

Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

MIDDLEFIELD BANC CORP  
Form 10-Q/A  
November 14, 2001

UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20552

FORM 10 - Q

QUARTERLY REPORT UNDER SECTION 13 OF 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934

For the quarterly period ended September 30, 2001

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 33-23094  
-----

Middlefield Banc Corp.  
-----

(Exact name of registrant as specified in its charter)

Ohio  
-----

34 - 1585111  
-----

(State or other jurisdiction of  
incorporation or organization)

(IRS Employer Identification No.)

15985 East High Street, Middlefield, Ohio 44062-9263  
-----

(Address of principal executive offices)

(440) 632-1666  
-----

(Registrant's telephone number, including area code)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or 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    X  
-----

State the number of shares outstanding of each of the issuer's classes of common equity as of the latest practicable date:

Class: Common Stock, without par value  
Outstanding at November 9, 2001: 1,102,954

MIDDLEFIELD BANC CORP.  
INDEX

Page  
Number  
-----

Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

Consolidated Balance Sheet (Unaudited) as of September 30, 2001 and December 31, 2000	3
Consolidated Statement of Income (Unaudited) for the Nine and Three Months ended September 30, 2001 and 2000	4
Consolidated Statement of Changes in Stockholders' Equity (Unaudited)	5
Consolidated Statement of Cash Flows (Unaudited) for the Nine Months ended September 30, 2001 and 2000	6
Notes to Unaudited Consolidated Financial Statements	7 - 11

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	12 - 16
--	---------

Item 3. Quantitative and Qualitative Disclosures About Market Risk	18 - 19
--	---------

PART II - OTHER INFORMATION

Item 1. Legal Proceedings	20
Item 2. Changes in Securities	20
Item 3. Default Upon Senior Securities	20
Item 4. Submissions of Matters to a Vote of Security Holders	20
Item 5. Other Information	20
Item 6. Exhibits and Reports on Form 8 - K	20 - 21

SIGNATURES	22
------------	----

MIDDLEFIELD BANC CORP.  
CONSOLIDATED BALANCE SHEET  
(Unaudited)

	September 30 2001 -----	Decemb 20 -----
<b>ASSETS</b>		
Cash and due from banks	\$ 4,429,131	\$ 3,
Federal funds sold	1,920,000	1,
	-----	-----
Cash and cash equivalents	6,349,131	4,
Interest-bearing deposits in other institutions	890,198	
Investment securities available for sale	17,514,223	11,
Investment securities held to maturity (estimated)		

Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

market value of \$11,310,338 and \$17,942,255)	11,006,296	17,
Loans	149,438,223	135,
Less allowance for loan losses	2,048,027	2,
	-----	-----
Net loans	147,390,196	133,
Premises and equipment	6,000,927	5,
Accrued interest and other assets	2,430,127	2,
	-----	-----
TOTAL ASSETS	\$ 191,581,098	\$ 176,
	=====	=====
LIABILITIES		
Deposits:		
Noninterest-bearing demand	\$ 24,149,286	\$ 23,
Interest-bearing demand	6,803,635	6,
Money market	7,461,686	9,
Savings	36,548,244	32,
Time	86,075,193	76,
	-----	-----
Total deposits	161,038,044	147,
Short-term borrowings	713,523	
Other borrowings	9,349,450	9,
Accrued interest and other liabilities	840,317	
	-----	-----
TOTAL LIABILITIES	171,941,334	158,
	-----	-----
STOCKHOLDERS' EQUITY		
Common stock, no par value; 5,000,000 shares authorized, 1,148,676 shares issued	6,287,011	6,
Retained earnings	14,569,319	13,
Accumulated other comprehensive income	259,874	
Treasury stock, at cost (45,722 shares)	(1,476,440)	(1,
	-----	-----
TOTAL STOCKHOLDERS' EQUITY	19,639,764	18,
	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 191,581,098	\$ 176,
	=====	=====

See accompanying notes to unaudited consolidated financial statements.

