

SUMMIT BANCSHARES INC /TX/  
Form 10-K  
March 11, 2004

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

**FORM 10-K**

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

For the Fiscal Year Ended December 31, 2003

Commission File Number 0-11986

**SUMMIT BANCSHARES, INC.**

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(Exact name of registrant as specified in its charter)

Texas

75-1694807

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(State or other jurisdiction of organization or incorporation)

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

3880 Hulen St., Fort Worth, Texas 76107

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(Address of principal executive offices, including zip code)

(817) 336-6817

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(Registrant's telephone number, including area code)

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

None

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

Common Stock, \$1.25 par value

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(Title of Class)

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 authorized to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

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 the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Annual Report on Form 10-K or any amendment to this Annual Report on Form 10-K.

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

Yes No

The aggregate market value of the shares of common stock, par value \$1.25 per share ( Common Stock ), of the registrant held by non-affiliates of the registrant at June 30, 2003 was approximately \$123,273,000, based on a closing bid price of \$23.48 per share on that date.

The number of shares of Common Stock outstanding at March 1, 2004 was 6,153,599 shares.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's Proxy Statement, which will be filed within 120 days after December 31, 2003, pursuant to the Securities Exchange Act of 1934 in connection with the registrant's 2004 Annual Meeting of Shareholders are incorporated by reference into Part III of this Annual Report on Form 10-K.

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SUMMIT BANCSHARES, INC.  
ANNUAL REPORT ON FORM 10-K

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## PART I

### ITEM 1. BUSINESS.

#### GENERAL

Summit Bancshares, Inc. (the Corporation) was incorporated under the laws of the state of Texas in 1979. The Corporation is a bank holding company registered under the Bank Holding Company Act of 1956, as amended (the BHC Act), and became a financial holding company under the Gramm-Leach-Bliley Act (the GLB Act) in February 2002. The Corporation maintains its principal executive offices at 3880 Hulen Street, Suite 300, Fort Worth, Texas 76107. At December 31, 2003, the Corporation had consolidated total assets of \$795.5 million, consolidated total loans of \$553.8 million, consolidated total deposits of \$641.4 million and consolidated total shareholders' equity of \$68.7 million.

The Corporation's principal activity is the ownership and management of its direct and indirect wholly-owned subsidiaries, Summit Delaware Financial Corporation, Summit Bank, National Association (the Bank) and SIA Insurance Agency, Inc. (SIA). The Corporation provides advice and services to the Bank and coordinates its activities in the areas of financial accounting controls and reports, internal audit programs, regulatory compliance, financial planning and employee benefit programs, although the Bank operates under the day-to-day management of its own officers and directors.

#### PRODUCTS AND SERVICES

The products and services offered by the Corporation through its subsidiaries are generally those offered by commercial banks of comparable size, including:

**Commercial Banking Services.** The Bank provides general commercial banking services for corporate and other business clients principally located in Tarrant County, Texas. Loans are made for a wide variety of purposes, including interim construction and mortgage financing on real estate and financing of equipment and inventories.

**Consumer Banking Services.** The Bank provides a full range of consumer banking services, including interest and noninterest-bearing checking accounts, various savings programs, installment and real estate loans, money transfers, on-site ATM facilities and safe deposit facilities.

**Securities Services.** The Corporation offers full-service brokerage services through an agreement with Raymond James Financial Services, Inc., including securities brokerage services relating to tax-free municipals, government securities, stocks, mutual funds and annuities, and asset management and financial planning services. Raymond James Financial Services, Inc. is a registered broker-dealer and member of the National Association of Securities Dealers, Inc.

**Insurance Products and Services.** SIA is a full-service insurance agency that provides commercial property and casualty insurance as well as life, health and disability insurance and benefits planning to the Corporation's existing and prospective commercial customers. These services are offered through an alignment the Corporation has established with local agencies Wm. Rigg Insurance Co. for property and casualty insurance and CSG/Hull Benefits, Inc. for life and benefits insurance.

#### AVAILABLE INFORMATION

The Corporation's website is [www.summitbank.net](http://www.summitbank.net). The Corporation makes copies of its annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and any amendments to those reports, publicly available free of charge through its website as soon as reasonably practicable after it electronically files or furnishes such materials with the Securities and Exchange Commission (the SEC). The Corporation also makes information relating to its corporate governance policies and practices publicly available free of charge through its website. Copies of the foregoing materials may also be obtained by written request to the Corporation at 3880 Hulen Street, Suite 300, Fort Worth, Texas 76107, Attention: Corporate Secretary.

#### COMPETITION

The Corporation and its subsidiaries encounter intense competition for their products and services from bank holding companies and other financial institutions located in Tarrant County, Texas, including banks, savings and loan associations, credit unions, factors, insurance companies and commercial and captive finance companies, many of which are larger than the Corporation and its subsidiaries in terms of capital, resources and personnel.

#### EMPLOYEES

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As of December 31, 2003, the Corporation and the Bank collectively had a total of 216 full-time employees and 18 part-time employees.

## REGULATION AND SUPERVISION

The Corporation and its subsidiaries are subject to federal and state laws applicable to financial institutions and businesses generally. This regulatory framework is intended primarily for the protection of depositors, federal deposit insurance funds and the banking system as a whole, and not for the protection of shareholders and creditors of the Corporation. The following summary of statutory and regulatory provisions is not intended to be a complete description of all of the statutes and regulations to which the Corporation and its subsidiaries are subject and is qualified in its entirety by reference to the applicable statutes and regulations. Any change in applicable statutes, regulations or policies of regulatory authorities could have a material effect on the business, results of operations and financial condition of the Corporation and its subsidiaries.

### The Corporation

**General.** As a bank holding company and a financial holding company, the Corporation is subject to regulation under the BHC Act, the GLB Act and to inspection, supervision and examination by the Board of Governors of the Federal Reserve System (the FRB). Under the BHC Act, the GLB Act and other federal laws, regulations and policies, the Corporation is subject to restrictions on the types of activities in which it may engage and is subject to regulatory enforcement actions for any violations of such laws, regulations and policies.

**Scope of Permissible Activities.** The BHC Act generally prohibits the Corporation from directly or indirectly engaging in, or from directly or indirectly acquiring 5.0% or more of any class of voting securities of any company engaged in any activities other than banking, managing or controlling banks or other activities determined by the FRB to be so closely related to banking as to be a proper incident thereto. Some activities that the FRB has determined to be closely related to banking include making or servicing loans, performing certain data processing services, acting as an investment or financial adviser and providing certain securities brokerage services.

The GLB Act amended the BHC Act in November 1999 to permit the creation of a financial holding company, a new type of bank holding company with powers exceeding those of a traditional bank holding company. As a financial holding company under the GLB Act, the Corporation may provide a wide variety of financial services previously reserved for insurance companies and securities firms, including services such as lending, investing for others, safeguarding money or securities, underwriting insurance, issuing annuities, acting as an insurance principal, agent or broker and providing financial or investment advice.

