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FIRST BANCSHARES INC /MS/  
Form 10-K  
March 31, 2009

U.S. SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2008

OR

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

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

Commission file no. 33-94288

THE FIRST BANCSHARES, INC.

-----  
(Exact name of registrant as specified in its charter)

Mississippi

64-0862173

-----  
(State or Other Jurisdiction of  
Incorporation or Organization)

-----  
(I.R.S. Employer Identifica

6480 U.S. Hwy. 98 West  
Hattiesburg, Mississippi

39402

-----  
(Address of principal executive offices)

-----  
(Zip Code)

Issuer's telephone number: (601) 268-8998

Securities registered under Section 12(b) of the Exchange Act:

Title of Each Class

Name of Each Exchange on  
Which Registered

-----  
Common Stock, \$1.00 par value

-----  
NASDAQ Stock Market, LLC

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in rule 405

Yes \_\_\_\_\_ No  \_\_\_\_\_

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act.

Yes \_\_\_\_\_ No  \_\_\_\_\_

Note - Checking the box above will not relieve any registrant required to file reports pursuant to

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Exchange Act from their obligations under those Sections.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 15(d) of the 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 X No
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Indicate by check mark if disclosure of delinquent filers in response to Item 405 of Regulation S-K is contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive reports incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K [ X ]

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

Indicate by check mark whether the registrant is a large accelerated filer, an 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
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Based on the price at which the registrant's Common Stock was last sold at March 24, 2009, the aggregate market value of the registrant's Common Stock held by non-affiliates of the registrant for purposes of this calculation that all directors and executive officers of the registrant are "affiliates" of the registrant is \$2,990,201.

State the number of shares outstanding of each of the registrant's classes of common stock as of the latest practicable date. 2,990,201 on March 26, 2009.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the following documents are incorporated by reference to Parts II and III of this Form 10-K: the Registrant's Statement dated April 16, 2009, and the Annual Report to the Stockholders for the year ended December 31, 2008.

THE FIRST BANCSHARES, INC.
FORM 10-K
TABLE OF CONTENTS

PART I

ITEM 1. BUSINESS.....
ITEM 1A. RISK FACTORS.....
ITEM 1B. UNRESOLVED STAFF COMMENTS.....
ITEM 2. PROPERTIES.....
ITEM 3. LEGAL PROCEEDINGS.....
ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.....

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.....
ITEM 6. SELECTED FINANCIAL DATA.....
ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS.....
ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES.....
ITEM 8. FINANCIAL STATEMENTS.....
ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.....
ITEM 9A(T). CONTROLS AND PROCEDURES.....
ITEM 9B. OTHER INFORMATION.....

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PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.....

ITEM 11. EXECUTIVE COMPENSATION.....

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

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.....

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES.....

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.....

**THE FIRST BANCSHARES, INC.**  
**FORM 10-K**

**PART I**

This Report contains statements which constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and the Securities Exchange Act of 1934. These statements appear in a number of places in this Report and include all statements regarding the intent, belief or current expectations of the Company, its directors or its officers with respect to, among other things: (i) the Company s financing plans; (ii) trends affecting the Company s financial condition or results of operations; (iii) the Company s growth strategy and operating strategy; and (iv) the declaration and payment of dividends. Investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve risks and uncertainties, and that actual results may differ materially from those projected in the forward-looking statements as a result of various factors discussed herein and those factors discussed in detail in the Company s filings with the Securities and Exchange Commission.

**ITEM 1. BUSINESS.**

**BUSINESS OF THE COMPANY**

**General**

The First Bancshares, Inc. (the Company ) was incorporated on June 23, 1995 to serve as a bank holding company for The First, A National Banking Association ( The First ) located in Hattiesburg, Mississippi. The First began operations on August 5, 1996 from its main office in the Oak Grove community, which was on the outskirts of Hattiesburg but now is included in the city of Hattiesburg. In addition to the main office in Hattiesburg and the branch in Laurel, The First also operates two other branches in Hattiesburg, one in Purvis, one in Picayune, one in Pascagoula, one in Bay St. Louis, one in Wiggins, and one in Gulfport, Mississippi. The Company and its subsidiary bank engage in a general commercial and retail banking business characterized by personalized service and local decision-making, emphasizing the banking needs of small to medium-sized businesses, professional concerns and individuals. The First is a wholly-owned subsidiary bank of the Company.

**Location and Service Area**

The First serves the cities of Hattiesburg, Laurel, Purvis, Picayune, Pascagoula, Bay St. Louis, Wiggins, Gulfport and the surrounding areas of Lamar, Forrest, Jones, Pearl River ,Jackson, Hancock, Stone and Harrison Counties, Mississippi. The First has a main office located in the

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city of Hattiesburg, Mississippi, in Lamar County. The First has a branch office located on Highway 589 in the city of Purvis, Mississippi, also in Lamar County, a third office located at the intersection of Lincoln Road and South 28th Avenue in Hattiesburg, a fourth location at 110 S. 40th Ave. in Hattiesburg, a fifth location at Hwy 15 North in Laurel, a sixth location at Hwy 43 South in Picayune, a seventh location at Jackson Avenue in Pascagoula, an eighth location at Hwy 90 in Bay St. Louis, a ninth location at Border Ave. in Wiggins and a tenth location at Hwy 49 and O Neal Rd in Gulfport, Mississippi.

The main office primarily serves the area in and around the northern portion of Lamar County. The Purvis office primarily serves the area in and around Purvis, Mississippi, which is in the east central part of Lamar County and is the county seat. Lamar County is located in the southeastern section of Mississippi. Hattiesburg, one of the largest cities in Mississippi, is located in Forrest and Lamar Counties. The Laurel office serves the city of Laurel and the surrounding area of Jones County, Mississippi. The Picayune office primarily serves the area in and around Picayune, Mississippi, including areas of north Hancock County and Pearl River, LA and Slidell, LA. Picayune is located in the southern part of Pearl River County. Pearl River County is located in the southern section of Mississippi. The Pascagoula office primarily serves the area in and around Pascagoula, Mississippi, including areas of Jackson County. Hattiesburg can be reached via U.S. Highways 98 and 49 and Interstate 59. Major employers located in the Lamar and Forrest County areas include Forrest General Hospital, the University of Southern Mississippi, Wesley Medical Center, Camp Shelby, the Hattiesburg Public Schools, the Hattiesburg Clinic, the City of Hattiesburg, and Marshall Durbin Poultry. The principal components of the economy of the Lamar and Forrest County areas include service industries, wholesale and retail trade, manufacturing, and transportation and public utilities. The Laurel branch is located at 1945 Highway 15 North, Laurel, MS, with the majority of its retail business coming from the local area and the remaining business coming from other areas of Jones County, as well as portions of Jasper