MIDDLEFIELD BANC CORP.  
CONSOLIDATED STATEMENT OF INCOME  
(Unaudited)

	Nine Months Ended		T
	September 30,		
	2001	2000	200
	-----	-----	-----
INTEREST INCOME			

Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

Interest and fees on loans	\$ 8,818,686	\$ 8,035,655	\$ 3,04
Interest-bearing deposits in other institutions	47,801	77,867	1
Federal funds sold	114,668	57,338	1
Investment securities:			
Taxable interest	939,442	889,596	31
Tax-exempt interest	349,574	399,188	11
	-----	-----	-----
Total interest income	10,270,171	9,459,644	3,50
	-----	-----	-----
INTEREST EXPENSE			
Deposits	4,694,735	3,861,098	1,59
Short-term borrowings	13,000	53,737	
Other borrowings	403,752	394,663	13
	-----	-----	-----
Total interest expense	5,111,487	4,309,498	1,73
	-----	-----	-----
NET INTEREST INCOME	5,158,684	5,150,146	1,77
Provision for loan losses	125,000	225,000	4
	-----	-----	-----
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	5,033,684	4,925,146	1,73
	-----	-----	-----
NONINTEREST INCOME			
Service charges on deposit accounts	688,038	593,480	23
Investment securities gains, net	97,807	886	9
Other income	106,387	97,102	3
	-----	-----	-----
Total noninterest income	892,232	691,468	36
	-----	-----	-----
NONINTEREST EXPENSE			
Salaries and employee benefits	1,693,834	1,633,886	54
Occupancy expense	216,996	242,722	6
Equipment expense	221,199	169,657	7
Data processing costs	211,367	184,189	7
Ohio state franchise tax	180,050	170,180	6
Other expense	954,065	814,332	32
	-----	-----	-----
Total noninterest expense	3,477,511	3,214,966	1,14
	-----	-----	-----
Income before income taxes	2,448,405	2,401,648	94
Income taxes	759,826	721,370	28
	-----	-----	-----
NET INCOME	\$ 1,688,579	\$ 1,680,278	\$ 65
	=====	=====	=====
EARNINGS PER SHARE			
Basic	\$ 1.53	\$ 1.52	\$
Diluted	1.53	1.52	

See accompanying notes to unaudited consolidated financial statements.

MIDDLEFIELD BANC CORP.  
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY  
(Unaudited)

	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock
	-----	-----	-----	-----
Balance, December 31, 2000	\$ 6,287,011	\$ 13,343,980	\$ 88,811	\$ (1,476,44
Net income		1,688,579		
Other comprehensive income:				
Unrealized gain on available for sale securities net of taxes of \$58,161			171,063	
Comprehensive income				
Cash dividends (\$.42 per share)		(463,240)		
	-----	-----	-----	-----
Balance, September 30, 2001	\$ 6,287,011	\$ 14,569,319	\$ 259,874	\$ (1,476,44
	=====	=====	=====	=====

See accompanying notes to unaudited consolidated financial statements.

MIDDLEFIELD BANC CORP.  
CONSOLIDATED STATEMENT OF CASH FLOWS  
(Unaudited)

	Nine Months Ended September 30,	
	2001	2000
	-----	-----
OPERATING ACTIVITIES		
Net income	\$ 1,688,579	\$ 1,68
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	125,000	22
Depreciation and amortization	255,354	29

Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

Investment security gains, net	(97,807)	
Increase in accrued interest receivable	(44,762)	(7
Increase in accrued interest payable	148,030	8
Other, net	(176,503)	(15
	-----	-----
Net cash provided by operating activities	1,897,891	2,06
	-----	-----
INVESTING ACTIVITIES		
Decrease in interest-bearing deposits in other institutions, net	94,243	2,24
Investment securities available for sale:		
Proceeds from repayments and maturities	3,530,734	1,20
Proceeds from sales	2,092,981	11
Purchases	(10,913,812)	(1,67
Investment securities held to maturity:		
Proceeds from repayments and maturities	6,891,514	2,47
Increase in loans, net	(14,235,110)	(11,61
Purchase of Federal Home Loan Bank stock	(124,800)	(11
Purchase of premises and equipment	(791,298)	(8
	-----	-----
Net cash used for investing activities	(13,455,548)	(7,45
	-----	-----
FINANCING ACTIVITIES		
Net increase in deposits	13,871,998	11,90
Increase in short-term borrowings, net	170,301	(1,85
Repayment of other borrowings	(512,146)	
Proceeds from other borrowings	--	33
Purchase of treasury stock	--	(1,31
Sale of treasury stock	--	3
Cash dividends	(463,240)	(35
	-----	-----
Net cash provided by financing activities	13,066,913	8,75
	-----	-----
Increase in cash and cash equivalents	1,509,256	3,35
CASH AND CASH EQUIVALENTS		
AT BEGINNING OF PERIOD	4,839,875	3,21
	-----	-----
CASH AND CASH EQUIVALENTS		
AT END OF PERIOD	\$ 6,349,131	\$ 6,57
	=====	=====
SUPPLEMENTAL INFORMATION Cash paid during the year for:		
Interest on deposits and borrowings	\$ 4,963,457	\$ 4,22
Income taxes	660,000	78

See accompanying notes to unaudited consolidated financial statements.

## Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

### NOTE 1 - BASIS OF PRESENTATION

The consolidated financial statements of Middlefield Banc Corp. ("Middlefield") includes its wholly-owned subsidiary, The Middlefield Banking Company (the "Bank"). All significant intercompany items have been eliminated.

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions for Form 10-Q and Article 10 of Regulation S-X. In Management's opinion, the financial statements include all adjustments, consisting of normal recurring adjustments, that Middlefield considers necessary to fairly state Middlefield's financial position and the results of operations and cash flows. The balance sheet at December 31, 2000, has been derived from the audited financial statements at that date but does not include all of the necessary informational disclosures and footnotes as required by accounting principles generally accepted in the United States of America. The accompanying financial statements should be read in conjunction with the financial statements and notes thereto included with Middlefield's Amended Form 10 (File No. 33-23094). Certain amounts in the 2000 financial statements have been reclassified to conform to 2001 presentation. The results of Middlefield's operations for any interim period are not necessarily indicative of the results of Middlefield's operations for any other interim period or for a full fiscal year.

### NOTE 2 - EARNINGS PER SHARE

Middlefield provides dual presentation of Basic and Diluted earnings per share. Basic earnings per share utilizes net income as reported as the numerator and the actual average shares outstanding as the denominator. Diluted earnings per share includes any dilutive effects of options, warrants, and convertible securities. For the nine and three months ended September 30, 2001, the diluted number of shares outstanding from employee stock options was 1,381 and 521, respectively. There was no diluted effect for the nine or three months ended September 30, 2000.

### NOTE 3 - COMPREHENSIVE INCOME

The components of comprehensive income consist exclusively of unrealized gains and losses on available for sale securities. For the nine months ended September 30, 2001, this activity is shown under the heading Comprehensive Income as presented in the Consolidated Statement of Changes in Stockholders' Equity (Unaudited). For the nine months ended September 30, 2000, comprehensive income totaled \$1,716,298. For the three months ended September 30, 2001 and 2000, comprehensive income totaled \$727,402 and \$632,886, respectively.

7

### NOTE 4 - RECENT ACCOUNTING PRONOUNCEMENTS

In July 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 141, Business Combinations, effective for all business combinations initiated after June 30, 2001, as well as all business combinations accounted for by the purchase method that are completed after June 30, 2001. The new statement requires that the purchase method of accounting be used for all business combinations and prohibits the use of the pooling-of-interests method. The adoption of Statement No. 141 is not expected to have a material affect on Middlefield's financial position or results of operations.

Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets, effective for fiscal years beginning after December 15, 2001. The new statement changes the accounting for goodwill from an amortization method to an impairment-only approach. Thus, amortization of goodwill, including goodwill recorded in past business combinations, will cease upon adoption of this Statement. The adoption of Statement No. 142 is not expected to have a material affect on Middlefield's financial position or results of operations.

NOTE 5 - INVESTMENT SECURITIES AVAILABLE FOR SALE

The amortized cost and estimated market values of securities available for sale are as follows:

	2001			Esti Mar Va
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
U.S. Government agency securities	\$ 2,156,189	\$ 86,568	\$ --	\$ 2,2
Obligations of states and political subdivisions:				
Taxable	1,408,186	28,188	--	1,4
Tax-exempt	4,266,442	139,829	--	4,4
Corporate securities	550,658	28,318	--	5
Mortgage-backed securities	8,739,000	123,892	(13,047)	8,8
<b>Total</b>	<b>\$17,120,475</b>	<b>\$ 406,795</b>	<b>\$ (13,047)</b>	<b>\$17,5</b>

8

NOTE 5 - INVESTMENT SECURITIES AVAILABLE FOR SALE (Continued)

	2000			Esti Mar Va
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
U.S. Government agency securities	\$ 3,990,419	\$ 70,843	\$ (1,419)	\$ 4,0
Obligations of states and political subdivisions:				
Taxable	1,458,400	11,744	(2,645)	1,4
Tax-exempt	3,685,472	42,258	(16,746)	3,7
Corporate securities	701,306	3,400	(2,800)	7



Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

Mortgage-backed securities	1,898,177	29,928	--	1,9
	-----	-----	-----	-----
Total	\$11,733,774	\$ 158,173	\$ (23,610)	\$11,8
	=====	=====	=====	=====

The amortized cost and estimated market value of debt securities at September 30, 2001, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Market Value
	-----	-----
Due in one year or less	\$ 2,550,848	\$ 2,574,370
Due after one year through five years	5,561,590	5,783,505
Due after five years through ten years	1,483,786	1,555,758
Due after ten years	7,524,251	7,600,590
	-----	-----
Total	\$17,120,475	\$17,514,223
	=====	=====

9

NOTE 6 - INVESTMENT SECURITIES HELD TO MATURITY

The amortized cost and estimated market values of securities held to maturity are as follows:

	2001			Esti
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Mar Va
	-----	-----	-----	-----
Obligations of states and political subdivisions:				
Taxable	\$ 2,050,577	\$ 73,694	\$ --	\$ 2,1
Tax-exempt	6,009,822	157,376	--	6,1
Corporate securities	2,717,907	65,692	--	2,7
Mortgage-backed securities	227,990	7,280	--	2
	-----	-----	-----	-----
Total	\$11,006,296	\$ 304,042	\$ --	\$11,3
	=====	=====	=====	=====

Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

	2000			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Esti Mar Va
U.S. Government agency securities	\$ 1,899,752	\$ --	\$ (8,565)	\$ 1,8
Obligations of states and political subdivisions:				
Taxable	3,723,251	18,354	(19,685)	3,7
Tax-exempt	7,480,801	26,182	(7,420)	7,4
Corporate securities	4,525,466	7,829	(18,683)	4,5
Mortgage-backed securities	313,040	1,933	--	3
Total	\$17,942,310	\$ 54,298	\$ (54,353)	\$17,9

10

NOTE 6 - INVESTMENT SECURITIES HELD TO MATURITY (Continued)

The amortized cost and estimated market value of debt securities at September 30, 2001, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Market Value
Due in one year or less	\$ 3,421,750	\$ 3,473,809
Due after one year through five years	7,115,489	7,353,191
Due after five years through ten years	141,067	149,098
Due after ten years	327,990	334,240
Total	\$11,006,296	\$11,310,338

11

## Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

### MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

#### General

The Private Securities Litigation Act of 1995 contains safe harbor provisions regarding forward-looking statements. Forward-looking statements can be identified by terminology such as "believes," "expects," "anticipates," "estimates," "intends," "should," "will," "plans," "potential" and similar words. Forward-looking statements are also statements that are not statements of historical fact. Forward-looking statements necessarily involve risks and uncertainties. They are merely predictive or statements of probabilities, involving known and unknown risks, uncertainties and other factors.

If one or more of these risks of uncertainties occurs or if the underlying assumptions prove incorrect, actual results in 2001 and beyond could differ materially from those expressed in or implied by the forward-looking statements.

Forward-looking statements are based upon a variety of estimates and assumptions. The estimates and assumptions involve judgments about a number of things, including future economic, competitive, and financial market conditions and future business decisions. These matters are inherently subject to significant business, economic and competitive uncertainties, all of which are difficult to predict and many of which are beyond Middlefield's control. Although Middlefield believes its estimates and assumptions are reasonable, actual results could vary materially from those shown. Inclusion of forward-looking information in this Form 10-Q does not constitute a representation by Middlefield or any other person that the indicated results will be achieved. Investors are cautioned not to place undue reliance on forward-looking information.

#### Comparison of Financial Condition at September 30, 2001 and December 31, 2000.

Total assets increased \$15.0 million to \$191.5 million at September 30, 2001 from \$176.5 million at December 31, 2000. This increase primarily resulted from an increase in net loans receivable of \$14.1 million that was funded by an \$13.9 million net increase in deposits.

Overall, total investment securities of \$28.5 million at September 30, 2001 remained relatively unchanged from \$29.8 million at December 31, 2000. Management's focus on supplementing loan demand primarily by lengthening the maturities of the investment portfolio through a net increase in higher yielding, mortgage-backed securities of \$6.8 million continues, although less aggressively, in the third quarter reflecting the Nation's general economic trends. This has resulted in a shift in the composition of the investment securities portfolio at September 30, 2001, as mortgage-backed securities now comprise 31.4% of the total portfolio as compared to 7.5% at December 31, 2000. Furthermore, available for sale securities now comprise 61.4% of the investment securities portfolio as compared to 41.3% at December 31, 2000.