Under the GLB Act, the Corporation may also engage in, and acquire and retain shares of any company engaged in any activity that the FRB determines to be financial in nature or incidental thereto or complementary to a financial activity, provided that such activity does not pose a substantial risk to the safety or soundness of depository institutions or the financial system generally. The GLB Act also generally permits the Corporation to invest in non-financial companies as a part of a bona fide underwriting or merchant or investment banking activities if it holds an investment only for a period of time to enable its sale or disposition on a reasonable basis consistent with the financial viability of the foregoing activities.

**Source of Strength to the Bank.** Under FRB regulations, the Corporation is expected to serve as a source of financial and managerial strength to the Bank and, under appropriate circumstances, commit resources to its support. This support may be required at times when the Corporation may not be able to provide such support. If the Corporation fails to meet its obligations to serve as a source of strength to the Bank, the FRB may find the Corporation to be engaged in an unsafe or unsound banking practice and in violation of FRB regulations.

**Restrictions on Payment of Dividends.** Under FRB regulations, the FRB has the authority to prohibit bank holding companies from engaging in activities that the FRB considers unsafe or unsound banking practices. Under certain circumstances, the FRB may take the position that payment of dividends by the Corporation would constitute an unsafe or unsound banking practice in light of the financial condition of the Corporation. Under FRB policies, a bank holding company should pay cash dividends on its common stock only out of income available over the past year and should not pay cash dividends if such payment would undermine its ability to serve as a source of strength to its banking subsidiaries. The Corporation's ability to pay cash dividends is further limited by its obligation to maintain adequate levels of capital in accordance with the FRB's capital adequacy guidelines. See Business - The Corporation - Capital Adequacy Requirements.

**Capital Adequacy Requirements.** The FRB has established guidelines to assess the capital adequacy of bank holding companies. The guidelines impose two sets of capital adequacy requirements on bank holding companies: (i) risk-based capital guidelines, which require bank holding companies to maintain a specified minimum ratio of qualifying total capital to risk-weighted assets, and (ii) leverage ratios, which require bank holding companies to maintain a specified minimum ratio of capital to total assets. Failure to comply with these capital adequacy guidelines could subject the Corporation to a variety of enforcement actions as well as certain limitations on its business, including, but not limited to, restrictions on the payment of dividends to its shareholders.

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Under the risk-based capital guidelines, the FRB requires bank holding companies to maintain a minimum ratio of qualifying total capital to risk-weighted assets of at least 8.0% (of which at least 4.0% must be in the form of Tier 1 capital). A bank holding company's qualifying total capital represents the sum of its Tier 1 and Tier 2 capital (with Tier 2 capital being limited to 100% of Tier 1 capital), less investments in certain unconsolidated subsidiaries. Tier 1 capital generally includes common shareholders' equity, qualifying preferred stock and minority interests in consolidated subsidiaries, less goodwill, intangible assets and certain other adjustments. Tier 2 capital generally includes certain other preferred stock, qualifying debt instruments and allowances for loan losses. Risk-weighted assets are calculated by multiplying asset balances by corresponding risk weights generally based on perceived credit risk. At December 31, 2003, the Corporation's ratios of Tier 1 and qualifying total capital to risk-weighted assets were 11.5% and 12.7%, respectively, both of which exceeded regulatory minimums.

The FRB guidelines also require bank holding companies with high regulatory ratings to maintain minimum leverage ratios of at least 3.0%, which are calculated by dividing Tier 1 capital by adjusted average total consolidated assets. Other bank holding companies with supervisory, financial or managerial weaknesses, as well as those anticipating or experiencing significant growth, are expected to maintain leverage ratios in excess of 3.0%. At December 31, 2003, the Corporation's ratio of Tier 1 capital to adjusted average total consolidated assets was 8.6%, which exceeded the regulatory minimum.

**Liability for Undercapitalized Subsidiaries.** The Federal Deposit Insurance Corporation Improvements Act of 1991 ( FDICIA ) requires bank regulators to take prompt corrective action against an insured depository institution if that institution does not meet certain capital adequacy guidelines. In the event an insured depository institution becomes undercapitalized under the FDICIA capital adequacy guidelines, it must submit a capital restoration plan to its federal regulatory agency. Before regulatory authorities will approve an undercapitalized institution's capital restoration plan, each company that controls the institution must guarantee, up to certain limits, the institution's compliance with the capital restoration plan. Because the Bank is an insured depository institution under FDICIA that is controlled by the Corporation, the Corporation would be required to guarantee the Bank's compliance with a capital restoration plan in the event the Bank becomes undercapitalized under the FDICIA capital adequacy guidelines. See Business - the Bank - Capital Adequacy Requirements for additional information regarding the FDICIA capital adequacy guidelines.

Under FDICIA, liability for the fulfillment of any such guarantee could extend up to 5.0% of the undercapitalized institution's assets at the time it became undercapitalized or the amount necessary to bring the undercapitalized institution into compliance with the capital adequacy guidelines. In addition, a bank holding company controlling an undercapitalized institution may be required to obtain FRB approval prior to paying cash dividends or engaging in other activities. Under certain circumstances, the FRB may also require a bank holding company to divest itself of an undercapitalized institution or other affiliates of the bank holding company.

**Liability of Commonly Controlled Institutions.** The Financial Institution Reform, Recovery and Enforcement Act of 1989 ( FIRREA ) contains a cross-guarantee provision under which commonly controlled insured depository institutions can be held liable to the Federal Deposit Insurance Corporation (the FDIC ) for any losses incurred, or reasonably expected to be incurred, by the FDIC due to the default of an insured depository institution, and for any assistance provided by the FDIC to an insured depository institution that is in danger of default. An FDIC cross-guarantee claim against an insured depository institution for administrative expenses and claims of such institution's depositors (including the FDIC, as subrogee of such depositors) has priority over the rights of such institution's shareholders and other creditors.

**Acquisition by Bank Holding Companies.** Under the BHC Act, prior FRB approval is required before a bank holding company merges or consolidates with, or acquires direct or indirect control of more than 5.0% of the outstanding shares of any class of voting securities or substantially all of the assets of, any bank or bank holding company. In approving any of the foregoing transactions, the FRB is required to consider the financial and managerial resources and future prospects of the banks and bank holding companies concerned, the convenience and needs of the communities to be served and other various competitive factors.

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the Interstate Banking Act ) provides that the FRB may approve an application of an adequately capitalized and managed bank holding company to acquire banks located in other states, regardless of whether the acquisition would be prohibited by applicable state laws. Any such approval, however, would be subject to applicable state age laws. An out-of-state bank holding company seeking to acquire ownership or control of a bank located in Texas must obtain the prior approval of both the FRB and the Banking Commissioner of Texas (the Commissioner ) if the Texas bank has not been in existence for five years. If the FRB approves an acquisition that the Commissioner disapproves, the Commissioner may accept the FRB decision or attempt to have the decision overturned by a federal court.

