operations. We anticipate that we have sufficient capital resources to satisfy our capital requirements for the foreseeable future. We may at some point, however, need to raise additional capital to support our continued growth. If we raise capital through the issuance of additional shares of our common stock or other securities, it would dilute the ownership interests of existing shareholders and may dilute the per share book value of our common stock. New investors may also have rights, preferences and privileges senior to our current shareholders, which may adversely impact our current shareholders.

Our ability to raise additional capital, if needed, will depend on conditions in the capital markets at that time, which are outside of our control, and on our financial performance. Accordingly, we may not be able to raise additional capital, if needed, on terms acceptable to us. If we cannot raise additional capital when needed, our ability to further expand our operations through internal growth could be materially impaired.

Recently enacted regulatory reform may have a material impact on our operations.

On July 21, 2010, the President signed into law The Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”). The Dodd-Frank Act restructures the regulation of depository institutions. The Dodd-Frank Act also creates a new federal agency to administer consumer protection and fair lending laws, a function that is now performed by the depository institution regulators. The federal preemption of state laws currently accorded federally chartered depository institutions will be reduced as well, and State Attorneys General will have greater authority to bring a suit against a federally chartered institution for violations of certain state and federal consumer protection laws. The Dodd-Frank Act contains various other provisions designed to enhance the regulation of depository institutions. The full impact of the Dodd-Frank Act on our business and operations will not be known for years until regulations implementing the statute are written and adopted. The Dodd-Frank Act may have a material impact on our operations, particularly through increased regulatory burden and compliance costs.

The limitations on dividends and repurchases imposed through our participation in the Capital Purchase Program may make our common stock a less attractive investment.

On December 19, 2008, the United States Department of the Treasury purchased newly issued shares of our preferred stock as part of the Troubled Asset Relief Program’s Capital Purchase Program. As part of this transaction, we agreed to not increase the dividend paid on our common stock and to not repurchase shares of our common stock for a period of three years, without prior approval of the Treasury. These capital management devices contribute to the attractiveness of our common stock and limitations and prohibitions on such activities may make our common stock less attractive to investors.

The limitations on executive compensation imposed through our participation in the Capital Purchase Program may restrict our ability to attract, retain and motivate key employees, which could adversely affect our operations.

As part of our participation in the Capital Purchase Program, we agreed to be bound by certain executive compensation restrictions, including limitations on severance payments and the clawback of any bonus and incentive compensation that were based on materially inaccurate financial statements or any other materially inaccurate performance metric criteria. Subsequent to the issuance of the preferred stock, the President signed the American Recovery and Reinvestment Act of 2009 into law, which provided more stringent limitations on severance pay and the payment of bonuses. To the extent that any of these compensation restrictions do not permit us to provide a comprehensive compensation package to our key employees that is competitive in our market area, we may have difficulty in attracting, retaining and motivating our key employees, which could have an adverse effect on our results of operations.

The terms governing the issuance of the preferred stock to the Treasury may be changed, the effect of which may have an adverse effect on our operations.

The terms of the agreement we entered into with the Treasury provides that the Treasury may unilaterally amend any provision of the Securities Purchase Agreement to the extent required to comply with any changes in applicable federal statutes that may occur in the future. The American Recovery and Reinvestment Act of 2009, which placed more stringent limits on executive compensation, including a prohibition on the payment of bonuses or severance and a requirement that compensation paid to executives be presented to shareholders for a “non-binding” vote. We have no

assurances that further changes in the terms of the transaction will not occur in the future. Such changes may place further restrictions on our business or results of operation, which may adversely affect the market price of our common stock.

Strong competition within our market area could hurt our profits and slow growth.