Total loans increased to \$149,400,000 at September 30, 2001 from \$135,304,000 at December 31, 2000. The increase in net loans receivable resulted from the economic health of Middlefield's market area and the strategic, service-oriented marketing approach taken by management to meet the lending needs of the area.

## Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

The majority of lending activity is predominately mortgage loans secured by one-to-four family residential property. Such loans grew \$8.8 million to \$110.2 million at September 30, 2001. Management attributes the increases in residential real estate properties to continued customer referrals and Middlefield's overall relationship with its customers. Also impacted by the local economic conditions were commercial and commercial real estate loans which increased in total by \$4.5 million to \$30.8 million.

The allowance for loan losses represents the amount that management estimates is adequate to provide for probable losses inherent in the loan portfolio, as of the balance sheet date. Accordingly, all loan losses are charged to the allowance, and all recoveries are credited to it. At September 30, 2001, Middlefield's allowance for loan losses remained relatively unchanged at \$2.0 million. The allowance for loan losses is established through a provision for loan losses, which is charged to operations. The provision is based on management's periodic evaluation of the adequacy of the allowance for loan losses, taking into account the overall risk characteristics of the various portfolio segments, past experience with losses, the impact of economic conditions on borrowers, and other relevant factors. The estimates used to determine the adequacy of the allowance for loan losses, including the amounts and timing of future cash flows expected on impaired loans, are particularly susceptible to significant change in the near term. The total allowance for loan losses is a combination of a specific allowance for identified problem loans, a formula allowance, and an unallocated allowance.

Total deposits increased to \$161.0 million at September 30, 2001 from \$147.2 million at December 31, 2000. Growth was primarily concentrated in time and savings deposits and resulted from continual marketing efforts by management. Time deposits account for approximately 53.3% of the total deposit portfolio and continue to be a dominant resource for funds.

Total stockholders' equity increased \$1,396,000 to \$19.6 million at September 30, 2001 due to net income of \$1,689,000 and increases in accumulated other comprehensive income of \$171,000. These increases in stockholders' equity were offset by dividend payments of \$463,000. Accumulated other comprehensive income increased as a result of changes in the net unrealized gain on investment securities available for sale due to fluctuations in interest rates. Because of interest rate volatility, accumulated other comprehensive income could materially fluctuate for each interim period and year-end period depending on economic and interest rate conditions.

13

Comparison of Results of Operations for the Nine and Three Months Ended September 30, 2001 and 2000.

Net income for the nine months ended September 30, 2001 of \$1,689,000 increased from \$1,680,000 for the same period ended 2000. Basic and diluted earnings per share increased to \$1.53 per share in 2001 from \$1.52 per share in 2000. Net income for the three months ended September 30, 2001 of \$660,000 increased from \$571,000 for the same period ended 2000.

Net interest income for the nine months ended September 30, 2001 increased slightly to \$5,159,000, compared to \$5,151,000 for the same period ended 2000. While both interest income and interest expense increased for the period, interest income increased at a greater rate than interest expense. Interest income for the first nine months of 2001 was influenced mainly by increases in interest earned on loans receivable of \$783,000 and federal funds sold of

## Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

\$57,000, while offset by decreases in interest-bearing deposits in other institutions of \$30,000. The increases in interest income and expense were both primarily driven by increases in the average balances of related interest-earning assets and interest-bearing liabilities. The average balances of loans receivable increased \$14.1 million, or 11.2%, to \$141.0 million as of September 30, 2001, and resulted in an increase in interest-earning assets of \$15.8 million. Lessening the impact of the increase in volume of interest-earning assets was a slight decline on the tax-equivalent yield on interest earning assets to 7.91% for the nine months ended September 30, 2001 from 8.03% for the same period ended 2000. In addition, the average balance of time deposits increased \$13.6 million, or 19.9%, to \$81.8 million as of September 30, 2001, and resulted in an increase in interest-bearing liabilities of \$13.8 million. Middlefield's competitively priced deposit products and continual marketing efforts contributed to the overall increase in the cost of funds to 4.82% for the nine-month period ended September 30, 2001 from 4.50% for the same period ended 2000.