The Interstate Banking Act also provides that a bank holding company and its affiliates may not acquire a bank located in Texas if, as a result of the acquisition, the bank holding company and its affiliates would control more than 10.0% of total deposits in insured depository institutions nationwide or 30.0% or more of total deposits in insured depository institutions in the home state of the bank to be acquired. However, states may adopt deposit concentration caps that are more restrictive than those set forth in the Interstate Banking Act, and Texas has adopted a deposit concentration cap of 20.0% of in-state insured deposits that will apply in connection with acquisitions of banks located in Texas.

**Acquisition of Bank Holding Companies.** The Change in Bank Control Act of 1978 (the CBC Act ) prohibits a person or group of persons from acquiring control of a bank holding company unless the FRB has been given prior notice and has not disapproved the acquisition. For purposes of the CBC Act, the acquisition of 25.0% or more of any class of voting securities of a bank holding company constitutes an acquisition of control. The FRB presumes that the acquisition of 10.0% or more of any class of voting securities of a bank holding company constitutes acquisition of control if either the bank holding company has a class of equity securities registered under Section 12 of the Exchange Act of 1934 or if no other person will own or control a greater percentage of that class of securities immediately after the acquisition. This presumption can be rebutted by showing that the acquisition will not in fact result in an acquisition of control of the bank holding company under the CBC Act.



***Enforcement.*** The FRB has broad supervisory enforcement authority over bank holding companies and their nonbanking subsidiaries. The FRB may seek various administrative remedies in connection with activities and practices of bank holding companies and their nonbanking subsidiaries that constitute violations of federal laws and FRB regulations, including issuing cease and desist orders that may, among other things, require affirmative action to correct improper conditions, restitution, reimbursement, indemnification, guaranty against loss, restrictions on growth, disposal of certain assets or such other action as the FRB determines to be appropriate.

FIRREA significantly expanded the FRB's enforcement powers over bank holding companies and their nonbanking subsidiaries. Under FIRREA, the scope of individuals and entities against whom enforcement may be sought and penalties assessed was expanded to include, among others, directors, officers, employees or controlling shareholders of bank holding companies and their nonbanking subsidiaries. FIRREA also increased the amount of civil penalties that the FRB and other regulatory agencies may assess for knowing or recklessly committing certain activities that cause a substantial loss to a depository institution.

### **The Bank**

**General.** The Bank is a national banking association organized under the National Bank Act, as amended (the National Bank Act), and is subject to supervision and examination by the Office of the Comptroller of the Currency (the OCC). The OCC regulates national banks with respect to, among other matters, capital adequacy, reserves, loan portfolios, investments and management practices, and the OCC may seek various administrative remedies in connection with activities and practices of national banks that are unsafe or unsound or constitute violations of law. The Bank is also subject to regulation and supervision by the FDIC because the Bank's deposits are insured by the Bank Insurance Fund (BIF) of the FDIC. The FRB also has supervisory and regulatory authority over the activities and practices of the Bank.

**Scope of Permissible Activities.** Under the National Bank Act, a national bank may engage in making, arranging, purchasing or selling loans, purchasing, holding and conveying real estate under certain conditions, dealing in investment securities under certain circumstances and, generally, engaging in the business of banking and activities that are incidental thereto. Activities that are deemed to be incidental to the business of banking include, among others, borrowing and lending of money, receiving deposits, holding or selling securities or other property acquired in connection with security on a loan, discounting and negotiating evidences of debt, issuing letters of credit to or on behalf of its customers, operating a safe deposit business, providing check guarantee plans, issuing credit cards, operating a loan production office, selling loans under repurchase agreements and verifying and collecting checks.

**Branching.** National banks with a main office or a branch in Texas may establish branches anywhere in Texas with prior OCC approval. In acting on a branch application of a national bank, the OCC considers a number of factors, including the bank's financial history, capital adequacy and earnings prospects, the character of its management and needs of the community.

The Interstate Banking Act also permits banks to merge across state lines and thereafter have interstate branches by continuing to operate, as a main office or a branch, any office of any bank acquired in connection with an interstate bank acquisition. The Interstate Banking Act also allows a bank to open new branches in a state in which it does not already have banking operations if the laws of that state permit a de novo branch of an out-of-state bank. A de novo branch is a branch office of a bank that was originally established as a branch rather than as a result of an acquisition or merger. Under Texas law, an out-of-state bank may establish a de novo branch in Texas if the laws of the home state of the out-of-state bank permit a Texas bank to establish a de novo branch in such state. An out-of-state bank that has established or acquired a branch in Texas may establish or acquire additional in-state branches to the same extent as a Texas bank.

**Restrictions on Transactions with Affiliates.** The Bank is subject to federal statutes which limit transactions between the Bank and its affiliates. Section 23A of the Federal Reserve Act places limitations on the Bank's ability to make loans to, purchases assets from and make investments in, its affiliates, and it also requires certain levels of collateral for loans made by the Bank to its affiliates. Transactions between the Bank and its affiliates are also subject to Section 23B of the Federal Reserve Act which requires, among other things, that certain transactions between the Bank and its affiliates must be on terms substantially the same, or at least as favorable to the Bank, as those prevailing at the time for comparable transactions with or involving other nonaffiliated companies.

The Federal Reserve Act and FRB Regulation O also impose restrictions on the ability of the Bank and its affiliates to make loans to their directors, executive officers, principal shareholders and their related interests. These restrictions include limits on loans to one borrower and conditions that must be met before such loans can be made. There is also an aggregate limitation on all loans to insiders and their related interests. In the aggregate, these loans generally may not exceed the institution's total unimpaired capital and surplus. Directors, executive officers, principal shareholders and their related interests are subject to enforcement actions for knowingly accepting loans in violation of these restrictions.

**Interest Rate Limits and Lending Regulations.** The Bank is subject to various state and federal statutes relating to the extension of credit and the making of loans. The National Banking Act generally defers to state law for the maximum rate of interest which may be charged by national banks. The maximum legal rate of interest that the Bank may charge on a loan under Texas law depends on a variety of factors, including the type of borrower, the purpose of the loan, the amount of the loan and the date on which the loan is made. Penalties are provided by law for charging interest in excess of the maximum lawful rate.

Loans made by banks located in Texas are subject to numerous other federal and state laws and regulations, including the Truth-in-Lending Act, the Texas Finance Code, the Equal Credit Opportunity Act, the Real Estate Settlement Procedures Act and the Home Mortgage Disclosure Act. Failure to comply with these laws could result in certain remedies for borrowers and penalties for lenders. The scope and requirements of these

and similar laws and regulations have expanded in recent years and, as a result, claims by borrowers under these laws and regulations may increase in the future.

