

SURREY BANCORP
Form 10-K
March 26, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20429

Form 10-K

(MARK ONE)

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

For the fiscal year ended December 31, 2009

TRANSITION REPORT UNDER SECTION 13 OR 15(b) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 0000-50313

SURREY BANCORP

(Exact Name of Registrant as Specified in Its Charter)

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NORTH CAROLINA
(State or Other Jurisdiction of

59-3772016
(IRS Employer

incorporation or organization)

Identification No.)

145 North Renfro Street (P.O. Box 1227); Mount Airy, NC 27030

(Address of principal executive office)

(336) 783-3900

(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, NO PAR VALUE

(Title of Class)

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

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

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

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

The aggregate market value of the voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second quarter was \$17.5 million.

3,206,495 shares of the Registrant's common stock were issued and outstanding as of March 12, 2010.

DOCUMENTS INCORPORATED BY REFERENCE

The annual report to security holders for fiscal year ended December 31, 2009, is incorporated by reference into Form 10-K Part II, Items 6, 7 and 8, and Part IV, Item 15. The registrant's Proxy Statement dated March 31, 2010, is incorporated by reference into Form 10-K Part III, Items 10, 11, 12, 13 and 14.

PART I

ITEM 1. BUSINESS

General

Surrey Bancorp (the Company) began operations on May 1, 2003 and was created for the purpose of acquiring all the outstanding shares of common stock of Surrey Bank & Trust. The Company is subject to regulation by the Federal Reserve.

Surrey Bank & Trust (the Bank) was incorporated on July 15, 1996 as a North Carolina banking corporation and opened for business on July 22, 1996. As such, the Bank operates under the laws of the State of North Carolina. As a state chartered, nonmember bank, the Bank is subject to regulation, supervision and regular examination by the North Carolina Banking Commission (the Commission) through the North Carolina Commissioner of Banks (the Commissioner) and its applicable federal regulator is the Federal Deposit Insurance Corporation (the FDIC). The North Carolina Banking Commission and the FDIC have the power to enforce compliance with applicable banking statutes and regulations.

The principal business of the Company is to provide comprehensive individual and corporate financial services through its main and branch offices in Mount Airy, North Carolina and branch offices in Stuart, Virginia and Pilot Mountain, North Carolina. These services include demand and time deposits as well as commercial, installment, mortgage and other consumer lending services, insurance and investment services.

Competitive Conditions

The principal areas and methods of competition in the banking industry are the services that are offered, the pricing of those services, the convenience and availability of the services and the degree of expertise and personal manner with which those services are offered. The Company encounters strong competition from other commercial banks, including the largest North Carolina banks, operating in Mount Airy, North Carolina, and the surrounding area. In the conduct of certain aspects of its business, the Bank also competes with credit unions, insurance companies, money market mutual funds, and other non-bank financial institutions, some of which are not subject to the same degree of regulation as the Company. Many of these competitors have substantially greater resources and lending abilities than the Company and offer certain services, such as investment banking, trust, interstate and international banking services, that the Company does not provide.

Material Customers

Deposits are derived from a broad base of customers in the Company's trade area. No material portion of deposits have been obtained from a single person or a few persons (including Federal, State, and local governments and agencies thereunder), the loss of which would have a materially adverse effect on the business of the Company.

The majority of loans and commitments to extend credit have been granted to customers in the Company's market area. The majority of such customers are depositors. The Company generally does not extend credit to any single borrower or group of related borrowers in excess of approximately \$4,600,000. Although the Company has a reasonably diversified portfolio, it has loan concentrations relating to customers who are in the following industries: residential real estate, real estate leasing and development, motion picture and sound recording industries, trucking, metal building fabrication and assembly, highway and bridge construction, furniture manufacturing and building contractors. Total loans and loan commitments to these industry groups at December 31, 2009 and 2008 are summarized in the table below:

| Industry | Loans and Commitments December 31, | |
|---|---------------------------------------|---------------|
| | 2009 | 2008 |
| Real Estate | \$ 15,346,000 | \$ 16,446,000 |
| Motion Picture and Sound Recording Industries | 9,661,000 | 3,806,000 |
| Truck Transportation | 9,032,000 | 6,253,000 |

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| | | |
|--|-----------|-----------|
| Fabricated Metal Products Manufacturing | 8,876,000 | 9,118,000 |
| Heavy and Civil Engineering Construction | 8,034,000 | 8,346,000 |
| Construction of Buildings | 6,947,000 | 6,562,000 |
| Amusement, Gambling, and Recreation Industries | 6,378,000 | |
| Wood Product Manufacturing | 5,113,000 | 5,027,000 |
| Motor Vehicle and Parts Dealers | 4,926,000 | 3,800,000 |
| Food Service and Drinking Places | 4,822,000 | 4,427,000 |
| Educational Services | 4,760,000 | 4,908,000 |
| Repair and Maintenance Industries | 4,372,000 | 5,181,000 |
| Nonmetallic Mineral Product Manufacturing | 3,922,000 | 3,372,000 |
| Religious, Civic and Similar Organizations | 3,412,000 | 2,804,000 |
| Crop Production | 2,917,000 | 2,903,000 |
| Specialty Trade Contractors | 2,663,000 | 2,779,000 |
| Nursing and Residential Care Facilities | 2,550,000 | |
| Furniture and Related Product Manufacturing | 2,512,000 | 2,705,000 |

Rights

No patents, trademarks, licenses, franchises or concessions held are of material significance to the Company.