We face intense competition both in making loans and attracting deposits. This competition may make it more difficult for us to originate new loans and may force us to offer higher deposit rates than currently. Price competition for loans and deposits might result in lower interest rates earned on our loans and higher interest rates paid on our deposits, which would reduce net interest income. According to the Federal Deposit Insurance Corporation, as of June 30, 2010, we held 17.7% of the deposits in Calvert, Charles and St. Mary's counties, Maryland, which was the third largest market share of deposits out of the 14 financial institutions that held deposits in these counties. Some of the institutions with which we compete have substantially greater resources and lending limits than we have and may offer services that we do not provide. We expect competition to increase in the future as a result of legislative, regulatory and technological changes and the continuing trend of consolidation in the financial services industry. Our profitability depends upon our continued ability to compete successfully in our market area.

If the value of real estate in Southern Maryland were to continue to decline, a significant portion of our loan portfolio could become under-collateralized, which could have a material adverse effect on us.

Real estate values in Southern Maryland have experienced declines over the past few years. A continued decline in local economic conditions could adversely affect the value of the real estate collateral securing our loans. A continued decline in property values would diminish our ability to recover on defaulted loans by selling the real estate collateral, making it more likely that we would suffer losses on defaulted loans. Additionally, a decrease in asset quality could require additions to our allowance for loan losses through increased provisions for loan losses, which would hurt our profits. Real estate values are affected by various factors in addition to local economic conditions, including, among other things, changes in general or regional economic conditions, governmental rules or policies and natural disasters.

Our business is subject to the success of the local economy in which we operate.

Because the majority of our borrowers and depositors are individuals and businesses located and doing business in Southern Maryland, our success depends, to a significant extent, upon economic conditions in Southern Maryland. Adverse economic conditions in our market area could reduce our growth rate, affect the ability of our customers to repay their loans and generally affect our financial condition and results of operations. Conditions such as inflation, recession, unemployment, high interest rates, short money supply, scarce natural resources, international disorders, terrorism and other factors beyond our control may adversely affect our profitability. We are less able than a larger institution to spread the risks of unfavorable local economic conditions across a large number of diversified economies. Any sustained period of increased payment delinquencies, foreclosures or losses caused by adverse market or economic conditions in the State of Maryland could adversely affect the value of our assets, revenues, results of operations and financial condition.

Increased and/or special FDIC assessments will hurt our earnings.

The recent economic recession has caused a high level of bank failures, which has dramatically increased Federal Deposit Insurance Corporation resolution costs and led to a significant reduction in the balance of the Deposit Insurance Fund. As a result, the Federal Deposit Insurance Corporation has significantly increased the initial base assessment rates paid by financial institutions for deposit insurance. Increases in the base assessment rate have increased our deposit insurance costs and negatively impacted our earnings. In addition, in May 2009, the Federal Deposit Insurance Corporation imposed a special assessment on all insured institutions. Our special assessment, which was reflected in earnings for the quarter ended June 30, 2009, was \$193,000. In lieu of imposing an additional special assessment, the Federal Deposit Insurance Corporation required all institutions to prepay their assessments for all of 2010, 2011 and 2012, which for us totaled \$2.7 million. Additional increases in the base assessment rate or additional special assessments would negatively impact our earnings.

The trading history of our common stock is characterized by low trading volume. Our common stock may be subject to sudden decreases.

Although our common stock trades on OTC Electronic Bulletin Board, it has not been regularly traded. We cannot predict the extent to which investor interest in us will lead to a more active trading market in our common stock or how liquid that market might become. A public trading market having the desired characteristics of depth, liquidity and orderliness depends upon the presence in the marketplace of willing buyers and sellers of our common stock at any given time, which presence is dependent upon the individual decisions of investors, over which we have no control.

The market price of our common stock may be highly volatile and subject to wide fluctuations in response to numerous factors, including, but not limited to, the factors discussed in other risk factors and the following:

Ø actual or anticipated fluctuations in our operating results;

Ø changes in interest rates;

Ø changes in the legal or regulatory environment in which we operate;

Ø press releases, announcements or publicity relating to us or our competitors or relating to trends in our industry;

Ø changes in expectations as to our future financial performance, including financial estimates or recommendations by securities analysts and investors;

Ø future sales of our common stock;

Ø changes in economic conditions in our marketplace, general conditions in the U.S. economy, financial markets or the banking industry; and

Ø other developments affecting our competitors or us.