***Restrictions on Payment of Dividends.*** The principal source of the Corporation's revenues is cash dividends received from the Bank. The National Bank Act provides that the Bank may pay dividends out of its current or retained net profits, after deducting reserves for losses and bad debts, but may not pay dividends out of its paid-in capital. The National Bank Act further restricts the Bank's payment of dividends by prohibiting the Bank from declaring a dividend until its surplus fund equals the amount of its capital stock or, if its surplus fund does not equal the amount of its capital stock, until one-tenth of the Bank's net profits for the preceding half year, in the

case of quarterly or semi-annual dividends, or the preceding two half-year periods, in the case of annual dividends, are transferred to the surplus fund. OCC approval is required prior to the payment of a dividend if the total of all dividends declared by the Bank in any calendar year would exceed the total of its net profits for that year combined with its net profits for the two preceding years. The Bank's ability to pay dividends is further restricted by the FDICIA capital adequacy guidelines. See Business - The Bank - Capital Adequacy Requirements. In addition, certain regulatory authorities are authorized to prohibit the Bank from paying dividends if any such payment would constitute an unsafe and unsound banking practice.

**Capital Adequacy Requirements.** FDICIA established a system of supervision of the capital adequacy of insured depository institutions based upon minimum risk-based capital ratios and leverage ratios which are similar to those established by the FRB for bank holding companies. The OCC regulations establish five capital categories ranging from well capitalized to critically undercapitalized. A depository institution is considered well capitalized if it has a total risk-based capital ratio of 10.0% or greater, a Tier 1 risk-based capital ratio of 6.0% or greater, a leverage ratio of 5.0% or greater and is not subject to an order, written agreement, capital directive or prompt corrective action directive to meet and maintain a specific capital level for any capital measure. A depository institution is considered adequately capitalized if it has a total risk-based capital ratio of 8.0% or greater, a Tier 1 risk-based capital ratio of 4.0% or greater and a leverage ratio of 4.0% or greater (or a leverage ratio of 3.0% or greater if the institution was given the highest rating in its most recent report of examination) and the institution does not meet the definition of a well capitalized institution. A depository institution is considered undercapitalized if it has a total risk-based capital ratio that is less than 8.0%, a Tier 1 risk-based capital ratio that is less than 4.0% or a leverage ratio that is less than 4.0% (or a leverage ratio that is less than 3.0% if the institution received the highest rating in its most recent report of examination). An institution is significantly undercapitalized if it has a total risk-based capital ratio that is less than 6.0%, a Tier 1 risk-based capital ratio that is less than 3.0% or a leverage ratio that is less than 3.0%. A depository institution is critically undercapitalized if it has a ratio of tangible equity to total assets that is equal to or less than 2.0%. At December 31, 2003, the Bank qualified as a well capitalized institution under the OCC regulations.

**Prompt Corrective Measures for Capital Deficiencies.** FDICIA requires federal banking regulators to take prompt corrective action with respect to capital-deficient insured depository institutions with the overall goal of limiting losses to the BIF. With certain exceptions, a depository institution is prohibited from making capital distributions or paying management fees to its bank holding company if the payment of such distributions or fees will cause the institution to become undercapitalized. Furthermore, an undercapitalized institution must file a capital restoration plan with the OCC, which must be guaranteed by each company that controls such institution. See Business - The Corporation - Liability for Undercapitalized Subsidiaries. Undercapitalized institutions also are subject to restrictions on growth, acquisitions, branching and engaging in new lines of business unless they have an approved capital restoration plan that otherwise permits such activities. An institution that is not well capitalized may not accept brokered deposits without prior regulatory approval and will be subject to limitations on interest rates that it offers on its deposits. In addition, the OCC may, among other things, require an undercapitalized institution to issue securities or other obligations to raise funds to recapitalize the institution or, under certain circumstances, divest one or more of its subsidiaries for such purpose.

The OCC and other Federal banking agencies are authorized by FDICIA to take various enforcement actions against any significantly undercapitalized institution and action may be taken against an institution that fails to submit an acceptable capital restoration plan or fails to implement a capital restoration plan approved by the OCC. Such actions may include, among other things, prohibiting asset growth or requiring asset reduction, restricting interest rates paid, requiring FRB prior approval of any capital distributions by any bank holding company which controls the institution, requiring divestiture by the institution of its subsidiaries or by the holding company of the institution itself, requiring an election of new directors of the institution and requiring the dismissal of its directors and officers.

Critically undercapitalized institutions may be subject to more extensive control and supervision. A critically undercapitalized institution may be prohibited from, among other things, entering into any material transaction not in the ordinary course of business, amending its charter or bylaws or engaging in certain transactions with affiliates. In addition, critically undercapitalized institutions generally will be prohibited from making payments of principal or interest on outstanding subordinated debt. Within 90 days of the date on which an institution becomes critically undercapitalized, the OCC must appoint a receiver or conservator unless certain findings are made with respect to the prospect for the institution's continued viability.

**Deposit Insurance Assessments.** Under FDICIA, the FDIC is required to assess premiums on an insured depository institution's deposits in order to adequately fund the BIF. The FDIC has established a risk-based insurance premium assessment system that is used to calculate deposit insurance assessments made on BIF member banks. Under the assessment system, each insured depository institution is assigned to one of nine risk classifications based upon certain capital and supervisory measures and, depending upon its classification, assessed insurance premiums on its deposits. Insured depository institutions are required to pay insurance premiums ranging from 0% of insured deposits to 0.27% of insured deposits. The Bank currently qualifies for the 0% insurance premium assessment.

Under the Deposit Insurance Funds Act of 1996 (the Funds Act), banks insured under the BIF were required to pay a part of the interest on bonds issued by the Financing Corporation ( FICO ) in the late 1980s to recapitalize the defunct Federal Savings and Loan Insurance Corporation. Before the Funds Act, FICO payments were made only by depository institutions which were members of the Savings Association Insurance Fund (the SAIF). Prior to January 1, 2000, the Funds Act provided that BIF members were assessed for FICO payments at only one-fifth the rate of assessment on SAIF members. However, beginning January 1, 2000, the Funds Act provided that all BIF- and SAIF-insured institutions must pay FICO assessments at the same rate. For the first quarter of 2004, FICO rates have been set at .0154% for both BIF and SAIF members. The FICO assessment rates for both BIF and SAIF members for 2003 were as follows:

Fourth Quarter	.0152%
Third Quarter	.0160%
Second Quarter	.0162%
First Quarter	.0168%

**Community Reinvestment Act.** The Community Reinvestment Act of 1977 ( CRA ) and the regulations issued by the OCC thereunder are intended to encourage banks to help meet the credit needs of their service area, including low and moderate income neighborhoods, consistent with the safe and sound operations of the banks. These regulations also provide for regulatory assessment of a bank's record in meeting the needs of its service area when considering applications to establish branches, merger applications and applications to acquire the assets of another bank. FIRREA requires federal banking agencies to publicly disclose the rating of a bank's performance under the CRA. In the case of a bank holding company, the CRA performance record of its subsidiary bank is reviewed in connection with the filing of an application to acquire ownership or control of securities or assets of a bank or to merge with any other bank holding company. An unsatisfactory record can substantially delay or block the transaction. A less than satisfactory CRA rating can limit the extent to which a bank holding company and its affiliates can take advantage of the expanded range of activities permitted by the GLB Act.