1

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County, Wayne County, Smith County, and Covington County. Major employers in the Jones County area include Howard Industries, Sanderson Farms, Inc., and South Central Regional Medical Center. Major employers in the Pearl River County area include Stennis Space Center, Chevron, Texaco, Arizona Chemical, American Crescent Elevator Co., City of Picayune, Crosby Memorial Hospital and the public schools. The principal components of the economy of the Pearl River County area include timber, service industries, wholesale and retail trade, manufacturing, and transportation and public utilities. Major employers in the Jackson County area include Northrop Grumman, Singing River Hospital, and Shell Oil Company. The Bay St. Louis office serves the City of Bay St. Louis and the surrounding area of Hancock County, Mississippi. Bay St. Louis can be reached via U.S. Highway 90. Major employers in the Hancock area include the City of Bay St. Louis, Hancock County, and Stennis Space Center. The Wiggins office serves the City of Wiggins and the surrounding area of Stone County, Mississippi. Stone County is south of Forrest County and north of Harrison County. Wiggins can be reached via U. S. Highway 49. The Gulfport office serves the City of Gulfport and the surrounding area of Harrison County, Mississippi. Gulfport can be reached via U.S. Highway 49. Major employers in the Harrison County area include Keesler Air Force Base and a vast array of casinos.

### **Banking Services**

The Company strives to provide its customers with the breadth of products and services comparable to those offered by large regional banks, while maintaining the quick response and personal service of a locally owned and managed bank. In addition to offering a full range of deposit services and commercial and personal loans, The First offers products such as mortgage loan originations. The following is a description of the products and services offered or planned to be offered by the Bank.

*Deposit Services.* The Bank offers a full range of deposit services that are typically a savings and loan associations, including checking accounts, NOW accounts, savings accounts

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of various types, ranging from daily money market accounts to longer-term certificates of deposit. Checking accounts and time certificates are tailored to the Bank's principal market area at rates of interest offered by other banks in the area. In addition, the Bank offers certain retirement accounts, including Individual Retirement Accounts (IRAs). All deposit accounts are insured by the Federal Deposit Insurance Corporation (the "FDIC") up to the maximum amount allowed by law. The Bank solicits the services of individuals, businesses, associations and organizations, and governmental authorities.

*Loan Products.* The Bank offers a full range of commercial and personal loans. Commercial loans include secured and unsecured loans for working capital (including loans secured by inventory and accounts receivable), business expansion (including acquisition of real estate and improvements), and purchase of machinery. Consumer loans include equity lines of credit and secured and unsecured loans for home improvements, education, and personal investments. The Bank also makes real estate acquisition loans. The Bank's lending activities are subject to a variety of lending limits under state law. While differing limits apply in certain circumstances based on the type of loan or borrower (including the borrower's relationship to the bank), in general the Bank is subject to a maximum loan-to-value of an amount equal to 15% of the Bank's unimpaired capital and surplus. The Bank may not make loans to a director, executive officer, or 10% shareholder unless the loan is approved by the Board of Directors and is made on terms not more favorable to such a person than would be available to a person not affiliated with the Bank.

*Mortgage Loan Divisions.* The Bank has mortgage loan divisions which originate loans to finance the purchase of new homes, construct new homes and to refinance existing mortgages.

*Other Services.* Other bank services include on-line Internet banking services, voice remote deposit capture service, commercial sweep accounts, cash management services, safe deposit boxes, travel services, and payroll and social security checks, and automatic drafts for various accounts. The Bank is a member of the Interlink, Plus, Pulse and Star networks of automated teller machines that may be used throughout Mississippi and other regions. The Bank also offers VISA and MasterCard credit cards and operates a correspondent bank.

### Competition

The Bank generally competes with other financial institutions through the selection of banking products and services offered, the pricing of services, the level of service provided, the convenience and availability of services, and the degree of expertise and the personal manner in which services are offered. Mississippi law permits statewide branching by banks and savings institutions, and many financial institutions in the state have branch networks. Consequently, commercial banking in Mississippi is highly competitive. Many large banking organizations currently operate in the Company's market area, several of which are controlled by out-of-state ownership. In addition, competition between commercial banks and thrift institutions (savings institutions and credit unions) has been intensified significantly by the elimination of many previous distinctions between the various types of financial institutions and the expanded powers and increased activity of thrift institutions in areas of banking which previously had been the sole domain of commercial banks. Federal legislation, together with other regulatory changes by the primary regulators of the various financial institutions, has resulted in the almost total elimination of practical distinctions between a commercial bank and a thrift institution. Consequently, competition among financial institutions of all types is largely unlimited with respect to legal ability and authority to provide most financial services.

The Company faces increased competition from both federally-chartered and state-chartered financial and thrift institutions, as well as credit unions, consumer finance companies, insurance companies, and other institutions in the Company's market area. Some of these competitors are not subject to the same degree of regulation and restriction imposed upon the Company. Many of these competitors also have broader geographic markets and substantially greater resources and lending limits than the Company and offer certain services such as trust banking that the Company does not currently provide. In addition, many of these competitors have

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numerous branch offices located throughout the extended market areas of the Company that may provide these competitors with an advantage in geographic convenience that the Company does not have at present.

Currently there are numerous other commercial banks, savings institutions, and credit unions operating in The First's primary service area.

### **Employees**

As of March 26, 2009 the Company had 148 full-time employees and 10 part-time employees.

### **SUPERVISION AND REGULATION**

The Company and its bank are subject to state and federal banking laws and regulations which impose specific requirements or restrictions on and provide for general regulatory oversight with respect to virtually all aspects of operations. These laws and regulations are generally intended to protect depositors, not shareholders. To the extent that the following summary describes statutory or regulatory provisions, it is qualified in its entirety by reference to the particular statutory and regulatory provisions. Any change in applicable laws or regulations may have a material effect on the business and prospects of the Company. Beginning with the enactment of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 ( FIRREA ) and following with Federal Deposit Insurance Corporation Improvement Act of 1991 ( FDICIA ), numerous additional regulatory requirements have been placed on the banking industry in the past several years, and additional changes have been proposed. The operations of the Company and the Bank may be affected by legislative changes and the policies of various regulatory authorities. The Company is unable to predict the nature or the extent of the effect on its business and earnings that fiscal or monetary policies, economic control, or new federal or state legislation may have in the future.