These factors may adversely affect the trading price of our common stock, regardless of our actual operating performance, and could prevent you from selling your common stock at or above the price you desire. In addition, the stock markets, from time to time, experience extreme price and volume fluctuations that may be unrelated or disproportionate to the operating performance of companies. These broad fluctuations may adversely affect the market price of our common stock, regardless of our trading performance.

We operate in a highly regulated environment and we may be adversely affected by changes in laws and regulations.

Community Bank of Tri-County is subject to extensive regulation, supervision and examination by the Commissioner of Financial Regulation of the State of Maryland, its chartering authority, the Federal Reserve Board, as its federal regulator, and by the Federal Deposit Insurance Corporation, as insurer of its deposits. Tri-County Financial Corporation is subject to regulation and supervision by the Federal Reserve Board. Such regulation and supervision govern the activities in which an institution and its holding company may engage and are intended primarily for the protection of the insurance fund and for the depositors and borrowers of Community Bank of Tri-County. The regulation and supervision by the Commissioner of Financial Regulation of the State of Maryland, the Federal Reserve Board and the Federal Deposit Insurance Corporation are not intended to protect the interests of investors in Tri-County Financial Corporation common stock. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on our operations, the classification of

our assets and determination of the level of our allowance for loan losses. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, legislation or supervisory action, may have a material impact on our operations.

Provisions of our articles of incorporation, bylaws and Maryland law, as well as state and federal banking regulations, could delay or prevent a takeover of us by a third party.

Provisions in our articles of incorporation and bylaws and the corporate law of the State of Maryland could delay, defer or prevent a third party from acquiring us, despite the possible benefit to our stockholders, or otherwise adversely affect the price of our common stock. These provisions include: supermajority voting requirements for certain business combinations; the election of directors to staggered terms of three years; and advance notice requirements for nominations for election to our board of directors and for proposing matters that shareholders may act on at shareholder meetings. In addition, we are subject to Maryland laws, including one that prohibits us from engaging in a business combination with any interested shareholder for a period of five years from the date the person became an interested shareholder unless certain conditions are met. These provisions may discourage potential takeover attempts, discourage bids for our common stock at a premium over market price or adversely affect the market price of, and the voting and other rights of the holders of, our common stock. These provisions could also discourage proxy contests and make it more difficult for you and other shareholders to elect directors other than the candidates nominated by our Board.

We rely on other companies to provide key components of our business infrastructure.

Third party vendors provide key components of our business infrastructure such as internet connections, network access and fund distribution. While we have selected these third party vendors carefully, we cannot control their actions. Any problems caused by these third parties, including those which result from their failure to provide services for any reason or their poor performance of services, could adversely affect our ability to deliver products and services to its customers and otherwise to conduct its business. Replacing these third party vendors could also entail significant delay and expense.

Item 1B. Unresolved Staff Comments

Not applicable.

Item 2. Properties

The Bank maintains its main office in Waldorf, Maryland, in addition to its branch offices in Lexington Park, Leonardtown, La Plata, Dunkirk, Bryans Road, Waldorf, Charlotte Hall, Prince Frederick and Lusby, Maryland. The Bank owns all of its branches except for the Dunkirk, Maryland branch and the land on which the Waldorf, Charlotte Hall, Prince Frederick and Lusby, Maryland branches are located. Lease expiration dates range from 2020 to 2028 with renewal options of 5 to 10 years. The total net book value of the properties at December 31, 2010 was \$10.6 million which included \$7.1 million related to buildings and improvements.

Item 3. Legal Proceedings

Neither the Company, the Bank, nor any subsidiary is engaged in any legal proceedings of a material nature at the present time. From time to time, the Bank is a party to legal proceedings in the ordinary course of business.

Item 4. [Removed and Reserved]

PART II

Item 5. Market for Registrant's Common Equity, Related Security Holder Matters and Issuer Purchases of Equity Securities

Market Price and Dividends on Registrant's and Related Stockholder Matters.