#### **Customer Privacy**

Under the GLB Act, federal banking regulators have adopted rules limiting the ability of banks and other financial institutions to disclose nonpublic information about consumers. These rules require each financial institution to establish an information security program and a written plan containing policies and procedures designed to prevent the disclosure of nonpublic information about consumers. The plan must be adjusted on a continuing basis for changes in technology, the sensitivity of consumer information and internal and external threats to information security. A financial institution's policy for protecting nonpublic information about consumers must be disclosed to the customer at the time the customer relationship is established and at least annually thereafter.

#### **Changing Regulatory Structure**

Various proposals relating to the regulation of banks and other financial institutions are introduced from time to time by Congress, states and other regulatory authorities. If enacted or otherwise adopted, any of such proposals could significantly change the regulation of banks and other financial institutions in substantial and unexpected ways. The Corporation cannot predict whether any such proposals will be enacted or otherwise adopted or, if enacted or adopted, the extent to which such proposals would affect the business, results of operations and financial condition of the Corporation or the Bank.

#### **Monetary Policy and Economic Controls**

The business, results of operations and financial condition of the Corporation and the Bank are affected by the policies of regulatory authorities, including the monetary policies of the FRB. An important function of the FRB is to promote orderly economic growth by influencing interest rates and the supply of money and credit. Among the methods that have been used by the FRB to achieve this objective are open market operations in United States government securities, control of borrowings at the discount window, changes in the discount rate for member bank borrowing, changes in reserve requirements against member bank deposits and certain borrowings by banks and their affiliates and the placement of limitations on interest rates that member banks may pay on time and savings deposits. FRB monetary policies have materially affected the business, results of operations and financial condition of banks and other financial institutions in the past and are expected to continue to do so in the future. The Corporation cannot predict the nature of any future monetary policies or the effect that such policies may have on the business, results of operations and financial condition of the Corporation and the Bank.

#### **ITEM 2. PROPERTIES.**

The principal executive offices of the Corporation are located at 3880 Hulen Street, Suite 300, Fort Worth, Texas 76107. The Corporation and the Bank lease space at this address from an unrelated third party through a lease that expires in May 2010. This banking facility opened in May

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2003.

The Camp Bowie office of the Bank is located at 3859 Camp Bowie Boulevard, Fort Worth, Texas. The Bank owns the building located at this address.

The Downtown office of the Bank is located at 1300 Summit Avenue, Fort Worth, Texas. The Bank leases space for its Downtown office from a third party under a lease agreement expiring in December 2009. The Bank also owns a detached motor bank facility at 1401 Summit Avenue.

The Alta Mesa office of the Bank is located at 3000 Alta Mesa Boulevard, Fort Worth, Texas. The Bank owns the building located at this address. The Bank uses approximately 20% of the facilities for its operations and leases the remainder of the facilities to others.

The Northeast office and a motor bank facility of the Bank are located at 9001 Airport Freeway, North Richland Hills, Texas. The Bank leases these facilities from a third party under a lease agreement expiring in April 2008. The Bank owns a tract of land adjacent to the Northeast office on which it intends to build a new motor bank facility that would be owned by the Bank.

The Fossil Creek office of the Bank is located at 3851 NE Loop 820, Fort Worth, Texas. The building located at this address is owned by a joint venture between the Bank and an unrelated third party. The Fossil Creek office occupies approximately 28% of the building pursuant to a long-term lease with the joint venture.

The Davis office of the Bank is located at 8501 Davis Boulevard, North Richland Hills, Texas. The Bank owns the building at this address. This banking facility opened in January 2003.

**ITEM 3. LEGAL PROCEEDINGS.**

Although the Corporation and the Bank are routinely involved in legal proceedings incidental to their businesses, the Corporation believes that neither it nor the Bank is currently a party to any material legal proceeding.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.**

No matters were submitted to a vote of security holders during the fourth quarter of 2003.

## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

**Market Information.** Since May 3, 1993, the Common Stock of the Corporation has traded on the Nasdaq National Market System under the symbol SBIT. The following table sets forth the high and low bid prices for the Common Stock for the periods indicated:

	<u>High</u>	<u>Low</u>
<u>2003 Fiscal Year:</u>		
First Quarter	\$ 20.00	\$ 18.86
Second Quarter	25.40	18.95
Third Quarter	28.50	23.47
Fourth Quarter	28.95	26.45
<u>2002 Fiscal Year:</u>		
First Quarter	\$ 21.15	\$ 18.00
Second Quarter	25.30	20.30
Third Quarter	24.59	20.22
Fourth Quarter	21.21	18.77

On June 30, 2003, the closing price reported for the Common Stock was \$23.48. The foregoing quotations reflect prices quoted by market makers of the Common Stock, without retail markup, markdown or commissions, and may not necessarily represent actual transactions.

**Shareholders.** At the close of business on March 1, 2004, there were 587 shareholders of record of the Common Stock.

**Dividends.** The Corporation has paid regular cash dividends on the Common Stock on a quarterly basis since 1993. The following table sets forth the quarterly dividends paid by the Corporation on the Common Stock for the indicated periods:

	<u>Dividends Per Share</u>	
<u>2003 Fiscal Year:</u>		
First Quarter	\$	0.12
Second Quarter		0.12
Third Quarter		0.14
Fourth Quarter		0.14
<u>2002 Fiscal Year:</u>		
First Quarter	\$	0.12
Second Quarter		0.12
Third Quarter		0.12
Fourth Quarter		0.12

Although the Corporation intends to continue to pay quarterly cash dividends on the Common Stock in the future, there can be no assurance that the Corporation will pay cash dividends in the future or, if paid, that such cash dividends will be comparable to cash dividends previously paid by the Corporation. The Corporation's future dividend policy is subject to the discretion of the Board of Directors of the Corporation and will depend upon a number of factors, including the Corporation's future earnings, financial condition and cash needs, general business conditions and the amount of dividends paid to the Corporation by the Bank. See Business - The Corporation - Restrictions on Payment of Dividends and Business - The Bank - Restrictions on Payment of Dividends for additional factors that may limit the ability of the Corporation and the Bank to pay cash dividends.



**ITEM 6. SELECTED FINANCIAL DATA.**

The following table sets forth selected financial data of the Corporation for the past five years (in thousands except ratios and per share data). The information set forth below is not necessarily indicative of future results, and should be read in conjunction with Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations and the Corporation's consolidated financial statements and notes thereto included in Item 8 of this Annual Report on Form 10-K.