New Services

No new services were added to the Company's operations in 2009.

Supervision and Regulation

Banking is a complex, highly regulated industry. The primary goals of banking regulations are to maintain a safe and sound banking system and to facilitate the conduct of sound monetary policy. In furtherance of these goals, Congress and the North Carolina General Assembly have created largely autonomous regulatory agencies and enacted numerous laws that govern banks, their holding companies and the banking industry. The descriptions of and references to the statutes and regulations below are brief summaries and do not purport to be complete. The descriptions are qualified in their entirety by reference to the specific statutes and regulations discussed.

As a North Carolina bank, Surrey Bank & Trust is subject to regulation, supervision and regular examination by the Commissioner and the FDIC. The Commissioner and the FDIC have the power to enforce compliance with applicable banking statutes and regulations.

Federal Regulation

As a bank holding company, Surrey Bancorp is subject to regulation, supervision and regular examinations by the Federal Reserve. The Bank Holding Company Act provides that a bank holding company must obtain the prior approval of the Federal Reserve for the acquisition of more than five percent of the voting stock or substantially all the assets of any bank or bank holding company. In addition, the Bank Holding Company Act restricts the extension of credit to any bank holding company by its subsidiary bank. The Bank Holding Company Act also provides that, with certain exceptions, a bank holding company may not engage in any activities other than those of banking or managing or controlling banks and other authorized subsidiaries or own or control more than five percent of the voting shares of any company that is not a bank. The Federal Reserve has deemed limited activities to be closely related to banking and therefore permissible for a bank holding company.

As a North Carolina bank, Surrey Bank & Trust is subject to regulation, supervision and regular examination by the FDIC. The FDIC is required to conduct regular on-site examinations of the operations of the Bank and enforces federal laws that set specific requirements for bank capital, the payment of dividends, loans to officers and directors, and types and amounts of loans and investments made by commercial banks. Among other things, the FDIC must approve the establishment of branch offices, conversions, mergers, assumption of deposit liabilities between insured banks and uninsured banks or institutions, and the acquisition or establishment of certain subsidiary corporations.

The FDIC can also prevent capital or surplus diminution in transactions where the deposit accounts of the resulting, continuing or assumed bank are insured by the FDIC.

Transactions with Affiliates. A bank may not engage in specified transactions (including, for example, loans) with its affiliates unless the terms and conditions of those transactions are 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 entities. In the absence of comparable transactions, any transaction between a bank and its affiliates must be on terms and under circumstances, including credit standards, which in good faith would be offered or would apply to nonaffiliated companies. In addition, transactions referred to as covered transactions between a bank and its affiliates may not exceed 10% of the bank's capital and surplus per affiliate and an aggregate of 20% of its capital and surplus for covered transactions with all affiliates. Certain transactions with affiliates, such as loans, also must be secured by collateral of specific types and amounts. The Bank also is prohibited from purchasing low quality assets from an affiliate. Every company under common control with the Bank is deemed to be an affiliate of the Bank.

Loans to Insiders. Federal law also constrains the types and amounts of loans that the Bank may make to its executive officers, directors and principal shareholders. Among other things, these loans are limited in amount, must be approved by the Bank's board of directors in advance, and must be on terms and conditions as favorable to the Bank as those available to an unrelated person.

Regulation of Lending Activities. Loans made by the Bank are also subject to numerous federal and state laws and regulations, including the Truth-In-Lending Act, Federal Consumer Credit Protection Act, the Equal Credit Opportunity Act, the Real Estate Settlement Procedures Act and adjustable rate mortgage disclosure requirements. Remedies to the borrower or consumer and penalties to the Bank are provided if the Bank fails to comply with these laws and regulations. The scope and requirements of these laws and regulations have expanded significantly in recent years.

Branch Banking. All banks located in North Carolina are authorized to branch statewide. Accordingly, a bank located anywhere in North Carolina has the ability, subject to regulatory approval, to establish branch facilities near any of our facilities and within our market area. If other banks were to establish branch facilities near our facilities, it is uncertain whether these branch facilities would have a material adverse effect on our business. Federal law provides for nationwide interstate banking and branching, subject to certain aging and deposit concentration limits that may be imposed under applicable state laws. Applicable North Carolina statutes permit regulatory authorities to approve de novo branching in North Carolina by institutions located in states that would permit North Carolina institutions to branch on a de novo basis into those states. Federal regulations prohibit an out-of-state bank from using interstate branching authority primarily for the purpose of deposit production. These regulations include guidelines to insure that interstate branches operated by an out-of-state bank in a host state are reasonably helping to meet the credit needs of the host state communities served by the out-of-state bank.