The information contained under the section captioned "Market for the Registrant's Common Stock and Related Security Holder Matters" in the Company's Annual Report to Stockholders for the fiscal year ended December 31, 2010 (the "Annual Report") filed as Exhibit 13 hereto is incorporated herein by reference.

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Stock Performance Graph.

Not required as the Company is a smaller reporting company.

Recent Sales of Unregistered Securities.

Not applicable.

Purchases of Equity Securities by the Issuer.

On September 25, 2008, the Company announced a repurchase program under which it would repurchase up to 5% of its outstanding common stock or approximately 147,435 shares. As part of the Company's participation in the Capital Purchase Program of the U.S. Department of Treasury's Troubled Asset Repurchase Program, prior to the earlier of (a) December 19, 2018 or (b) the date on which the Series A preferred stock and the Series B preferred stock has been redeemed in full or the Treasury has transferred all of the Series A preferred stock and the Series B preferred stock to non-affiliates, the Company, without the consent of the Treasury, cannot repurchase any shares of its common stock or other capital stock or equity securities or trust preferred securities. These repurchase restrictions do not apply in certain limited circumstances, including the repurchase of common stock in connection with the administration of any employee benefit plan in the ordinary course of business and consistent with past practice. In addition, during the period beginning on December 19, 2018 and ending on the date on which the Series A preferred stock and the Series B preferred stock have been redeemed in full or the Treasury has transferred all of the Series A preferred stock and the Series B preferred stock to non-affiliates, the Company cannot repurchase any shares of its common stock or other capital stock or equity securities or trust preferred securities without the consent of the Treasury.

On November 12, 2010, after approval from the Treasury, the Company approved a repurchase program under which the Company may repurchase shares of common stock equaling up to 1% of the Company's stockholders' equity under the previously authorized plan described below. The Company intends to repurchase shares from time to time, depending on market conditions. The following table presents information regarding the Company's stock repurchases during the three months ended December 31, 2010.

	(a)	(b)	(c)	(d)
	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
October 1 to October 31	-	\$-	-	140,146
November 1 to November 30	-	-	-	140,146
December 1 to December 31	1,500	16.00	1,500	138,646
	1,500	\$16.00	1,500	138,646

On September 25, 2008, Tri-County Financial Corporation announced a repurchase program under which it would repurchase up to 5% or 147,435 of its outstanding common stock shares.

Item 6. Selected Financial Data

The information contained under the section captioned “Selected Financial Data” of the Annual Report filed as Exhibit 13 hereto is incorporated herein by reference.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation

The information contained in the section captioned "Management's Discussion and Analysis of Financial Condition and Results of Operations" of the Annual Report filed as Exhibit 13 hereto is incorporated herein by reference.

Item 7A. Quantitative and Qualitative Disclosure About Market Risk

Not applicable as the Company is a smaller reporting company.

Item 8. Financial Statements and Supplementary Data

The Consolidated Financial Statements, Notes to Consolidated Financial Statements and Report of Independent Registered Public Accounting Firm included in the Annual Report filed as Exhibit 13 hereto are incorporated herein by reference.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

(a) Disclosure Controls and Procedures

The Company's management, including the Company's principal executive officer and principal financial officer, have evaluated the effectiveness of the Company's "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, (the "Exchange Act"). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the Securities and Exchange Commission (the "SEC") (1) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

(b) Internal Controls Over Financial Reporting

Management's annual report on internal control over financial reporting is incorporated herein by reference to the Company's audited Consolidated Financial Statements in this Annual Report on Form 10-K.

(c) Changes to Internal Control Over Financial Reporting

Except as indicated herein, there were no changes in the Company's internal control over financial reporting during the three months ended December 31, 2010 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B. Other Information

Not applicable.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

For information concerning the Company's directors, the information contained under the section captioned "Items to be voted on by Stockholders Item 1 – Election of Directors" in the Company's definitive proxy statement for the Company's 2011 Annual Meeting of Stockholders (the "Proxy Statement") is incorporated herein by reference. For information concerning the executive officers of the Company, see "Item 1 – Business – Executive Officers of the Registrant" under Part I of this Annual Report on Form 10-K.