Net interest income for the three months ended September 30, 2001 also increased slightly to \$1,777,000 compared to \$1,725,000 for the same period ended 2000. This increase also consisted primarily of an increase in interest earned on loans receivable of \$236,000, that resulted from an increase in the average balances of the related interest-earning asset of \$15.3 million. Increases in interest expense of \$188,000 for the three-months ended September 30, 2001 resulted primarily from an increase on interest incurred on deposits. This fluctuation was the result of an increase in the average balance of time deposits of \$12.2 million coupled with an increase in the related cost of such funds of 6 basis points to 4.77% for 2001 from 4.71% for 2000. These competitively priced products were heavily marketed throughout Middlefield's market area.

Total non-interest income for both the nine-months and three-months ended September 30, 2001 increased \$201,000 and \$119,000, respectively, as compared to the same period ended 2000. Noninterest income items are primarily comprised of service charges and fees on deposit account activity, along with fee income derived from other financial related services. Service fees on deposit accounts increased \$95,000 and \$23,000, respectively, and have progressively increased as the number of accounts and volume of

14

related transactions have increased. Furthermore, Middlefield recognized an increase in gains on sales of investment securities of \$97,000 in the third quarter of 2001 as compared to the prior year quarter.

Total non-interest expenses increased \$263,000 and \$78,000 for the nine and three-months ended September 30, 2001, respectively, as compared to the same period ended 2000. Compensation and employee benefits increased \$60,000 and \$8,000, respectively, primarily as a result of normal merit raises. Additionally, occupancy and equipment expenses increased \$26,000 for the nine-months ended September 30, 2001, as compared to the same period ended 2000 as a result of added capital expenditures in prior years from building and furnishing a new branch office in Garrettsville, and additional ATMs. As a result of increased transaction activity from operating a larger organization, data processing expenses increased \$27,000 and \$14,000 for the nine and three month periods ended 2001 in comparison to the prior year periods. Other expenses increased \$140,000 and \$49,000 for the nine and three month periods ended 2001 as compared to 2000, because of the marketing of the 100th anniversary of the Bank, costs incurred with the addition of internet banking, and increased professional fees associated with outside assistance in complying with the increased levels of regulatory compliance of a publicly reported company.

LIQUIDITY

Liquidity management for Middlefield is measured and monitored on both a short and long-term basis, thereby allowing management to better understand and react to emerging balance sheet trends. After assessing actual and projected cash flow needs, management seeks to obtain funding at the most economical cost to Middlefield. Both short and long-term liquidity needs are addressed by maturities and sales of investment securities, loan payments and maturities, and liquidating money market investments such as federal funds sold. The use of these resources, in conjunction with access to credit, provide the core ingredients to meet depositor, borrower, and creditor needs.

Middlefield's liquid assets consist of cash and cash equivalents, which include investments in very short-term investments (i.e. federal funds sold), and investment securities classified as available for sale. The level of these assets is dependent on Middlefield's operating, investing, and financing activities during any given period. At September 30, 2001, cash and cash equivalents totaled \$6.3 million or 3.3% of total assets while investment securities classified as available for sale totaled \$17.5 million or 9.1% of total assets. Management believes that the liquidity needs of Middlefield are satisfied by the current balance of cash and cash equivalents, readily available access to traditional funding sources, FHLB advances, and the portion of the investment and loan portfolios that mature within one year. These sources of funds will enable Middlefield to meet cash obligations and off-balance sheet commitments as they come due.

Operating activities provided net cash of \$1.9 million and \$2.0 million for the nine-month periods ended September 30, 2001 and 2000, respectively, and were generated principally from net income of \$1.7 million for both periods.

15

Investing activities consist primarily of loan originations and repayments, and investment purchases and maturities. These activities used \$13.5 million in funds during the first nine months of 2001, principally for the purchase of investment securities and the net origination of loans. For the same period ended 2000, investing activities used \$7.4 million in funds, principally from the net origination of loans. In 2000, these cash usages were offset somewhat by an increase in net investment repayments and maturities coupled with a decline in interest-bearing deposits in other institutions from maturities of certificates of deposits.

Financing activities consist of the solicitation and repayment of customer deposits, borrowings and repayments, treasury stock activity, and the payment of dividends. During the nine months ended September 30, 2001, net cash provided by financing activities totaled \$13.1 million, principally derived from an increase in deposit accounts in general, and time deposits specifically. During the same period ended 2000, net cash provided by financing activities was \$8.8 million, and consisted of an increase in deposit accounts that was offset by the net acquisition of treasury stock and the repayment of other borrowing.