	Years Ended December 31,				
	2003	2002	2001	2000	1999
<b>Summary of Earnings:</b>					
Interest Income	\$ 38,527	\$ 38,657	\$ 44,497	\$ 47,609	\$ 40,232
Interest Expense	7,437	8,512	15,527	18,870	13,772
Net Interest Income	31,090	30,145	28,970	28,739	26,460
Provision for Loan Losses	880	3,140	1,755	2,606	1,001
Securities Gains (Losses)	230	165	-0-	(2)	(3)
Non-interest Income	5,798	5,302	4,516	3,780	3,883
Non-interest Expense	21,453	18,309	18,265	16,170	15,224
Earnings Before Income Taxes	14,785	14,163	13,466	13,741	14,115
Income Tax Expense	5,017	4,846	4,664	4,765	4,893
Net Income	\$ 9,768	\$ 9,317	\$ 8,802	\$ 8,976	\$ 9,222
<b>Balance Sheet Data (at period-end):</b>					
Total Assets	\$ 795,478	\$ 687,733	\$ 635,956	\$ 619,121	\$ 564,786
Investment Securities	195,959	173,512	160,136	149,647	156,440
Loans, Net of Unearned Discount	553,769	469,145	430,754	380,016	355,414
Allowance for Loan Losses	7,784	6,706	6,015	5,399	5,169
Demand Deposits	192,877	167,745	150,040	146,083	128,685
Total Deposits	641,381	581,949	543,803	539,666	480,546
Short Term Borrowings	82,234	37,255	28,366	19,910	32,091
Shareholders' Equity	68,684	64,938	60,536	55,571	48,709
<b>Per Share Data:</b>					
Net Income - Basic	\$ 1.59	\$ 1.50	\$ 1.39	\$ 1.41	\$ 1.44
Net Income - Diluted	1.55	1.46	1.36	1.38	1.39
Book Value - Period-End	11.17	10.58	9.67	8.73	7.66
Dividends Declared and Paid	0.52	0.48	0.44	0.40	0.32
Weighted Average Shares Outstanding (000)	6,161	6,224	6,318	6,364	6,411
Average Common Share Equivalents (000)	156	172	153	160	245
<b>Selected Performance Ratios:</b>					
Return on Average Assets	1.32%	1.39%	1.41%	1.54%	1.72%
Return on Average Shareholders' Equity	14.43	14.74	15.01	17.57	19.66
Dividend Payout Ratio	32.81	32.05	31.61	28.38	22.25
Net Interest Margin (tax equivalent)	4.48	4.80	4.93	5.25	5.31
Efficiency Ratio	57.57	51.26	54.55	49.71	50.14
<b>Asset Quality Ratios:</b>					
Non-Performing Loans to Total Loans - Period-End	0.43%	0.46%	0.96%	0.58%	0.69%
Non-Performing Assets to Total Assets - Period-End	0.30	0.50	0.72	0.61	0.78
Allowance for Loan Losses to Total Loans - Period-End	1.41	1.43	1.40	1.42	1.45
Allowance for Loan Losses to Non-Performing Loans - Period-End	324.0	314.0	146.0	247.0	211.0
Net Charge-Offs to Average Loans	(0.04)	0.53	0.28	0.64	0.16
<b>Capital Ratios:</b>					
Shareholders' Equity to Total Assets - Period-End	8.63%	9.44%	9.52%	8.98%	8.62%

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Average Shareholders Equity to Average Assets	9.15	9.45	9.40	8.74	8.71
Total Risk-based Capital to Risk Weighted Assets - Period-End*	12.70	13.41	14.34	14.97	14.59
Leverage Ratio - Period-End*	8.62	8.96	9.20	8.88	8.77

\*Calculated in accordance with Federal Reserve guidelines currently in effect.

**Quarterly Results (Unaudited)**

A summary of the unaudited results of operations for each quarter of 2003 and 2002 follows (in thousands except for per share data):

	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
<b>2003</b>				
Interest Income	\$ 9,251	\$ 9,547	\$ 9,709	\$ 10,020
Interest Expense	1,816	1,934	1,834	1,853
Net Interest Income	7,435	7,613	7,875	8,167
Provision for Loan Losses	300	240	46	294
Gain on Sale of Securities	-0-	12	89	129
Non-interest Income	1,347	1,586	1,494	1,371
Non-interest Expense	4,797	5,246	5,656	5,754
Earnings Before Income Taxes	3,685	3,725	3,756	3,619
Income Tax Expense	1,252	1,268	1,281	1,216
Net Income	\$ 2,433	\$ 2,457	\$ 2,475	\$ 2,403
Per Share Data:				
Net Income:				
Basic	\$ 0.39	\$ 0.40	\$ 0.40	\$ 0.39
Diluted	0.39	0.39	0.39	0.38
Dividends Paid	0.12	0.12	0.14	0.14
Stock Price Range:				
High	20.00	25.40	28.50	28.95
Low	18.86	18.95	23.47	26.45
Close	19.12	23.48	27.00	27.61
	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
<b>2002</b>				
Interest Income	\$ 9,549	\$ 9,666	\$ 9,839	\$ 9,603
Interest Expense	2,132	2,199	2,200	1,981
Net Interest Income	7,417	7,467	7,639	7,622
Provision for Loan Losses	545	470	1,350	775
Gain on Sale of Securities	-0-	2	163	-0-
Non-interest Income	1,245	1,330	1,367	1,360
Non-interest Expense	4,638	4,681	4,215	4,775
Earnings Before Income Taxes	3,479	3,648	3,604	3,432
Income Tax Expense	1,193	1,254	1,232	1,167
Net Income	\$ 2,286	\$ 2,394	\$ 2,372	\$ 2,265
Per Share Data:				
Net Income:				
Basic	\$ 0.37	\$ 0.38	\$ 0.38	\$ 0.37
Diluted	0.36	0.37	0.37	0.36
Dividends Paid	0.12	0.12	0.12	0.12
Stock Price Range:				

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High	21.15	25.30	24.59	21.21
Low	18.00	20.30	20.22	18.77
Close	20.80	24.29	21.05	19.50

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**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

The following discussion should be read in conjunction with the consolidated financial statements, accompanying notes and selected financial data appearing elsewhere in this Annual Report on Form 10-K and may contain certain forward-looking statements that are based on current management expectations. Generally, verbs in the future tense and the words, believe, expect, anticipate, intends, opinion, potential and similar expressions identify forward-looking statements. Examples of this forward-looking information can be found in, but are not limited to, the expected effects of accounting pronouncements and government regulation applicable to the Corporation's operations, the discussion of allowance for loan losses, litigation, subsequent events and any quantitative and qualitative disclosure about market risk. The actual results of the Corporation could differ materially from those management expectations. Further information concerning the Corporation and its business, including additional risk factors and uncertainties that could cause actual results to differ materially from the forward-looking statements contained in this Annual Report on Form 10-K are set forth below. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. The forward-looking statements contained herein speak only as of the date of this Annual Report on Form 10-K, and, except as may be required by applicable law and regulation, the Corporation does not undertake, and specifically disclaims any obligation, to publicly update or revise the such statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

**Overview.** The Corporation's business has been conducted primarily through its wholly-owned subsidiaries, the Bank, Summit Delaware Financial Corporation and SIA. The Bank operates its branch offices in seven locations in Fort Worth.