For information regarding compliance with Section 16(a) of the Exchange Act, the cover page of this Annual Report on Form 10-K and the information contained under the section captioned "Other Information Relating to Directors and Executive Officers Section 16(a) Beneficial Ownership Reporting Compliance" in the Proxy Statement are incorporated herein by reference.

For information concerning the Company's code of ethics, the information contained under the section captioned "Corporate Governance – Code of Ethics" in the Proxy Statement is incorporated by reference. A copy of the code of ethics and business conduct is filed as Exhibit 14 hereto.

For information regarding the audit committee and its composition and the audit committee financial expert, the section captioned "Corporate Governance – Committees of the Board of Directors – Audit Committee" in the Proxy Statement is incorporated by reference.

Item 11. Executive Compensation

For information regarding executive compensation, the information contained under the sections captioned "Executive Compensation" and "Directors' Compensation" in the Proxy Statement is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

(a) Security Ownership of Certain Owners

The information required by this item is incorporated herein by reference to the section captioned "Principal Holders of Voting Securities" in the Proxy Statement.

(b) Security Ownership of Management

Information required by this item is incorporated herein by reference to the section captioned "Principal Holders of Voting Securities" in the Proxy Statement.

(c) Changes in Control

Management of the Company knows of no arrangements, including any pledge by any person of securities of the Company, the operation of which may, at a subsequent date, result in a change in control of the registrant.

(d) Equity Compensation Plan Information

The Company maintains the Tri-County Financial Corporation 2005 Equity Compensation Plan. This plan covers employees and non-employee directors. The following table sets forth certain information with respect to the

Company's Equity Compensation Plan as of December 31, 2010.

	(a)	(b)	(c)
Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants, and rights	Weighted average exercise price of outstanding options, warrants, and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity plans approved by security holders	253,224	\$ 17.26	120,315
Equity compensation plans not approved by security holders (1)	46,013	\$ 14.64	-
Total	299,237	\$ 16.86	120,315

(1) Consists of the Company's 1995 Stock Option Plan for Non-Employee Directors, which expired in 2005 and which provided grants of non-incentive stock options to directors who are not employees of the Company or its subsidiaries. Options were granted at an exercise price equal to their fair market value at the date of grant and had a term of ten years. Options are generally exercisable while an optionee serves as a director or within one year thereafter.

Item 13. Certain Relationships, Related Transactions and Director Independence

The information regarding certain relationships and related transactions, the section captioned "Other Information Relating to Directors and Executive Officers – Policies and Procedures for Approval and Related Parties Transactions and Relationships and Transactions with the Company and the Bank" in the Proxy Statement is incorporated herein by reference.

For information regarding director independence, the section captioned "Proposal 1 – Election of Directors" in the Proxy Statement is incorporated by reference.

Item 14. Principal Accountant Fees and Services

The information required by this item is incorporated herein by reference to the section captioned "Audit Related Matters – Audit Fees" and "— an Pre-Approval of Services by the Independent Registered Public Accounting Firm" in the Proxy Statement.

PART IV

Item 15. Exhibits and Financial Statement Schedules

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

(1) Financial Statements. The following consolidated financial statements and notes related thereto are incorporated by reference from Item 8 hereof:

Report of Independent Registered Public Accounting Firm
Consolidated Balance Sheets as of December 31, 2010 and 2009
Consolidated Statements of Income for the Years Ended December 31, 2010 and 2009

Consolidated Statements of Changes in Stockholders' Equity for the Years Ended December 31, 2010
and 2009

Consolidated Statements of Cash Flows for the Years Ended December 31, 2010 and 2009

Notes to Consolidated 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 consolidated financial statements and related notes thereto.

(3) Exhibits. The following is a list of exhibits filed as part of this Annual Report on Form 10-K and is also the Exhibit Index.