Liquidity may be adversely affected by unexpected deposit outflows, excessive interest rates paid by competitors, and similar matters. Management monitors projected liquidity needs and determines the level desirable, based in part on the bank's commitment to make loans, as well as management's assessment of Middlefield's ability to generate funds. Middlefield anticipates it will have sufficient liquidity available to meet estimated short-term and long-term funding needs.

## Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

### CAPITAL RESOURCES

Middlefield is subject to federal regulations that impose certain minimum capital requirements. Management monitors both Middlefield's and the Bank's Total risk-based, Tier I risk-based and Tier I leverage capital ratios in order to assess compliance with regulatory guidelines. At September 30, 2001, both Middlefield and the Bank exceeded the Minimum risk-based and leverage capital ratio requirements. Middlefield's Total risk-based, Tier I risk-based and Tier I leverage ratios were 17.34%, 16.09%, 10.28%, and the bank's were 16.72%, 15.46%, 9.96%, respectively, at September 30, 2001.

### RISK ELEMENT

The table below presents information concerning nonperforming assets including nonaccrual loans, renegotiated loans, loans 90 days or more past due, other real estate loans, and repossessed assets. A loan is classified as nonaccrual when, in the opinion of management, there are serious doubts about collectibility of interest and principal. At the time the accrual of interest is discontinued, future income is recognized only when cash is received. Renegotiated loans are those loans which terms have been renegotiated to provide a reduction or deferral of principal or interest as a result of the deterioration of the borrower.

16

	September 30, 2001	December 31, 2000
	-----	-----
	(Dollars in thousands)	
Loans on nonaccrual basis	\$ --	\$ --
Loans past due 90 days or more and still accruing	254	\$ 5
	-----	-----
Total nonperforming loans	\$ 254	\$ 5
	-----	-----
Nonperforming loans as a percent of total loans	0.17%	-%
	=====	=====
Nonperforming assets as a percent of total assets	0.13%	-%
	=====	=====

At September 30, 2001 and December 31, 2000, no real estate or other assets were held as foreclosed or repossessed property.

Management monitors impaired loans on a continual basis. As of September 30, 2001, impaired loans had no material effect on the Company's financial position or results of operations.

During the nine-month period ended September 30, 2001, loans increased \$14.1 million while nonperforming loans increase to a total of \$254,000. The allowance for loan losses increased slightly by \$11,000 during this same period and resulted in the percentage of allowance for loan losses to loans outstanding to decline to 1.37% as compared to 1.51% at December 31, 2000. Nonperforming loans are primarily made up of residential and commercial mortgages. The collateral requirements on such loans reduce the risk of potential losses to an acceptable level in management's opinion.

The allowance for loan losses represents the amount that management estimates is adequate to provide for probable losses inherent in the loan portfolio, as of the balance sheet date. The relationship between the allowance for loan losses and outstanding loans is a function of the credit quality and known risk attributed to the loan portfolio. The on-going loan review program and credit approval process is used to determine the adequacy of the allowance for loan losses.

17

#### QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Like other financial institutions, the bank is subject to interest rate risk. The bank's interest-earning assets could mature or reprice more rapidly than or on a different basis from its interest-bearing liabilities (primarily borrowings and deposits with short- and medium-term maturities) in a period of declining interest rates. Although having assets that mature or reprice more frequently on average than liabilities will be beneficial in times of rising interest rates, that asset/liability structure will result in lower net interest income in periods of declining interest rates.

Interest rate sensitivity, or interest rate risk, relates to the effect of changing interest rates on net interest income. Interest-earning assets with interest rates tied to the prime rate for example, or that mature in relatively short periods of time, are considered interest-rate sensitive. Interest-bearing liabilities with interest rates that can be repriced in a discretionary manner, or that mature in relatively short periods of time, are also considered interest-rate sensitive. The differences between interest-sensitive assets and interest-sensitive liabilities over various time horizons are commonly referred to as sensitivity gaps. As interest rates change, a sensitivity gap will have either a favorable effect or an adverse effect on net interest income. A negative gap -- with liabilities repricing more rapidly than assets -- generally should have a favorable effect when interest rates are falling, and an adverse effect when rates are rising. A positive gap -- with assets repricing more rapidly than liabilities -- generally should have the opposite effect: an adverse effect when rates are falling and a favorable effect when rates are rising.