3

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### **The Company**

Because it owns the outstanding capital stock of the Bank, the Company is a bank holding company within the meaning of the Federal Bank Holding Company Act of 1956 (the BHCA ).

*The BHCA.* Under the BHCA, the Company is subject to periodic examination by the Federal Reserve and is required to file periodic reports of its operations and such additional information as the Federal Reserve may require. The Company's and the Bank's activities are limited to banking, managing or controlling banks, furnishing services to or performing services for its subsidiaries, and engaging in other activities that the Federal Reserve determines to be so closely related to banking or managing or controlling banks as to be a proper incident thereto.

*Investments, Control, and Activities.* With certain limited exceptions, the BHCA requires every bank holding company to obtain the prior approval of the Federal Reserve before (i) acquiring substantially all the assets of any bank, (ii) acquiring direct or indirect ownership or control of any voting shares of any bank if after such acquisition it would own or control more than 5% of the voting shares of such bank (unless it already owns or controls the majority of such shares), or (iii) merging or consolidating with another bank holding company.

In addition, and subject to certain exceptions, the BHCA and the Change in Bank Control Act, together with regulations thereunder, require Federal Reserve approval (or, depending on the circumstances, no notice of disapproval) prior to any person or company acquiring control of a

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bank holding company, such as the Company. Control is conclusively presumed to exist if an individual or company acquires 25% or more of any class of voting securities of the bank holding company. Control is rebuttably presumed to exist if a person acquires 10% or more but less than 25% of any class of voting securities and either the Company has registered securities under Section 12 of the Exchange Act (which the Company has done) or no other person owns a greater percentage of that class of voting securities immediately after the transaction. The regulations provide a procedure for challenge of the rebuttable control presumption.

Under the BHCA, a bank holding company is generally prohibited from engaging in, or acquiring direct or indirect control of more than 5% of the voting shares of any company engaged in nonbanking activities, unless the Federal Reserve Board, by order or regulation, has found those activities to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. Some of the activities that the Federal Reserve Board has determined by regulation to be proper incidents to the business of a bank holding company include making or servicing loans and certain types of leases, engaging in certain insurance and discount brokerage activities, performing certain data processing services, acting in certain circumstances as a fiduciary or investment or financial adviser, owning savings associations, and making investments in certain corporations or projects designed primarily to promote community welfare.

The Federal Reserve Board has imposed certain capital requirements on the Company under the BHCA, including a minimum leverage ratio and a minimum ratio of qualifying capital to risk-weighted assets. These requirements are described below under Capital Regulations. Subject to its capital requirements and certain other restrictions, the Company may borrow money to make a capital contribution to the Banks, and such loans may be repaid from dividends paid from the Bank to the Company (although the ability of the Bank to pay dividends is subject to regulatory restrictions as described below in The Bank Dividends ). The Company is also able to raise capital for contribution to the Bank by issuing securities without having to receive regulatory approval, subject to compliance with federal and state securities laws.

*Source of Strength; Cross-Guarantee.* In accordance with Federal Reserve Board policy, the Company is expected to act as a source of financial strength to the Bank and to commit resources to support the Bank in circumstances in which the Company might not otherwise do so. Under the BHCA, the Federal Reserve Board may require a bank holding company to terminate any activity or relinquish control of a nonbank subsidiary (other than a nonbank subsidiary of a bank) upon the Federal Reserve Board's determination that such activity or control constitutes a serious risk to the financial soundness or stability of any subsidiary depository institution of the bank holding company. Further, federal bank regulatory authorities have additional discretion to require a bank holding company to divest itself of any bank or nonbank subsidiary if the agency determines that divestiture may aid the depository institution's financial condition.

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### **The Bank**

The Bank operates as a national banking association incorporated under the laws of the United States and subject to examination by the Office of Comptroller of the Currency ( OCC ). Deposits in the Bank are insured by the FDIC up to a maximum amount (generally \$250,000 per depositor, subject to aggregation rules). The OCC and the FDIC regulate or monitor virtually all areas of the Bank's operations, including security devices and procedures, adequacy of capitalization and loan loss reserves, loans, investments, borrowings, deposits, mergers, issuances of securities, payment of dividends, interest rates payable on deposits, interest rates or fees chargeable on loans, establishment of branches, corporate reorganizations, maintenance of books and records, and adequacy of staff training to carry on safe lending and deposit gathering practices. The OCC requires the Bank to maintain certain capital ratios and imposes limitations on the Bank's aggregate investment in real estate, bank premises, and furniture and fixtures. The Bank is required by the OCC to prepare quarterly reports on their financial condition and to conduct an annual audit of their financial affairs in compliance with minimum standards and procedures

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prescribed by the OCC.

Under FDICIA, all insured institutions must undergo regular on-site examinations by their appropriate banking agency. The cost of examinations of insured depository institutions and any affiliates may be assessed by the appropriate agency against each institution or affiliate as it deems necessary or appropriate. Insured institutions are required to submit annual reports to the FDIC and the appropriate agency (and state supervisor when applicable). FDICIA also directs the FDIC to develop with other appropriate agencies a method for insured depository institutions to provide supplemental disclosure of the estimated fair market value of assets and liabilities, to the extent feasible and practicable, in any balance sheet, financial statement, report of condition, or any other report of any insured depository institution. FDICIA also requires the federal banking regulatory agencies to prescribe, by regulation, standards for all insured depository institutions and depository institution holding companies relating, among other things, to: (i) internal controls, information systems, and audit systems; (ii) loan documentation; (iii) credit underwriting; (iv) interest rate risk exposure; and (v) asset quality.

National banks and their holding companies which have been chartered or registered or undergone a change in control within the past two years or which have been deemed by the OCC or the Federal Reserve Board, respectively, to be troubled institutions must give the OCC or the Federal Reserve Board, respectively, thirty days prior notice of the appointment of any senior executive officer or director. Within the thirty day period, the OCC or the Federal Reserve Board, as the case may be, may approve or disapprove any such appointment.