Exhibit No	Description	Incorporated by Reference to
3.1	Articles of Incorporation of Tri-County Financial Corporation	Form S-4 (Registration No. 333-31287).
3.2	Amended and Restated Bylaws of Tri-County Financial Corporation	Form 8-K as filed on August 27, 2010
4.1	Articles Supplementary establishing Fixed Rate Cumulative Perpetual Preferred Stock, Series A, of Tri-County Financial Corporation	Form 8-K as filed on December 22, 2008
4.2	Form of stock certificate for Fixed Rate Cumulative Perpetual Preferred Stock, Series	Form 8-K as filed on December 22, 2008
4.3	Articles Supplementary establishing Fixed Rate Cumulative Perpetual Preferred Stock, Series B, of Tri-County Financial Corporation	Form 8-K as filed on December 22, 2008
4.4	Form of stock certificate for Fixed Rate Cumulative Perpetual Preferred Stock, Series B	Form 8-K as filed on December 22, 2008
10.1*	Tri-County Financial Corporation 1995 Stock Option and Incentive Plan, as amended	Form 10-K for the year ended December 31, 2000 as filed on March 30, 2001.
10.2*	Tri-County Financial Corporation 1995 Stock Option Plan for Non-Employee Directors, as amended	Form 10-K for the year ended December 31, 2000 as filed on March 30, 2001.
10.3*	Employment Agreement with Michael L. Middleton	Form 10-Q for the quarter ended September 30, 2006 as filed on November 14, 2006.
10.4*	Amended and Restated Executive Incentive Compensation Plan	Form 10-K/A for the year ended December 31, 2008 as filed on April 20, 2009.
10.5*	Retirement Plan for Directors	Form 10-K for the year ended December 31, 2006 as filed on March 27, 2007.
10.6*	Split Dollar Agreements with Michael L. Middleton	Form 10-K for the year ended December 31, 2000 as filed on March 30, 2001.
10.7*	Split Dollar Agreement with William J. Pasenelli	Form 10-K for the year ended December 31, 2001 as filed on April 1, 2002.

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|-------|--|--|
| 10.8* | Salary Continuation Agreement with Michael L. Middleton, dated September 6, 2003 | Form 10-K for the year ended December 31, 2003 as filed on March 26, 2004. |
| 10.9* | First Amendment to the Salary Continuation Agreement, dated September 6, 2003, with Michael L. Middleton | Form 10-K for the year ended December 31, 2008 as filed on March 9, 2009. |

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10.10*	Tri-County Financial Corporation 2005 Equity Compensation Plan	Definitive Proxy Statement as filed on April 11, 2005
10.11*	Amendment No. 1 to the Tri-County Financial Corporation 2005 Equity Compensation Plan	Form 10-Q for the quarter ended September 30, 2007 as filed on November 13, 2007.
10.12*	Community Bank of Tri-County Executive Deferred Compensation Plan	Form 10-K for the year ended December 31, 2006 as filed on March 27, 2007.
10.13*	Amended and Restated Employment Agreement by and among Community Bank of Tri-County, William J. Pasenelli and Tri-County Financial Corporation, as guarantor	Form 10-Q for the quarter ended March 31, 2007 as filed on May 11, 2007.
10.14*	Amended and Restated Employment Agreement by and among Community Bank of Tri-County, Gregory C. Cockerham and Tri-County Financial Corporation, as guarantor	Form 10-Q for the quarter ended March 31, 2007 as filed on May 11, 2007.
10.15*	Salary Continuation Agreement with Gregory C. Cockerham, dated August 21, 2006	Form 10-Q for the quarter ended September 30, 2006 as filed on November 14, 2006.
10.16*	First Amendment to the Salary Continuation Agreement, dated August 21, 2006, with Gregory C. Cockerham	Form 10-K/A for the year ended December 31, 2008 as filed on April 20, 2009.
10.17*	Second Amendment to the Salary Continuation Agreement, dated August 21, 2006, with Gregory C. Cockerham	Form 10-K/A for the year ended December 31, 2008 as filed on April 20, 2009.
10.18*	Salary Continuation Agreement with William J. Pasenelli, dated August 21, 2006	Form 10-Q for the quarter ended September 30, 2006 as filed on November 14, 2006.
10.19*	First Amendment to the Salary Continuation Agreement, dated August 21, 2006, with William J. Pasenelli	Form 10-K/A for the year ended December 31, 2008 as filed on April 20, 2009.
10.20*	Second Amendment to the Salary Continuation Agreement, dated August 21, 2006, with William J. Pasenelli	Form 10-K/A for the year ended December 31, 2008 as filed on April 20, 2009.
10.21*	Letter Agreement and related Securities Purchase Agreement – Standard Terms, dated December 19, 2008, between Tri-County Financial Corporation and United States Department of the Treasury	Form 8-K as filed on December 22, 2008.