The Corporation's results of operations are primarily dependent on net interest income, which is the difference between the income earned on its loan and investment portfolios and its cost of funds, consisting of the interest paid on deposits and borrowings. Results of operations are also affected by the Corporation's allowance for loan losses, investment activities, loan servicing fees and other fees. The Corporation's non-interest expense principally consists of compensation and benefits, occupancy and equipment expense, advertising, data processing expense and other expenses.

Net income for 2003 was \$9.8 million, an increase of \$0.5 million, or 4.8%, compared to \$9.3 million recorded for 2002. On a weighted average share basis, net income for 2003 was \$1.55 per diluted share as compared to \$1.46 per diluted share for 2002, an increase of 6.2%. The increase in earnings during 2003 was primarily due to an increase in net interest income of \$1.0 million over 2002. The increase in net interest income was primarily due to growth in average loans of 8.9%, which more than offset the impact of the low interest rate environment and a declining net interest margin. The increase in non-interest expenses during 2003 was primarily attributable to strategic investments in new technology, new branches, new support facilities and additional lending staff. These expenses were offset during 2003 by a significant reduction in the provision for loan losses as compared to 2002. In 2003, loan recoveries exceeded loan losses, as credit quality and the local economy both continued to improve.

Continuing to reflect an improving economy in the Corporation's market area, total loans at December 31, 2003 were \$553.8 million, which represented an increase of 18.0% over total loans for 2002. Total funding (deposits and short term borrowings) also experienced growth, increasing 16.9% over the same period to \$723.6 million. Shareholders' equity was \$68.7 million at December 31, 2003, which represented an increase of 5.8% compared to December 31, 2002.

Net income for 2002 was \$9.3 million compared to net income of \$8.8 million for 2001, an increase of 5.9%. The increase in net income for 2002 was primarily attributable to merger-related expenses incurred during the first quarter of 2001 when two of the Corporation's wholly-owned banking subsidiaries were merged. Net income in 2002 was reduced by an increase in the provision for loan losses, which was primarily due to increased loan charge-offs, as compared to 2001.

The following table shows selected performance ratios over the last three years that management believes to be key indicators of the Corporation's performance:

	2003	2002	2001
Return on Average Assets (ROAA)	1.32%	1.39%	1.41%
Return on Average Shareholders' Equity (ROAE)	14.43	14.74	15.01
Shareholders' Equity to Assets - Average	9.15	9.45	9.40
Dividend Payout Ratio	32.81	32.05	31.61
Net Interest Margin (tax equivalent)	4.48	4.80	4.93
Efficiency Ratio	57.57	51.26	54.55

The return on average assets ratio is calculated by dividing net income by average total assets for the year. Management believes the Corporation's return on average assets ratio of 1.32% in 2003 compares favorably to the return on average assets ratio of other financial institutions in the Corporation's peer group, which was 1.34% in 2003. The Corporation's peer group is comprised of other publicly traded bank holding companies headquartered in Texas and was selected by management of the Corporation.

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The return on average shareholders' equity ratio is calculated by dividing net income by average shareholders' equity for the year. Management believes the Corporation's return on average shareholders' equity ratio of 14.43% in 2003 compares favorably to the return on average shareholders' equity ratio of other financial institutions in the Corporation's peer group, which was 15.49% in 2003.

The shareholders' equity to assets ratio is calculated by dividing average shareholders' equity by average total assets for the year. Management believes the Corporation's average shareholders' equity to average assets ratio of 9.15% in 2003 compares favorably to the return on average shareholders' equity to average asset ratio of other financial institutions in the Corporation's peer group, which was 8.63% in 2003.

The dividend payout ratio is determined by dividing the total dividends paid by net income for the year. The Corporation's dividend payout ratio results in a yield-to-market price return equal to or greater than the Corporation's peer group.

Net interest margin is calculated by dividing net interest income on a tax equivalent basis by average total earning assets. Management believes the Corporation's net interest margin ratio of 4.48% in 2003 compares favorably to the net interest margin ratio of other financial institutions in the Corporation's peer group, which was 4.07% in 2003.

The efficiency ratio is calculated by dividing non-interest expenses by the sum of total non-interest income and net interest income for the year. The efficiency ratio provides a measure of the extent to which the Corporation's revenues are absorbed by its non-interest expenses. Management believes the Corporation's efficiency ratio of 57.57% in 2003 compares favorably to the average efficiency ratio of other financial institutions in the Corporation's peer group, which was 59.71% in 2003.

**Net Interest Income.** Net interest income is the difference between the interest earned by the Corporation on its earning assets and the interest paid by the Corporation for the funds, primarily deposits, supporting those assets. The largest category of the Corporation's earning assets consists of loans to businesses and individuals. The second largest category of the Corporation's earning assets is investment securities. Interest rate fluctuations, as well as changes in the amount and type of earning assets and sources of funds supporting those assets, affect net interest income. Interest rates primarily are determined by national and international market trends, as well as competitive pressures in the Corporation's operating markets. For analytical purposes, income from tax-exempt assets, which consists primarily of securities issued by or loans made to state and local governments, is adjusted by an increment which equates income from tax-exempt assets to income from taxable assets.

Net interest income (tax equivalent) for 2003 was \$31.2 million, which represented an increase of \$1.0 million, or 3.3%, compared to 2002. The net increase in net interest income in 2003 reflected a \$0.1 million decrease in interest income which was offset by a \$1.1 million decrease in interest expense.

The decreases in interest income and interest expense in 2003 were primarily due to decreases in the Corporation's yield on earning assets and rates paid on its interest-bearing liabilities. The yield on earning assets decreased to 5.54% for 2003 from 6.15% for 2002, and the rates paid on interest-bearing liabilities decreased to 1.50% for 2003 from 1.91% for 2002. These decreases resulted in the net interest margin decreasing to 4.48% in 2003 from 4.80% for 2002. The decreases in the yields earned on earning assets and the rates paid on interest-bearing liabilities reflect the decline in market rates from 2002 to 2003, as measured by the decline in average prime rates over the same period (as published by the Wall Street Journal) of 55 basis points.

The increase in net interest income for 2003 was primarily due to the 8.9% growth in average loans and the 8.2% growth in average deposits during the same period, which offset the 32 basis point decline in net interest margin. Average demand deposits as a percent of average total deposits increased to 28.4% in 2003 from 27.9% in 2002.

Net interest income (tax equivalent) for 2002 was \$30.2 million, which represented an increase of \$1.3 million, or 4.4%, compared to 2001. The net increase in net interest income in 2002 reflected a \$5.7 million decrease in interest income which was offset by a \$7.0 million decrease in interest expense.