*Deposit Insurance.* The FDIC establishes rates for the payment of premiums by federally insured banks and thrifts for deposit insurance. A separate Bank Insurance Fund ( BIF ) and Savings Association Insurance Fund ( SAIF ) are maintained for commercial banks and thrifts, respectively, with insurance premiums from the industry used to offset losses from insurance payouts when banks and thrifts fail. Since 1993, insured depository institutions like the Bank have paid for deposit insurance under a risk-based premium system.

*Transactions With Affiliates and Insiders.* The Bank is subject to Section 23A of the Federal Reserve Act, which places limits on the amount of loans to, and certain other transactions with, affiliates, as well as on the amount of advances to third parties collateralized by the securities or obligations of affiliates. The aggregate of all covered transactions is limited in amount, as to any one affiliate, to 10% of the Bank s capital and surplus and, as to all affiliates combined, to 20% of the Bank s capital and surplus. Furthermore, within the foregoing limitations as to amount, each covered transaction must meet specified collateral requirements.

The Bank is also subject to Section 23B of the Federal Reserve Act, which prohibits an institution from engaging in certain transactions with affiliates unless the transactions are on terms substantially the same, or at least as favorable to such institution, as those prevailing at the time for comparable transactions with nonaffiliated companies. The Bank is subject to certain restrictions on extensions of credit to executive officers, directors, certain principal shareholders, and their related interests. Such extensions of credit (i) must be made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with third parties and (ii) must not involve more than the normal risk of repayment or present other unfavorable features.

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*Dividends.* A national bank may not pay dividends from its capital. All dividends must be paid out of undivided profits then on hand, after deducting expenses, including reserves for losses and bad debts. In addition, a national bank is prohibited from declaring a dividend on its shares of common stock until its surplus equals its stated capital, unless the bank has transferred to surplus no less than one-tenth of its net profits of the preceding two consecutive half-year periods (in the case of an annual dividend). The approval of the OCC is required if the total of all dividends declared by a national bank in any calendar year exceeds the total of its net profits for that year combined with its retained net profits for the



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preceding two years, less any required transfers to surplus. In addition, under FDICIA, the banks may not pay a dividend if, after paying the dividend, the bank would be undercapitalized. See Capital Regulations below.

*Branching.* National banks are required by the National Bank Act to adhere to branch office banking laws applicable to state banks in the states in which they are located. Under current Mississippi law, the Banks may open branches throughout Mississippi with the prior approval of the OCC. In addition, with prior regulatory approval, the Banks are able to acquire existing banking operations in Mississippi. Furthermore, federal legislation has recently been passed which permits interstate branching. The new law permits out of state acquisitions by bank holding companies (subject to veto by new state law), interstate branching by banks if allowed by state law, interstate merging by banks, and de novo branching by national banks if allowed by state law. See Recent Legislative Developments.

*Community Reinvestment Act.* The Community Reinvestment Act requires that, in connection with examinations of financial institutions within their respective jurisdictions, the Federal Reserve, the FDIC, the OCC, or the Office of Thrift Supervision shall evaluate the record of the financial institutions in meeting the credit needs of their local communities, including low and moderate income neighborhoods, consistent with the safe and sound operation of those institutions. These factors are also considered in evaluating mergers, acquisitions, and applications to open a branch or facility.

*Other Regulations.* Interest and certain other charges collected or contracted for by the Banks are subject to state usury laws and certain federal laws concerning interest rates. The Bank's loan operations are subject to certain federal laws applicable to credit transactions, such as the federal Truth-In-Lending Act, governing disclosures of credit terms to consumer borrowers; the Home Mortgage Disclosure Act of 1975, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs community it serves; the Equal Credit Opportunity Act, prohibiting discrimination on the basis of creed or other prohibited factors in extending credit; the Fair Credit Reporting Act of 1978, governing the use and provision of information to credit reporting agencies; the Fair Debt Collection Act, concerning the manner in which consumer debts may be collected by collection agencies; and the rules and regulations of the various federal agencies charged with the responsibility of implementing such federal laws. The deposit operations of the Bank also are subject to the Right to Financial Privacy Act, which imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records, and the Electronic Funds Transfer Act and Regulation E issued by the Federal Reserve Board to implement that Act, which governs automatic deposits to and withdrawals from deposit accounts and customers' rights and liabilities arising from the use of automated teller machines and other electronic banking services.

*Capital Regulations.* The federal bank regulatory authorities have adopted risk-based capital guidelines for banks and bank holding companies that are designed to make regulatory capital requirements more sensitive to differences in risk profile among banks and bank holding companies, account for off-balance sheet exposure, and minimize disincentives for holding liquid assets. The resulting capital ratios represent qualifying capital as a percentage of total risk-weighted assets and off-balance sheet items. The guidelines are minimums, and the federal regulators have noted that banks and bank holding companies contemplating significant expansion programs should not allow expansion to diminish their capital ratios and should maintain ratios well in excess of the minimums. The current guidelines require all bank holding companies and federally-regulated banks to maintain a minimum risk-based total capital ratio equal to 8%, of which at least 4% must be Tier 1 capital. Tier 1 capital includes common shareholders' equity, qualifying perpetual preferred stock, and minority interests in equity accounts of consolidated subsidiaries, but excludes goodwill and most other intangibles and excludes the allowance for loan and lease losses. Tier 2 capital includes the excess of any preferred stock not included in Tier 1 capital, mandatory convertible securities, hybrid capital instruments, subordinated debt and intermediate term-preferred stock, and general reserves for loan and lease losses up to 1.25% of risk-weighted assets.

Under the guidelines, banks and bank holding companies assets are given risk-weights of 0%, 20%, 50% and 100%. In addition, certain off-balance sheet items are given credit conversion factors to convert them to asset equivalent amounts to which an appropriate risk-weight will apply. These computations result in the total risk-weighted assets. Most loans are assigned to the 100% risk category, except for first mortgage loans fully secured by residential property and, under certain circumstances, residential construction loans, both of which carry a 50% rating. Most investment securities are assigned to the 20% category, except for municipal or state revenue bonds, which have a 50% rating, and direct obligations of or obligations guaranteed by the United States Treasury or United States Government agencies, which have a 0% rating.

The federal bank regulatory authorities have also implemented a leverage ratio, which is Tier 1 capital as a percentage of average total assets less intangibles, to be used as a supplement to the risk-based guidelines. The principal objective of the leverage ratio is to place a constraint on the maximum degree to which a bank holding company may leverage its equity capital base. The minimum required leverage ratio for top-rated institutions is 3%, but most institutions are required to maintain an additional cushion of at least 100 to 200 basis points.