Reserve Requirements. Pursuant to regulations of the Federal Reserve, the Bank must maintain average daily reserves against its transaction accounts. During 2009, no reserves were required to be maintained on the first \$10.3 million of transaction accounts, but reserves equal to 3.0% were required to be maintained on the aggregate balances of those accounts between \$10.3 million and \$44.4 million, and additional reserves were required to be maintained on aggregate balances in excess of \$44.4 million in an amount equal to 10.0% of the excess. These percentages are subject to annual adjustment by the Federal Reserve, which has advised that for 2010, no reserves will be required to be maintained on the first \$10.7 million of transaction accounts, but reserves equal to 3.0% must be maintained on the aggregate balances of those accounts between \$10.7 million and \$55.2 million, and additional reserves are required on aggregate balances in excess of \$55.2 million in an amount equal to 10.0% of the excess. Because required reserves must be maintained in the form of vault cash or in an account at a Federal Reserve Bank bearing nominal interest, the effect of the reserve requirement is to reduce the amount of the institution's interest-earning assets and interest income. As of December 31, 2009, the Bank met its reserve requirements.

Community Reinvestment. Under the Community Reinvestment Act (CRA), as implemented by regulations of the federal bank regulatory agencies, an insured bank has a continuing and affirmative obligation, consistent with its safe and sound operation, to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs for banks, nor does it limit a bank's discretion to develop the types of products and services that it believes are best suited to its particular

community, consistent with the CRA. The CRA requires the federal bank regulatory agencies, in connection with their examination of insured banks, to assess the banks' records of meeting the credit needs of their communities, using the ratings of outstanding, satisfactory, needs to improve, or substantial noncompliance, and to take that record into account in its evaluation of certain applications by those banks. All banks are required to make public disclosure of their CRA performance ratings. The Bank received a satisfactory rating in its most recent CRA examination.

Governmental Monetary Policies. The commercial banking business is affected not only by general economic conditions but also by the monetary policies of the Federal Reserve, a federal banking regulatory agency that regulates the money supply in order to mitigate recessionary and inflationary pressures. Among the techniques used to implement these objectives are open market transactions in United States government securities, changes in the rate paid by banks on bank borrowings, and changes in reserve requirements against bank deposits. These techniques are used in varying combinations to influence overall growth and distribution of bank loans, investments, and deposits, and their use may also affect interest rates charged on loans or paid for deposits. The monetary policies of the Federal Reserve have had a significant effect on the operating results of commercial banks in the past and are expected to continue to do so in the future. In view of changing conditions in the national economy and money markets, as well as the effect of actions by monetary and fiscal authorities, no prediction can be made as to possible future changes in interest rates, deposit levels, loan demand or the business and earnings of the Bank.

Dividends. Under federal banking law, no cash dividend may be paid if a bank is undercapitalized or insolvent or if payment of the cash dividend would render the bank undercapitalized or insolvent and no cash dividend may be paid by a bank if it is in default of any deposit insurance assessment due to the FDIC.

Deposit Insurance Assessments. Effective through December 31, 2013, the Bank's deposits are insured up to \$250,000 per insured non-IRA and IRA account by the Deposit Insurance Fund of the Federal Deposit Insurance Corporation. On January 1, 2014, the standard coverage limit will return to \$100,000 for all deposit categories except IRAs and certain retirement accounts, which will continue to be insured up to \$250,000 per owner. Unlimited deposit insurance coverage is available through June 30, 2010, for non-interest bearing transaction accounts at institutions participating in the FDIC's Temporary Liquidity Guarantee Program. The bank is required to pay deposit insurance assessments set by the FDIC. The FDIC determines the Bank's deposit insurance assessment rates on the basis of four risk categories. During 2009, the Bank's assessment was determined by a formula that ranged from 0.12% to 0.16% at the lowest assessment category up to a maximum assessment of 0.45% of the Bank's average deposit base, with the exact assessment determined by the Bank's assets, its capital and the FDIC's supervisory opinion of its operations. The insurance assessment rate may change periodically and for 2010, the formula will range from 0.12% to 0.24% at the lowest assessment category up to a maximum assessment of 0.775% on a bank's average deposit base. In an effort to encourage banks to limit the FDIC's exposure, the 2010 insurance assessment rate formula will also:

Reduce the assessment rate paid by a bank by up to 0.05% based on the amount of unsecured debt held by the institution;

Increase a bank's assessment by up to 0.225% based on its risk profile if the bank has high levels of secured liabilities, since those claims must be paid before depositors can make claims in the event of a failure; and

Increase a bank's assessment if it is already considered risky and brokered deposits make up more than 10% of the institution's domestic deposits.

The assessment rates, including the special assessment, are subject to change at the discretion of the Board of Directors of the FDIC.

Increases in the assessment rate may have an adverse effect on the Bank's operating results. The FDIC has the authority to terminate deposit insurance.