10.22* Form of Waiver executed by each of Michael Form 8-K as filed on December 22, 2008
L. Middleton, Gregory C. Cockerham and
William J. Pasenelli

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10.23*	Form of Letter Agreement between Tri-County Financial Corporation and each of Michael L. Middleton, Gregory C. Cockerham and William J. Pasenelli	Form 8-K as filed on December 22, 2008
10.24*	Salary Continuation Agreement between Gregory C. Cockerham and Community Bank of Tri-County, dated September 6, 2003, as amended on December 22, 2008	Form 10-K/A for the year ended December 31, 2008 as filed on April 20, 2009.
10.25*	Salary Continuation Agreement between William J. Pasenelli and Community Bank of Tri-County, dated September 6, 2003, as amended on June 11, 2004 and December 22, 2008	Form 10-K/A for the year ended December 31, 2008 as filed on April 20, 2009.
13.0	Annual Report to Stockholders for the year ended December 31, 2010	
14.0	Code of Ethics	Form 10-K for the year ended December 31, 2005 as filed on March 30, 2006.
21.0	List of Subsidiaries	
23.1	Consent of Stegman & Company	
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer	
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer	
32.0	Section 1350 Certification of Chief Executive Officer, Chief Financial Officer and Chief Accounting Officer	
99.1	Principal Executive Officer Certification regarding TARP	
99.2	Principal Executive Officer Certification regarding TARP	

(*) Management contract or compensating arrangement.

(b) Exhibits. The exhibits required by Item 601 of Regulation S-K are either filed as part of this Annual Report on Form 10-K 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 this Annual Report pursuant to Rule 14a-3(b)(1) 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.

TRI-COUNTY FINANCIAL CORPORATION

Date: March 4, 2011

By:

/s/ Michael L. Middleton
Michael L. Middleton
President and Chief Executive Officer
(Duly Authorized Representative)

Pursuant to the requirement of 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.

By: /s/ Michael L. Middleton
Michael L. Middleton
Director, President and Chief
Executive Officer
(Principal Executive Officer)

By: /s/ William J. Pasenelli
William J. Pasenelli
Director, Executive Vice President
and Chief
Financial Officer
(Principal Financial and Accounting
Officer)

Date: March 4, 2011

Date: March 4, 2011

By: /s/ H. Beaman Smith
H. Beaman Smith
Director

By: /s/ Austin J. Slater, Jr.
Austin J. Slater, Jr.
Director

Date: March 4, 2011

Date: March 4, 2011

By: /s/ Louis P. Jenkins, Jr.
Louis P. Jenkins, Jr.
Director

By: /s/ James R. Shepherd
James R. Shepherd
Director

Date: March 4, 2011

Date: March 4, 2011

By: /s/ Philip T. Goldstein
Philip T. Goldstein
Director

By: /s/ Joseph V. Stone, Jr.
Joseph V. Stone, Jr.
Director

Date: March 4, 2011

Date: March 4, 2011

By: /s/ Mary Todd Peterson
Mary Todd Peterson
Director

Date: March 4, 2011