FDICIA established a capital-based regulatory scheme designed to promote early intervention for troubled banks and requires the FDIC to choose the least expensive resolution of bank failures. The capital-based regulatory framework contains five categories of compliance with regulatory capital requirements, including well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized. To qualify as a well capitalized institution, a bank must have a leverage ratio of no less than 5%, a Tier 1 risk-based ratio of no less than 6%, and a total risk-based capital ratio of no less than 10%, and the Bank must not be under any order or directive from the appropriate regulatory agency to meet and maintain a specific capital level. As of December 31, 2006, the Company and The First, were qualified as well capitalized.

Under the FDICIA regulations, the applicable agency can treat an institution as if it were in the next lower category if the agency determines (after notice and an opportunity for hearing) that the institution is in an unsafe or unsound condition or is engaging in an unsafe or unsound practice. The degree of regulatory scrutiny of a financial institution will increase, and the permissible activities of the institution will decrease, as it moves downward through the capital categories. Institutions that fall into one of the three undercapitalized categories may be required to (i) submit a capital restoration plan; (ii) raise additional capital; (iii) restrict their growth, deposit interest rates, and other activities; (iv) improve their management; (v) eliminate management fees; or (vi) divest themselves of all or part of their operations. Bank holding companies controlling financial institutions can be called upon to boost the institutions capital and to partially guarantee the institutions performance under their capital restoration plans.

These capital guidelines can affect the Company in several ways. If the Company continues to grow at a rapid pace, a premature squeeze on capital could occur making a capital infusion necessary. The requirements could impact the Company's ability to pay dividends. The Company's present capital levels are more than adequate; however, rapid growth, poor loan portfolio performance, or poor earnings performance could change the Company's capital position in a relatively short period of time.

Failure to meet these capital requirements would mean that a bank would be required to develop and file a plan with its primary federal banking regulator describing the means and a schedule for achieving the minimum capital requirements. In addition, such a bank would generally not receive regulatory approval of any application that requires the consideration of capital adequacy, such as a branch or merger application, unless the Bank could demonstrate a reasonable plan to meet the capital requirement within a reasonable period of time.

*Enforcement Powers.* FIRREA expanded and increased civil and criminal penalties available for use by the federal regulatory agencies against depository institutions and certain institution-affiliated parties (primarily including management, employees, and agents of a

financial institution, independent contractors such as attorneys and accountants, and others who participate in the conduct of the financial institution's affairs). These practices can include the failure of an institution to timely file required reports; the filing of false or misleading information; or the submission of inaccurate reports. Civil penalties may be as high as \$1,000,000 a day for such violations. Criminal penalties for some financial institution crimes have been increased to twenty years. In addition, regulators are provided with greater flexibility to commence enforcement actions against institutions and institution-affiliated parties. Possible enforcement actions include the termination of deposit insurance. Furthermore, FIRREA expanded the appropriate banking agencies' power 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, indemnifications, or guarantees against loss. A financial institution may also be ordered to restrict its growth, dispose of certain assets, rescind agreements or contracts, or take other actions as determined by the ordering agency to be appropriate.

7

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*Effect of Governmental Monetary Policies.* The earnings of the Bank are affected by domestic economic conditions and the monetary and fiscal policies of the United States government and its agencies. The Federal Reserve Board's monetary policies have had, and are likely to continue to have, an important impact on the operating results of commercial banks through its power to implement national monetary policy in order, among other things, to curb inflation or combat a recession. The monetary policies of the Federal Reserve Board have major effects upon the levels of bank loans, investments, and deposits through its open market operations in United States government securities and through its regulation of the discount rate on borrowings of member banks and the reserve requirements against member bank deposits. It is not possible to predict the nature or impact of future changes in monetary and fiscal policies.

*Significant Legislative Developments.* On September 29, 1994, the federal government enacted the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the Interstate Banking Act). This Act became effective on September 29, 1995 and permits eligible bank holding companies in any state, with regulatory approval, to acquire banking organizations in any other state. Since June 1, 1997, the Interstate Banking Act has allowed banks with different home states to merge, unless a particular state opts out of the statute. In addition, beginning June 1, 1997, the Interstate Banking Act has permitted national and state banks to establish de novo branches in another state if there is a law in that state which applies equally to all banks and expressly permits all out-of-state banks to establish de novo branches.

On November 12, 1999, the Gramm-Leach-Bliley Act of 1999 (the Financial Services Modernization Act) was signed into law. The Financial Services Modernization Act repeals the two affiliation provisions of the Glass-Steagall Act: Section 20, which restricted the affiliation of Federal Reserve Member Banks with firms engaged principally in specified securities activities; and Section 32, which restricts officer, director, or employee interlocks between a member bank and any company or person primarily engaged in specified securities activities. In addition, the Financial Services Modernization Act also contains provisions that expressly preempt any state law restricting the establishment of financial affiliations, primarily related to insurance. The general effect of the law is to establish a comprehensive framework to permit affiliations among commercial banks, insurance companies, securities firms, and other financial service providers by revising and expanding the BHCA framework to permit a holding company system to engage in a full range of financial activities through a new entity known as a Financial Holding Company.

Financial activities is broadly defined to include not only banking, insurance, and securities activities, but also merchant banking and additional activities that the Federal Reserve, in consultation with the Secretary of the Treasury, determines to be financial in nature, incidental to such financial activities, or complementary activities that do not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally.

Generally, the Financial Services Modernization Act:

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Repeals historical restrictions on, and eliminates many federal and state law barriers among banks, securities firms, insurance companies, and other financial service

Provides a uniform framework for the functional regulation of the activities of financial institutions, and their holding companies;

Broadens the activities that may be conducted by national banks, banking subsidiary companies, and their financial subsidiaries;

8

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Provides an enhanced framework for protecting the privacy of consumer information

Adopts a number of provisions related to the capitalization, membership, corporate measures designed to modernize the Federal Home Loan Bank system;

Modifies the laws governing the implementation of the Community Reinvestment Act

Addresses a variety of other legal and regulatory issues affecting both day-to-day activities of financial institutions.