Changes in Management. Any depository institution that has been chartered less than two years, is not in compliance with the minimum capital requirements of its primary federal banking regulator, or is otherwise in a troubled condition must notify its primary federal banking regulator of the proposed addition of any person to the

board of directors or the employment of any person as a senior executive officer of the institution at least 30 days before such addition or employment becomes effective. During this 30-day period, the applicable federal banking regulatory agency may disapprove of the addition of such director or employment of such officer. The Bank is not subject to any such requirements.

Enforcement Authority. The federal banking laws also contain civil and criminal penalties available for use by the appropriate regulatory agency against certain institution-affiliated parties including management, employees and agents of a financial institution, as well as independent contractors such as attorneys and accountants and others who participate in the conduct of the financial institution's affairs and who caused or are likely to cause more than minimum financial loss to or a significant adverse affect on the institution, who knowingly or recklessly violate a law or regulation, breach a fiduciary duty or engage in unsafe or unsound practices. These practices can include the failure of an institution to timely file required reports or the submission of inaccurate reports. These laws authorize the appropriate banking agency to issue cease and desist orders that may, among other things, require affirmative action to correct any harm resulting from a violation or practice, including restitution, reimbursement, indemnification or guarantees against loss. A financial institution may also be ordered to restrict its growth, dispose of certain assets or take other action as determined by the primary federal banking agency to be appropriate.

Capital Adequacy. The Bank is subject to capital requirements and limits on activities established by the FDIC. Under the capital regulations, the Bank generally is required to maintain Tier 1 risk-based capital, as such term is defined therein, of 4% and total risk-based capital, as such term is defined therein, of 8%. In addition, the Bank is required to provide a minimum leverage ratio of Tier 1 capital to adjusted average quarterly assets (leverage ratio) equal to 3%, plus an additional cushion of 1% to 2% if the Bank has less than the highest regulatory rating. The Bank is not permitted to engage in any activity not permitted for a national bank unless (i) it is in compliance with its capital requirements and (ii) the FDIC determines that the activity would not pose a risk to the deposit insurance fund. With certain exceptions, the Bank also is not permitted to acquire equity investments of a type, or in an amount, not permitted for a national bank.

Prompt Corrective Action. Banks are subject to restrictions on their activities depending on their level of capital. Federal prompt corrective action regulations divide banks into five different categories, depending on their level of capital. Under these regulations, a bank is deemed to be well capitalized if it has a total risk-based capital ratio of 10% or more, a core capital ratio of 6% or more and a leverage ratio of 5% or more, and if the bank is not subject to an order or capital directive to meet and maintain a certain capital level. Under these regulations, a bank is deemed to be adequately capitalized if it has a total risk-based capital ratio of 8% or more, a core capital ratio of 4% or more and a leverage ratio of 4% or more (unless it receives the highest composite rating at its most recent examination and is not experiencing or anticipating significant growth, in which instance it must maintain a leverage ratio of 3% or more). Under these regulations, a bank is deemed to be undercapitalized if it has a total risk-based capital ratio of less than 8%, a core capital ratio of less than 4% or a leverage ratio of less than 3%. Under these regulations, a bank is deemed to be significantly undercapitalized if it has a risk-based capital ratio of less than 6%, a core capital ratio of less than 3% and a leverage ratio of less than 3%. Under such regulations, a bank is deemed to be critically undercapitalized if it has a leverage ratio of less than or equal to 2%. In addition, the applicable federal banking agency has the ability to downgrade a bank's classification (but not to critically undercapitalized) based on other considerations even if the bank meets the capital guidelines.

If a bank is classified as undercapitalized, the bank is required to submit a capital restoration plan to the FDIC and the FDIC may also take certain actions to correct the capital position of the bank. An undercapitalized bank is prohibited from increasing its assets, engaging in a new line of business, acquiring any interest in any company or insured depository institution, or opening or acquiring a new branch office, except under certain circumstances, including the acceptance by the FDIC of a capital restoration plan for the bank.

If a state bank is classified as significantly undercapitalized, the FDIC would be required to take one or more prompt corrective actions. These actions would include, among other things, requiring sales of new securities to bolster capital, changes in management, limits on interest rates paid, prohibitions on transactions with affiliates, termination of certain risky activities and restrictions on compensation paid to executive officers. If a bank is classified as critically undercapitalized, the bank must be placed into conservatorship or receivership within 90 days, unless the FDIC determines otherwise.

The capital classification of a bank affects the frequency of regulatory examinations of the bank and impacts the ability of the bank to engage in certain activities and affects the deposit insurance premiums paid by the bank. The FDIC is required to conduct a full-scope, on-site examination of every bank on a periodic basis.

Banks also may be restricted in their ability to accept brokered deposits, depending on their capital classification. Well capitalized banks are permitted to accept brokered deposits, but all banks that are not well capitalized are not permitted to accept such deposits. The FDIC may, on a case-by-case basis, permit banks that are adequately capitalized to accept brokered deposits if the FDIC determines that acceptance of such deposits would not constitute an unsafe or unsound banking practice with respect to the bank.