The decreases in interest income and interest expense in 2002 were primarily due to decreases in the Corporation's yield on earning assets and rates paid on its interest-bearing liabilities. The yield on earning assets decreased to 6.15% for 2002 from 7.57% for 2001, and the rates paid on interest-bearing liabilities decreased to 1.91% for 2002 from 3.67% for 2001. These decreases resulted in the net interest margin decreasing to 4.80% in 2002 from 4.93% for 2001. The decreases in the yields earned on earning assets and the rates paid on interest-bearing liabilities reflect the decline in market rates from 2001 to 2002, as measured by the decline in average prime rates over the same period (as published by the Wall Street Journal) of 224 basis points.

The increase in net interest income for 2002 was primarily due to the 15.0% growth in average loans and the 3.5% growth in average deposits during the same period, which offset the 13 basis point decline in net interest margin. Average demand deposits as a percent of average total deposits increased to 27.9% in 2002 from 25.5% in 2001.

**Summary of Earning Assets and Interest-Bearing Liabilities**

Although the year-end detail provides satisfactory indicators of general trends, management believes the daily average balance sheets are more meaningful for analytical purposes than year-end data because averages reflect the day-to-day fluctuations that are common to bank balance sheets. Average balances for earning assets and interest-bearing liabilities also can be related directly to the components of interest income and interest expense on the consolidated statements of income. This data provides the basis for analyzing rates earned and paid as well as sources of increases and decreases in net interest income as derived from changes in volumes and rates. The following table presents average balance sheets for the most recent three years in a format that highlights the Corporation's earning assets and interest-bearing liabilities over such periods:

(Dollars in Thousands)	2003			2002			2001		
	Average Balance	Interest	Yield/Rate	Average Balance	Interest	Yield/Rate	Average Balance	Interest	Yield/Rate
<b>Earning Assets:</b>									
Federal Funds Sold and Due From Time	\$ 7,912	\$ 81	1.02%	\$ 12,989	\$ 212	1.63%	\$ 44,689	\$ 1,972	4.41%
Investment Securities (Taxable)	179,539	7,106	3.96	150,704	7,046	4.68	139,875	7,966	5.70
Investment Securities (Tax-exempt)(2)	5,779	314	5.43	3,060	177	5.77	231	17	7.36
Loans, Net of Unearned Discount(1)	504,520	31,171	6.18	463,106	31,326	6.76	402,763	34,548	8.58
<b>Total Earning Assets</b>	<b>697,750</b>	<b>38,672</b>	<b>5.54</b>	<b>629,859</b>	<b>38,761</b>	<b>6.15</b>	<b>587,558</b>	<b>44,503</b>	<b>7.57</b>
<b>Other Assets:</b>									
Cash and Due From Banks	26,295			25,728			24,259		
Other Assets	22,964			19,760			17,922		
Allowance for Loan Losses	(7,351)			(6,438)			(5,816)		
<b>Total Assets</b>	<b>\$ 739,658</b>			<b>\$ 668,909</b>			<b>\$ 623,923</b>		
<b>Interest-Bearing Liabilities:</b>									
<b>Interest-Bearing</b>									
Transaction Accounts	\$ 193,841	2,108	1.09	\$ 180,060	2,378	1.32	\$ 167,853	4,298	2.56
Savings	119,851	1,581	1.32	112,977	1,909	1.69	101,295	3,367	3.32
Certificates of Deposit under \$100,000 and IRAs	62,938	1,563	2.48	64,042	2,041	3.19	77,968	4,198	5.39
Certificates of Deposit \$100,000 or More	59,072	1,551	2.63	48,286	1,542	3.19	56,848	3,061	5.38
Other Time	315	7	2.26	339	11	3.18	723	43	5.91
Other Borrowings	60,156	627	1.04	39,453	631	1.60	18,518	560	3.02
<b>Total Interest-Bearing Liabilities</b>	<b>496,173</b>	<b>7,437</b>	<b>1.50</b>	<b>445,157</b>	<b>8,512</b>	<b>1.91</b>	<b>423,205</b>	<b>15,527</b>	<b>3.67</b>
<b>Other Liabilities:</b>									
Demand Deposits	172,784			156,868			138,880		
Other Liabilities	3,028			3,695			3,188		
Shareholders' Equity	67,673			63,189			58,650		
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 739,658</b>			<b>\$ 668,909</b>			<b>\$ 623,923</b>		



Net Interest Income and Margin (T/E Basis)(2)	\$ 31,235	4.48%	\$ 30,249	4.80%	\$ 28,976	4.93%
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(1) Loan interest income includes fees and loan volumes include loans on non-accrual. The loan fees include loan origination fees which are considered adjustments to interest income. These fees aggregated \$1,248,000, \$1,097,000 and \$928,000 for the years ended December 31, 2003, 2002 and 2001, respectively. Related loan origination costs are not separately allocated to loans, but are charged to non-interest expense. For the purpose of calculating loan yields, average loan balances include non-accrual loans with no related interest income.

(2) Presented on a tax equivalent basis ( T/E ) using a federal income tax rate of 34% in all three years.

Net interest margin was 4.48% for 2003, which represented a decrease of 32 basis points from 2002. This decrease in net interest margin in 2003 reflected a 61 basis point decrease in yield on earning assets from 2002 to 2003, which was offset by a 41 basis point decrease in rates paid on interest-bearing liabilities from 2002 to 2003. The decrease in net interest margin also reflected less earned income from the Corporation's investment in earning assets of its non-interest fundings, demand deposits and shareholders' equity in 2003 compared to 2002 due to the lower interest rate environment during this period.

Net interest margin was 4.80% for 2002, which represented a decrease of 13 basis points from 2001. This decrease in net interest margin in 2002 reflected a 142 basis point decrease in yield on earning assets from 2001 to 2002, which was offset by a 176 basis point decrease in rates paid on interest-bearing liabilities from 2001 to 2002. The decrease in net interest margin also reflected less earned income from the Corporation's investment in earning assets of its non-interest fundings, demand deposits and shareholders' equity in 2002 compared to 2001 due to the lower interest rate environment during this period.

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With the projected continued low interest rate environment for 2004, it would be expected that the net interest margin would remain in the 4.40% range.

In the event that the Corporation's average loans continue to grow during 2004 and the Corporation is unable to fund any such growth through the generation of additional deposits, the Corporation may be required to obtain funding from secondary sources, such as the Federal Home Loan Bank, which could have a negative impact on its net interest margin.

The table below analyzes the increase in net interest income on a fully tax equivalent basis for each of the fiscal years ended December 31, 2001 to December 31, 2003. Non-accruing loans have been included in assets for these computations, thereby reducing yields on total loans. The changes in interest due to both rate and volume in the rate/volume analysis table below have been allocated to volume or rate change in proportion to the absolute amounts of the change in each.

(Dollars in Thousands)	2003 vs. 2002 Increase (Decrease) Due to Changes in:			2002 vs. 2001 Increase (Decrease) Due to Changes in:		
	Volume	Rate	Total	Volume	Rate	Total
Interest Earning Assets:						