In order for a bank holding company to take advantage of the ability to affiliate with other financial services providers, that company must become a Financial Holding Company as permitted under an amendment to the BHCA. To become a Financial Holding Company, the company would file a declaration with the Federal Reserve, electing to engage in activities permissible for Financial Holding Companies and certifying that it is eligible to do so because all of its insured depository institution subsidiaries are well-capitalized and well-managed. In addition, the Federal Reserve must also determine that each insured depository institution subsidiary of the Company has at least a satisfactory CRA rating.

The Financial Services Modernization Act also permits national banks to engage in expanded activities through the formation of financial subsidiaries. A national bank may have a subsidiary engaged in any activity authorized for national banks directly or any financial activity, except for insurance underwriting, insurance investments, real estate investment or development, or merchant banking, which may only be conducted through a subsidiary of a Financial Holding Company. Financial activities include all activities permitted under new sections of the BHCA or permitted by regulation.

A national bank seeking to have a financial subsidiary, and each of its depository institution affiliates, must be well-capitalized and well-managed. The total assets of all financial subsidiaries may not exceed the lesser of 45% of a bank's total assets, or \$50 billion. A national bank must exclude from its assets and equity all equity investments, including retained earnings, in a financial subsidiary. The assets of the subsidiary may not be consolidated with the bank's assets. The bank must also have policies and procedures to assess financial subsidiary risk and protect the bank from such risks and potential liabilities.

The Financial Services Modernization Act also includes a new section of the Federal Deposit Insurance Act governing subsidiaries of state banks that engage in activities as principal that would only be permissible for a national bank to conduct in a financial subsidiary. It expressly preserves the ability of a state bank to retain all existing subsidiaries. Because Mississippi permits commercial banks chartered by the state to engage in any activity permissible for national banks, the state bank competitors of The First will be permitted to form subsidiaries to engage in the activities authorized by the Financial Services Modernization Act, to the same extent as The First. In order to form a financial subsidiary, a state bank must be well-capitalized, and the state bank would be subject to the same capital deduction, risk management and affiliate transaction rules as applicable to national banks.

The Company and the Bank do not believe that the Financial Services Modernization Act will have a material adverse effect on operations in the near-term. However, to the extent that it permits

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banks, securities firms, and insurance companies to affiliate, the financial services industry may experience further consolidation. The Financial Services Modernization Act is intended to grant to community banks certain powers as a matter of right that larger institutions have accumulated on an ad hoc basis. Nevertheless, this act may have the result of increasing the amount of competition that the Company and the Bank face from larger institutions and other types of companies offering financial products, many of which may have substantially more financial resources than the Company and the Bank.

9

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In 2001, the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA Patriot Act) was signed into law. The USA Patriot Act broadened the application of anti-money laundering regulations to apply to additional types of financial institutions, such as broker-dealers, and strengthened the ability of the U.S. Government to detect and prosecute international money laundering and the financing of terrorism. The principal provisions of Title III of the USA Patriot Act require that regulated financial institutions, including state member banks: (i) establish an anti-money laundering program that includes training and audit components; (ii) comply with regulations regarding the verification of the identity of any person seeking to open an account; (iii) take additional required precautions with non-U.S. owned accounts; and (iv) perform certain verification and certification of money laundering risk for their foreign correspondent banking relationships. The USA Patriot Act also expanded the conditions under which funds in a U.S. interbank account may be subject to forfeiture and increased the penalties for violation of anti-money laundering regulations. Failure of a financial institution to comply with the USA Patriot Act's requirements could have serious legal and reputational consequences for the institution. The Bank has adopted policies, procedures and controls to address compliance with the requirements of the USA Patriot Act under the existing regulations and will continue to revise and update its policies, procedures and controls to reflect changes required by the USA Patriot Act and implementing regulations.

In July 2002, Congress enacted the Sarbanes-Oxley Act of 2002, which addresses, among other issues, corporate governance, auditing and accounting, executive compensation, and enhanced and timely disclosure of corporate information. Section 404 of the Sarbanes-Oxley Act, and regulations adopted by the SEC will in the future require the Company to include in its Annual Report, a report stating management's responsibility to establish and maintain adequate internal control over financial reporting and management's conclusion on the effectiveness of the internal controls at year end. Additionally, the Company's independent registered public accounting firm will in the future be required to attest to and report on management's evaluation of internal control over financial reporting.

From time to time, various bills are introduced in the United States Congress with respect to the regulation of financial institutions. Certain of these proposals, if adopted, could significantly change the regulation of banks and the financial services industry. The Company cannot predict whether any of these proposals will be adopted or, if adopted, how these proposals would affect the Company.

### **Recent Developments**

*Recent Legislative and Regulatory Initiatives to Address Financial and Economic Crises.* The Congress, Treasury Department and the federal banking regulators, including the FDIC, have taken broad action since early September, 2008 to address volatility in the U.S. banking system.

*Emergency Economic Stabilization Act of 2008.* In October 2008, the Emergency Economic Stabilization Act of 2008 (EESA) was enacted. The EESA authorizes the Treasury Department to purchase from financial institutions and their holding companies up to \$700 billion in mortgage loans, mortgage-related securities and certain other financial instruments, including debt and equity securities issued by financial institutions and their holding companies in a troubled asset relief program (TARP). The purpose of TARP is to restore confidence and stability to the

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U.S. banking system and to encourage financial institutions to increase their lending to customers and to each other. The Treasury Department has allocated \$250 billion towards the TARP Capital Purchase Program ( CPP ). Under the CPP, Treasury will purchase debt or equity securities from participating institutions. The TARP also will include direct purchases or guarantees of troubled assets of financial institutions. Participants in the CPP are subject to executive compensation limits and are encouraged to expand their lending and mortgage loan modifications.

On February 6, 2009, as part of the TARP CPP, the Company entered into a Letter Agreement and Securities Purchase Agreement (collectively, the Purchase Agreement ) with the Treasury Department, pursuant to which the Company sold (i) 5,000 shares of the Company s Fixed Rate Cumulative Perpetual Preferred Stock, Series UST, no par value per share (the Series UST Preferred Stock ) and (ii) a warrant (the Warrant ) to purchase 54,705 shares of the Company s common stock ( the Common Stock ), no par value per share, for an aggregate purchase price of \$5 million in cash.

The Series UST Preferred Stock will qualify as Tier 1 capital and will be entitled to cumulative dividends at a rate of 5% per annum for the first five years, and 9% per annum thereafter. The Series UST Preferred Stock may be redeemed by the Company after three years. Prior to the end of three years, the Series UST Preferred Stock may be redeemed by the Company only with proceeds from the sale of qualifying equity securities of the Company. The Warrant has a 10-year term and is immediately exercisable upon its issuance, with an exercise price, subject to anti-dilution adjustments, equal to \$13.71 per share of the common stock. For more information, please see the Company s Form 8-K filed on February 12, 2009.