Treasury Regulations. In June 2009, the United States Treasury Department adopted new rules to implement the requirements of the American Recovery and Reinvestment Act of 2009 which add a number of obligations to institutions that hold investments under the Capital Purchase Program, such as the Company, that are in addition to those agreed to by the Company at the time of the Treasury investment. Among other things, these rules: require that the Compensation Committee of the Board meet at least every six months and undertake various reviews of the risks presented to the Company by its compensation practices; increase the number of employees subject to clawback of incentive compensation in the event of inaccurate financial statements by the Company; prohibit the Company from paying any severance compensation to certain executives even where the Company has a contractual obligation to make those payments; limits the amount of incentive compensation payments to certain executives and only permits those payments in the form of restricted stock or units; requires the Company to permit a non-binding shareholder vote on the Company's executive compensation; requires the Company to adopt an excessive or luxury expenditures policy; prohibits the Company from paying any tax gross-ups on compensation for certain executives; and requires the Company to identify a number of its most highly compensated employees.

State Regulation

As a North Carolina-chartered bank, the Bank is also subject to extensive supervision and regulation by the Commissioner. The Commissioner enforces state laws that set specific requirements for bank capital, the payment of dividends, loans to officers and directors, record keeping, and types and amounts of loans and investments made by commercial banks. Among other things, the approval of the Commissioner is generally required before a North Carolina-chartered commercial bank may establish branch offices. North Carolina banking law requires that any merger, liquidation or sale of substantially all of the assets of the Bank must be approved by the Commissioner and the holders of two thirds of the Bank's outstanding common stock.

Change of control. North Carolina banking laws provide that no person may directly or indirectly purchase or acquire voting stock of the Bank that would result in the change in control of the Bank unless the Commissioner has approved the acquisition. A person will be deemed to have acquired control of the Bank if that person directly or indirectly (i) owns, controls or has power to vote 10% or more of the voting stock of the Bank, or (ii) otherwise possesses the power to direct or cause the direction of the management and policy of the Bank.

Loans. In its lending activities, the Bank is subject to North Carolina usury laws which generally limit or restrict the rates of interest, fees and charges and other terms and conditions in connection with various types of loans. North Carolina banking law also limits the amount that may be loaned to any one borrower.

Dividends. The ability of the Bank to pay dividends is restricted under applicable law and regulations. Under North Carolina banking law, dividends must be paid out of retained earnings and no cash dividends may be paid if payment of the dividend would cause the bank's surplus to be less than 50% of its paid-in capital.

Holding companies. North Carolina banking law requires that bank holding companies register with the Commissioner. The Commissioner must also approve any acquisition of control of a state-chartered bank by a bank holding company.

Future Legislation and Regulations

The Company cannot predict what new legislation might be enacted or what regulations might be adopted or amended, or if enacted, adopted or amended, their effect on its operations. Any change in applicable law or regulation, state or federal, may have a material adverse effect on its business.

Environmental Laws

Compliance with federal, state, or local provisions regulating the discharge of materials into the environment has not had, nor is it expected to have in the future, a material effect upon the Bank's capital expenditures, earnings or competitive position.

Employees

All employees of the Company are compensated by the Company's subsidiary, the Bank. The Bank had nine (9) officers, fifty-eight (58) full-time employees (including the officers), and thirteen (13) part-time employees as of December 31, 2009.

ITEM 1A. RISK FACTORS

Not Applicable as a Smaller Reporting Company.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Company's permanent headquarters is a two-story brick building, with approximately 8,500 square feet of space located at 145 North Renfro Street, Mount Airy, North Carolina, which is also the headquarters of the Bank. The building has drive-up facilities. The Bank's finance, operations, mortgage lending and insurance departments are housed in a one-story brick building with approximately 7,500 square feet of space located at 199 North Renfro Street in Mount Airy, North Carolina.

The Company has a modular training facility located at 143 North Renfro Street, Mount Airy, North Carolina. The modular unit with approximately 1,600 square feet of floor space was moved from Stuart Virginia in early 2009. The unit previously served as the temporary branch office in Stuart.

The Bank owns a one-story brick building at 165 North Renfro Street that serves as the offices for its sales finance subsidiary, Freedom Finance, LLC. The building has approximately 1,600 square feet of floor space.

The Bank has two branch locations in Mount Airy, North Carolina. The 1280 West Pine Street branch is a two-story brick building with approximately 4,500 square feet of floor space. The branch also has drive up facilities and is leased under a five-year agreement, which extends through March of 2010. The 2050 Rockford Street branch is a one-story brick building with approximately 2,400 square feet of floor space with drive up facilities.

The Bank has a branch location in Stuart, Virginia located at 940 Woodland Drive. The branch is a one-story brick building with approximately 2,800 square feet of floor space. The building has drive up facilities.

The Bank has a branch location in Pilot Mountain, North Carolina at 653 South Key Street. The branch is a one-story brick building with approximately 2,800 square feet of floor space. The building has drive up facilities.

ITEM 3. LEGAL PROCEEDINGS

The Company is not party to, nor is any of its property the subject of, any material pending legal proceedings incidental to the business of the Company.