Middlefield and the bank have no financial instruments entered into for trading purposes. Interest rates change daily on federal funds purchased and sold. Federal funds are therefore the most sensitive to the market and have the most stable fair values. Loans and deposits tied to indices such as the prime rate or federal discount rate are also market sensitive, with stable fair values. The least sensitive instruments include long-term, fixed-rate loans and securities and fixed-rate savings deposits, which have the least stable fair value. Management of maturity distributions of assets and liabilities between these extremes is as important as the balances maintained. Management of maturity distributions involves matching interest rate maturities as well as principal maturities, and it influences net interest income significantly. In periods of rapidly changing interest rates, a negative or positive gap can cause major fluctuations in net interest income and earnings. Managing asset and liability sensitivities to enhance growth regardless of changes in market conditions is one of the objectives of the bank's asset/liability management strategy.

Evaluating the bank's exposure to changes in interest rates is the responsibility of the Asset/Liability Committee, a committee of bank directors and officers. The Asset/Liability Committee assesses both the adequacy of the management process used to control interest rate risk and the quantitative level



## Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

of exposure, ensuring that appropriate policies, procedures, management information systems and internal controls are in place to maintain interest rate risk at appropriate levels. Evaluating the quantitative level of

18

interest rate risk exposure requires assessment of existing and potential effects of changes in interest rates on the bank's financial condition, including capital adequacy, earnings, liquidity and asset quality.

The bank uses an asset/liability model to support its balance sheet strategies. Gap analysis, one of the methods used by management to analyze interest rate risk, does not necessarily show the precise impact of specific interest rate movements on Middlefield's net interest income because the re-pricing of certain assets and liabilities is discretionary and is subject to competitive and other pressures. In addition, assets and liabilities within the same period may, in fact, be repaid at different times and at different rate levels. Middlefield has not experienced the kind of earnings volatility that might be indicated from gap analysis.

Middlefield's use of a simulation model to better measure the impact of interest rate changes on net interest income is incorporated into the risk management process to effectively identify, measure, and monitor Middlefield's risk exposure. Interest rate simulations using a variety of assumptions are employed by Middlefield to evaluate its interest rate risk exposure. A shock analysis at September 30, 2001 indicated that a 200 basis point movement in interest rates in either direction would have had a minor impact on Middlefield's anticipated net interest income and the market value of assets and liabilities over the next 12 months, well within Middlefield's ability to manage effectively.

19

### PART II - OTHER INFORMATION

Item 1. Legal Proceedings

None

Item 2. Changes in rights of the Company's security holders

None

Item 3. Defaults by the Company on its senior securities

None

Item 4. Submission of matters to a vote of security holders

None

Item 5. Other information

None

## Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

### Item 6. Exhibits and Reports on Form 8-K

- (a) The following exhibits are included in this Report or incorporated herein by reference:
- 3.1 Second Amended and Restated Articles of Incorporation of Middlefield Banc Corp. \*
  - 3.2 Regulations of Middlefield Banc Corp. \*
  - 4 Specimen Stock Certificate \*
  - 10.1 1999 Stock Option Plan of Middlefield Banc Corp. \*
  - 10.2 Severance Agreement of President and Chief Executive Officer \*
  - 10.3 Severance Agreement of Executive Vice President \*
  - 10.4 Federal Home Loan Bank of Cincinnati Agreement for Advances and Security Agreement dated September 14, 2000 \*
  - 10.5 Collateral Assignment Split Dollar Agreement between the President and Chief Executive Officer and The Middlefield Banking Company \*
  - 21 Subsidiaries of Middlefield Banc Corp. \*
  - 99.1 Form of Indemnification Agreement with directors of Middlefield Banc Corp. and executive officers of Middlefield Banc Corp. and The Middlefield Banking Company \*
  - 99.2 Independent Accountants Report

20

\* Incorporated by reference to the identically numbered exhibit to the registration statement on Form 10 (File No. 033-23094) filed on April 17, 2001 and subsequently amended on June 14, 2001.

- (b) No reports on Form 8-K were filed by Middlefield Banc Corp. during the quarter ended September 30, 2001.

21

### SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned and hereunto duly authorized.

MIDDLEFIELD BANC CORP.

Edgar Filing: MIDDLEFIELD BANC CORP - Form 10-Q/A

Date: November 13, 2001

By: /s/Thomas G. Caldwell

-----  
Thomas G. Caldwell  
President and Chief Executive Officer

Date: November 13, 2001

By: /s/Donald L. Stacy

-----  
Donald L. Stacy  
Principal Financial and Accounting  
Officer