10

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EESA also increased FDIC deposit insurance on most accounts from \$100,000 to \$250,000. This increase is in place until the end of 2009 and is not covered by deposit insurance premiums paid by the banking industry.

Following a systemic risk determination, the FDIC established a Temporary Liquidity Guarantee Program ( TLGP ) on October 14, 2008. The TLGP includes the Transaction Account Guarantee Program ( TAGP ), which provides unlimited deposit insurance coverage through December 31, 2009 for noninterest-bearing transaction accounts (typically business checking accounts) and certain funds swept into noninterest-bearing savings accounts. Institutions participating in the TAGP pay a 10 basis points fee (annualized) on the balance of each covered account in excess of \$250,000, while the extra deposit insurance is in place. The TLGP also includes the Debt Guarantee Program ( DGP ), under which the FDIC guarantees certain senior unsecured debt of FDIC-insured institutions and their holding companies. The unsecured debt must be issued on or after October 14, 2008 and not later than June 30, 2009, and the guarantee is effective through the earlier of the maturity date or June 30, 2012. The DGP coverage limit is generally 125% of the eligible entity s eligible debt outstanding on September 30, 2008 and scheduled to mature on or before June 30, 2009 or, for certain insured institutions, 2% of their liabilities as of September 30, 2008. Depending on the term of the debt maturity, the nonrefundable DGP fee ranges from 50 to 100 basis points (annualized) for covered debt outstanding until the earlier of maturity or June 30, 2012. The TAGP and DGP are in effect for all eligible entities, unless the entity opted out on or before December 5, 2008. The Company will participate in the TAGP but has opted out of the DGP.

*America Reinvestment and Recovery Act of 2009.* On February 17, 2009, President Obama signed into law the America Reinvestment and Recovery Act of 2009 ( ARRA ). ARRA contains expansive new restrictions on executive compensation for financial institutions and other companies participating in the CPP. These restrictions apply to us.

ARRA prohibits the payment of any bonus, retention award, or incentive compensation to the Chief Executive Officer of the Company for as long as any CPP-related obligations are outstanding. The prohibition does not apply to bonuses payable pursuant to a written contract agreements in effect prior to February 11, 2009. Long-term restricted stock is excluded from ARRA s bonus prohibition, but only to the extent the value of the stock does not exceed one-third of the

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total amount of annual compensation of the employee receiving the stock, the stock does not fully vest until after all CPP-related obligations have been satisfied, and any other conditions which the Treasury may specify have been met.

ARRA prohibits any payment to the Chief Executive Officer and the next five highest paid Executive Officers of the Company upon termination of employment for any reason for as long as any CPP-related obligations remain outstanding.

Under ARRA CPP-participating companies are required to recover any bonus or other incentive payment paid to the Chief Executive Officer and the next twenty highest paid employees of the Company on the basis of materially inaccurate financial or other performance criteria.

ARRA prohibits CPP participants from implementing any compensation plan that would encourage manipulation of the reported earnings of the company in order to enhance the compensation of any of its employees. Earlier Treasury guidelines did not contain a similar requirement.

ARRA requires the Chief Executive Officer and the Chief Financial Officer of any publicly-traded CPP-participating company to provide a written certification of compliance with the executive compensation restrictions in ARRA in the company's annual filings with the SEC (presumably its annual report on Form 10-K or proxy statement).

11

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ARRA requires each CPP-participating company to implement a company-wide policy regarding excessive or luxury expenditures, including excessive expenditures on entertainment or events, office and facility renovations, aviation or other transportation services.

ARRA directs the Treasury to review bonuses, retention awards, and other compensation paid to the Chief Executive Officer and the next twenty highest paid employees of the Company of each company receiving CPP assistance before ARRA was enacted, and to seek to negotiate with the CPP recipient and affected employees for reimbursement if it finds any such payments were inconsistent with CPP or otherwise in conflict with the public interest.

The Compensation Committee will consider these new limits on executive compensation and determine how they impact the Company's executive compensation program.

### **ITEM 1A. RISK FACTORS**

Making or continuing an investment in securities, including The First Bancshares Common Stock, involves certain risks that you should carefully consider. The risks and uncertainties described below are not the only risks that may have a material adverse effect on First Bancshares. Additional risks and uncertainties also could adversely affect First Bancshares' business and results of operations. If any of the following risks actually occur, First Bancshares' business, financial condition or results of operations could be affected, the market price for your securities could decline, and you could lose all or a part of your investment. Further, to the extent that any of the information contained in this Annual Report on Form 10-K constitutes forward-looking statements, the risk factors set forth below also are cautionary statements identifying important factors that could cause First Bancshares' actual results to differ materially from those expressed in any forward-looking statements made by or on behalf of First Bancshares.

*First Bancshares may be vulnerable to certain sectors of the economy.*

A portion of First Bancshares' loan portfolio is secured by real estate. If the economy deteriorated and depressed real estate values beyond a certain point, that collateral value of the portfolio and the revenue stream from those loans could come under stress and possibly require additional loan loss accruals. First Bancshares' ability to dispose of foreclosed real estate at prices above the respective carrying values could also be impinged, causing additional

losses.

*Difficult market conditions have adversely affected the industry in which we operate.*

The capital and credit markets have been experiencing volatility and disruption for more than a year. In recent months, the volatility and disruption has reached unprecedented levels. Dramatic declines in the housing market over the past year, with falling home prices and increasing foreclosures, unemployment and under-employment, have negatively impacted the credit performance of mortgage loans and resulted in significant write-downs of asset values by financial institutions, including government-sponsored entities as well as major commercial and investment banks. Reflecting concern about the stability of the financial markets generally and the strength of counterparties, many lenders have reduced or ceased providing funding to borrowers, including to other financial institutions. This market turmoil and tightening of credit have led to an increased level of commercial and consumer delinquencies, lack of consumer confidence and widespread reduction of business activity generally. A worsening of these conditions would likely exacerbate the adverse effects of these difficult market conditions on us and others in the financial institution industry. Also, the economic downturn could exacerbate our exposure to credit risk, particularly in our real estate markets, as lower home prices and increased foreclosures may result in higher charge-offs and delinquencies.