**ITEM 4. RESERVED
PART II**

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

The Company's common stock is traded in the over the counter market, and is listed in the National Daily Quotation Service Bulletin Board under the symbol SRYB. The following table shows the high and low prices for each quarter of the fiscal years, and reflects inter-dealer prices, without retail mark-up, mark-down or commissions and may not represent actual transactions:

| | 2009 Price Per Share | | 2008 Price Per Share | |
|----------------|----------------------|---------|----------------------|---------|
| | High | Low | High | Low |
| First Quarter | \$ 10.05 | \$ 4.85 | \$ 11.90 | \$ 9.50 |
| Second Quarter | \$ 9.45 | \$ 7.25 | \$ 11.40 | \$ 9.70 |
| Third Quarter | \$ 9.48 | \$ 7.80 | \$ 10.00 | \$ 8.40 |
| Fourth Quarter | \$ 8.50 | \$ 7.60 | \$ 10.05 | \$ 7.35 |

The last sales price of the common stock on March 12, 2010 was \$7.05. The approximate number of holders of the Company's 3,198,105 shares of Common Stock as of December 31, 2009 is 1,600. There are 189,356 shares of the Company's Series A Preferred Stock issued and outstanding as of December 31, 2009. The preferred stock is non-cumulative and each share is convertible into 2.0868 shares of common stock. The preferred stock carries a dividend rate of 4.5% and has a liquidation value of \$14.00 per share. The preferred stock was issued under a private placement in the second quarter of 2003.

On January 9, 2009, the Company issued and sold to the US Department of the Treasury (i) 2,000 shares of the Company's Fixed Rate Cumulative Perpetual Preferred Stock, Series B, with a liquidation preference of \$1,000 per share (the Series B Preferred Stock) and (ii) a warrant to purchase 100.001 shares of the Company's Fixed Rate Cumulative Perpetual Preferred Stock, Series C, with a liquidation preference of \$1,000 per share (the Series C Preferred Stock), at an initial exercise price of \$0.01 per share (the Warrant). The Warrant was immediately exercisable. The Series B Preferred Stock pays cumulative dividends at a rate of 5% per annum for the first five years, and 9% per annum thereafter.

The Company may redeem the Series B Preferred Stock at par after February 15, 2012. Prior to this date, the Company may redeem the Series B Preferred Stock at par only if (i) the Company has raised aggregate gross proceeds in one or more qualified equity offerings in excess of approximately \$500,000, and (ii) the aggregate redemption price does not exceed the aggregate net proceeds from such qualified equity offerings. Any redemption of the Series B Preferred Stock is subject to the consent of the Board of Governors of the Federal Reserve System.

Immediately following the issuance of the Series B Preferred Stock and the Warrant, Treasury exercised its rights under the Warrant in a net cashless transaction and received 100 shares of Series C Preferred Stock, with an aggregate liquidation preference of \$100,000. The Series C Preferred Stock pays cumulative dividends at a rate of 9% per annum. The Series C Preferred Stock has no maturity date and ranks senior to the Company's common stock with respect to the payment of dividends and distributions and amounts payable upon liquidation, dissolution and winding up of the Company. The Series C Preferred Stock is generally non-voting. The Company may redeem the Series C Preferred Stock at par after February 15, 2012, provided that all of the outstanding shares of Series B Preferred Stock shall previously have been redeemed. Prior to this date, the Company may redeem the Series C Preferred Stock at par only if all the outstanding shares of Series B Preferred Stock have previously been redeemed and (i) the Company has raised aggregate gross proceeds in one or more qualified equity offerings in excess of approximately \$25,000 and (ii) the aggregate redemption price does not exceed the aggregate net proceeds from

such qualified equity offerings. Any redemption of the Series C Preferred Stock is subject to the consent of the Board of Governors of the Federal Reserve System.

Each holder of Common Stock is entitled to dividends paid by the Company when and if declared by the Board of Directors from funds legally available. The determination and declaration of dividends is within the discretion of the Board of Directors subject to legal conditions. As a bank holding company that does not, as an entity, currently engage in separate business activities of a material nature, the ability to pay cash dividends depends upon the cash dividends received from the subsidiary bank (Surrey Bank & Trust). The Company's only source of income is dividends paid by the Bank and interest income from excess funds invested in time deposits with the Bank. The Company must pay all of our operating expenses from funds that are received from the Bank. North Carolina banking requires that dividends from a bank be paid out of the Bank's retained earnings and prohibits the payment of cash dividends if payment of the dividend would cause the Bank's surplus to be less than 50% of its paid-in capital. Also, under federal banking law, no cash dividend may be paid if the Bank is undercapitalized or insolvent or if payment of the cash dividend would render the Bank undercapitalized or insolvent, and no cash dividend may be paid by the Bank if it is in default of any deposit insurance assessment due to the FDIC. Therefore, shareholders may receive dividends from the Company only to the extent that funds are available from the Bank. In addition, the Federal Reserve generally prohibits bank holding companies from paying dividends except out of operating earnings, and the prospective rate of earnings retention appears consistent with the bank holding company's capital needs, asset quality and overall financial condition. As a condition of the sale of its preferred stock to Treasury, the Company must obtain Treasury's consent to pay a cash dividend on its common stock. Subject to these restrictions, the Board of Directors will consider the payment of dividends when it is deemed prudent to do so.

No cash dividends on the common stock of the Company were declared in 2009.

ITEM 6. SELECTED FINANCIAL DATA

Incorporated by reference from the registrant's annual report to security holders for the fiscal year ended December 31, 2009 attached as Exhibit 15 to this Form 10-K.

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

Incorporated by reference from the registrant's annual report to security holders for the fiscal year ended December 31, 2009 attached as Exhibit 15 to this Form 10-K.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not Applicable as a Smaller Reporting Company.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Incorporated by reference from the registrant's annual report to security holders for the fiscal year ended December 31, 2009 attached as Exhibit 15 to this Form 10-K.

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

None.

ITEM 9A. CONTROLS AND PROCEDURES

As of the end of the period covered by this Annual Report on Form 10-K, an evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the design and operation of these disclosure controls and procedures were effective.

Disclosure controls and procedures are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

The design of any system of controls is based in part upon certain assumptions about the likelihood of future events. There can be no assurance that any design will succeed in achieving its stated goal under every potential condition, regardless of how remote. In addition, the operation of any system of controls and procedures is dependent upon the employees responsible for executing it. While we have evaluated the operation of our disclosure controls and procedures and found them effective, there can be no assurance that they will succeed in every instance to achieve their objective.

Management's Annual Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as such term is defined in Rule 13a-15(f) under the Exchange Act). Our internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on the financial statements.

Because of the inherent limitations in any internal control, no matter how well designed, misstatements may occur and not be prevented or detected. Accordingly, even effective internal control over financial reporting can provide only reasonable assurance with respect to financial statement preparation. Further, the evaluation of the effectiveness of internal control over financial reporting was made as of a specific date, and continued effectiveness in future periods is subject to the risks that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies and procedures may decline.

Management conducted an evaluation of the effectiveness of our system of internal control over financial reporting as of December 31, 2009, based on the framework set forth in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on its evaluation, management concluded that, as of December 31, 2009, Surrey Bancorp's internal control over financial reporting was effective.

This annual report does not include an attestation report of the company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this annual report.

Changes in Internal Control over Financial Reporting

There were no changes in the Company's internal controls over financial reporting during the fourth fiscal quarter of the fiscal year covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS, AND CORPORATE GOVERNANCE

Incorporated by reference from the registrant's definitive proxy statement to be filed with the SEC by April 30, 2010.

ITEM 11. EXECUTIVE COMPENSATION

Incorporated by reference from the registrant's definitive proxy statement to be filed with the SEC by April 30, 2010.

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

Incorporated by reference from the registrant's definitive proxy statement to be filed with the SEC by April 30, 2010.

The following table sets forth equity compensation plan information at December 31, 2009.

Equity Compensation Plan Information

| Plan Category | Number of securities to be issued upon exercise of outstanding options, warrants and rights (a) | Weighted-average exercise price of outstanding options, warrants and rights (b) | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column(a)) (c) |
|--|--|---|--|
| Equity compensation plans approved by security holders | 81,055 | \$ 8.86 | |
| Equity compensation plans not approved by security holders | NA | NA | NA |
| Total | 81,055 | \$ 8.86 | |

A description of the Company's equity compensation plans is presented in Note 14 to the financial statements in the Registrant's annual report to shareholders.

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

Incorporated by reference from the registrant's definitive proxy statement to be filed with the SEC by April 30, 2010.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

Incorporated by reference from the registrant's definitive proxy statement to be filed with the SEC by April 30, 2010.

PART IV

ITEM 15. EXHIBITS

The following documents are filed as part of the report:

| | 2009 Annual Report To Stockholders Pages* |
|---|--|
| 1. Consolidated Financial Statements | |
| <u>Consolidated Balance Sheets December 31, 2009 and 2008</u> | 3 |
| <u>Consolidated Statements of Income Years ended December 31, 2009, 2008 and 2007</u> | 4 |
| <u>Consolidated Statements of Changes in Stockholders Equity Years ended December 31, 2009, 2008 and 2007</u> | 5 |
| <u>Consolidated Statements of Cash Flows Years ended December 31, 2009, 2008 and 2007</u> | 7 |
| <u>Notes to Consolidated Financial Statements</u> | 9 37 |
| <u>Report of Registered Public Accounting Firm</u> | 38 |

* Incorporated by reference from the indicated pages of the 2009 Annual Report to Stockholders

2. Consolidated Financial Statement Schedules

All schedules are omitted as the required information is inapplicable or the information is presented in the Consolidated Financial Statements or related notes.

3. Exhibits

The exhibits filed as part of this report and exhibits incorporated herein by reference to other documents are listed in the Index to this Annual Report on Form 10-K.

SIGNATURES

In accordance with Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant caused this report to be signed on behalf by the undersigned, thereunto duly authorized

3/26/10
Date

SURREY BANCORP

s/ Edward C. Ashby, III
Edward C. Ashby, III

President and Chief Executive Officer

(Principal Executive Officer)

In accordance with the Exchange Act, this report has to be signed below by the following persons on behalf of the registrant and in the capacity and on the dates indicated.

| Signature | Title | Date |
|---|--|----------------|
| s/ Edward C. Ashby, III Edward C. Ashby, III | Director, President and Chief Executive Officer (Principal Executive Officer) | <u>3/26/10</u> |
| s/ Mark H. Towe Mark H. Towe | Sr. Vice President and Chief Financial Officer (Principal Financial Officer) | <u>3/26/10</u> |
| s/ Hylton Wright Hylton Wright | Chairman of the Board | <u>3/26/10</u> |
| s/ William A. Johnson William A. Johnson | Director | <u>3/26/10</u> |
| s/ Elizabeth Johnson Lovill Elizabeth Johnson Lovill | Director | <u>3/26/10</u> |
| s/ Robert H. Moody Robert H. Moody | Director | <u>3/26/10</u> |
| s/ Tom G. Webb Tom G. Webb | Director | <u>3/26/10</u> |
| s/ Gene Rees Gene Rees | Director | <u>3/26/10</u> |
| s/ Buddy Williams Buddy Williams | Director | <u>3/26/10</u> |

INDEX TO EXHIBITS

| Exhibit | Description | |
|---------|--|---|
| 3.1 | Surrey Bancorp Articles of Incorporation | Incorporated by reference to Exhibit 3.1 to the Registrant's form 10Q dated November 13, 2009 |
| 3.2 | Surrey Bancorp Bylaws | Incorporated by reference to Exhibit 3(i) to the Registrant's form 8K dated May 1, 2003 |
| 10.1 | 1997 Incentive Stock Option Plan | Incorporated by reference to Exhibit 4.1 to the Registrant's Form S-8 dated September 11, 2003 |
| 10.2 | 1997 Nonstatutory Stock Option Plan | Incorporated by reference to Exhibit 4.1 to the Registrant's Form S-8 dated September 11, 2003 |
| 10.3 | Executive Salary Continuation Agreement of Edward C. Ashby, III | Incorporated by reference to Exhibit 10.1 to the Registrant's 2005 2 nd Quarter Form 10Q |
| 10.4 | Executive Salary Continuation Agreement of Mark H. Towe | Incorporated by reference to Exhibit 10.3 to the Registrant's 2005 2 nd Quarter Form 10Q |
| 10.5 | Executive Salary Continuation Agreement of Pedro A. Pequeno, II | Incorporated by reference to Exhibit 10.2 to the Registrant's 2005 2 nd Quarter Form 10Q |
| 10.6 | 409A Amendment to Surrey Bank & Trust Executive Salary Continuation Plan between the Bank and Edward C. Ashby, III | Incorporated by reference to Exhibit 10.3 to the Registrant's 2008 2 nd Quarter Form 10Q |
| 10.7 | 409A Amendment to Surrey Bank & Trust Executive Salary Continuation Plan between the Bank and Mark H. Towe | Incorporated by reference to Exhibit 10.3 to the Registrant's 2008 2 nd Quarter Form 10Q |
| 10.8 | 409A Amendment to Surrey Bank & Trust Executive Salary Continuation Plan between the Bank and Pedro A. Pequeno, II | Incorporated by reference to Exhibit 10.3 to the Registrant's 2008 2 nd Quarter Form 10Q |
| 10.9 | Amendment No. One to Employment Agreement of Edward C. Ashby, III | Incorporated by reference to Exhibit 10.3 to the Registrant's 2007 Form 10-K |
| 10.10 | Amendment No. One to Employment Agreement of Mark H. Towe | Incorporated by reference to Exhibit 10.4 to the Registrant's 2007 Form 10-K |
| 10.11 | Amendment No. One to Employment Agreement of Pedro A. Pequeno, II | Incorporated by reference to Exhibit 10.6 to the Registrant's 2007 Form 10-K |
| 10.12 | Amendment No. Two to Employment Agreement of Edward C. Ashby, III | Incorporated by reference to Exhibit 10.12 to the Registrant's 2008 Form 10-K |
| 10.13 | Amendment No. Two to Employment Agreement of Mark H. Towe | Incorporated by reference to Exhibit 10.13 to the Registrant's 2008 Form 10-K |
| 10.14 | Amendment No. Two to Employment Agreement of Pedro A. Pequeno, II | Incorporated by reference to Exhibit 10.14 to the Registrant's 2008 Form 10-K |
| 15.1 | 2009 Annual Report to Stockholders (such report, except to the extent incorporated herein by reference, is being furnished | |

for the information of the SEC only and is not deemed to be filed as part of the Report on Form 10-K)

- 21 Subsidiaries of the Registrant
- 23 Consent of Elliott Davis, LLC
- 31.1 Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer
- 31.2 Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer
- 32 Section 1350 Certifications
- 99.1 TARP Certification by Chief Executive Officer
- 99.2 TARP Certification by Chief Financial Officer