12

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*General economic conditions in the areas where First Bancshares operations or loans are concentrated may adversely affect our customers ability to meet their obligations.*

A sudden or severe downturn in the economy in the geographic markets served by First Bancshares in the state of Mississippi may affect the ability of First Bancshares customers to meet loan payments obligations on a timely basis. The local economic conditions in these areas have a significant impact on First Bancshares commercial, real estate, and construction loans, the ability of borrowers to repay these loans and the value of the collateral securing such loans. Changes resulting in adverse economic conditions of First Bancshares market areas could negatively impact the financial results of First Bancshares banking operations and its profitability. Additionally, adverse economic changes may cause customers to withdraw deposit balances, thereby causing a strain on First Bancshares liquidity.

*First Bancshares is subject to a risk of rapid and significant changes in market interest rates.*

First Bancshares assets and liabilities are primarily monetary in nature, and as a result First Bancshares is subject to significant risks tied to changes in interest rates. First Bancshares ability to operate profitably is largely dependent upon net interest income. Unexpected movement in interest rates markedly changing the slope of the current yield curve could cause First Bancshares net interest margins to decrease, subsequently decreasing net interest income. In addition, such changes could adversely affect the valuation of First Bancshares assets and liabilities.

At present First Bancshares one-year interest rate sensitivity position is slightly asset sensitive, but a gradual increase in interest rates during the next twelve months should not have a significant impact on net interest income during that period. However, as with most financial institutions, First Bancshares results of operations are affected by changes in interest rates and First Bancshares ability to manage this risk. The difference between interest rates charged on interest-earning assets and interest rates paid on interest-bearing liabilities may be affected by changes in market interest rates, changes in relationships between interest rate indices, and/or changes in the relationships between long-term and short-term market interest rates. A change in this difference might result in an increase in interest expense relative to interest income, or a decrease in First Bancshares interest rate spread.

*Certain changes in interest rates, inflation, or the financial markets could affect demand for First Bancshares products and First Bancshares ability to deliver products efficiently.*



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Loan originations, and potentially loan revenues, could be adversely impacted by sharply rising interest rates. Conversely, sharply falling rates could increase prepayments within First Bancshares securities portfolio lowering interest earnings from those investments. An unanticipated increase in inflation could cause First Bancshares operating costs related to salaries & benefits, technology, & supplies to increase at a faster pace than revenues.

The fair market value of First Bancshares securities portfolio and the investment income from these securities also fluctuate depending on general economic and market conditions. In addition, actual net investment income and/or cash flows from investments that carry prepayment risk, such as mortgage-backed and other asset-backed securities, may differ from those anticipated at the time of investment as a result of interest rate fluctuations.

*Changes in the policies of monetary authorities and other government action could adversely affect First Bancshares profitability.*

The results of operations of First Bancshares are affected by credit policies of monetary authorities, particularly the Federal Reserve Board. The instruments of monetary policy employed by the Federal Reserve Board include open market operations in U.S. government securities, changes in the discount rate or the federal funds rate on bank borrowings and changes in reserve requirements against bank deposits. In view of changing conditions in the national economy and in the money markets, particularly in light of the continuing threat of terrorist attacks and the current military operations in the Middle East, we cannot predict possible future changes in interest rates, deposit levels, loan demand or First Bancshares business and earnings. Furthermore, the actions of the United States government and other governments in responding to such terrorist attacks or the military operations in the Middle East may result in currency fluctuations, exchange controls, market disruption and other adverse effects.

13

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*Natural disasters could affect First Bancshares ability to operate*

First Bancshares market areas are susceptible to natural disasters such as hurricanes. Natural disasters can disrupt First Bancshares operations, result in damage to properties and negatively affect the local economies in which First Bancshares operates. First Bancshares cannot predict whether or to what extent damage caused by future hurricanes will affect First Bancshares operations or the economies in First Bancshares market areas, but such weather events could cause a decline in loan originations, a decline in the value or destruction of properties securing the loans and an increase in the risk of delinquencies, foreclosures or loan losses.

*Greater loan losses than expected may adversely affect First Bancshares earnings.*

First Bancshares as lender is exposed to the risk that its customers will be unable to repay their loans in accordance with their terms and that any collateral securing the payment of their loans may not be sufficient to assure repayment. Credit losses are inherent in the business of making loans and could have a material adverse effect on First Bancshares operating results. First Bancshares credit risk with respect to its real estate and construction loan portfolio will relate principally to the creditworthiness of corporations and the value of the real estate serving as security for the repayment of loans. First Bancshares credit risk with respect to its commercial and consumer loan portfolio will relate principally to the general creditworthiness of businesses and individuals within First Bancshares local markets.

First Bancshares makes various assumptions and judgments about the collectibility of its loan portfolio and provide an allowance for estimated loan losses based on a number of factors. First Bancshares believes that its current allowance for loan losses is adequate. However, if First Bancshares assumptions or judgments prove to be incorrect, the allowance for loan losses may not be sufficient to cover actual loan losses. First Bancshares may have to increase its allowance in the future in response to the request of one of its primary banking regulators, to adjust for changing conditions and assumptions, or as a result of any deterioration in the quality of First Bancshares loan portfolio. The actual amount of future provisions for loan losses cannot be

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determined at this time and may vary from the amounts of past provisions.

*First Bancshares may need to rely on the financial markets to provide needed capital*

First Bancshares Common Stock is listed and traded on the NASDAQ stock market. Although First Bancshares anticipates that its capital resources will be adequate for the foreseeable future to meet its capital requirements, at times First Bancshares may depend on the liquidity of the NASDAQ stock market to raise equity capital. If the market should fail to operate, or if conditions in the capital markets are adverse, First Bancshares may be constrained in raising capital. Should these risks materialize, First Bancshares ability to further expand its operations through internal growth may be limited.

*First Bancshares is subject to regulation by various Federal and State entities*

First Bancshares is subject to the regulations of the Securities and Exchange Commission ( SEC ), the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the OCC. New regulations issued by these agencies may adversely affect First Bancshares ability to carry on its business activities. First Bancshares is subject to various Federal and state laws and certain changes in these laws and regulations may adversely affect First Bancshares operations.

First Bancshares is also subject to the accounting rules and regulations of the SEC and the Financial Accounting Standards Board. Changes in accounting rules could adversely affect the reported financial statements or results of operations of First Bancshares and may also require extraordinary efforts or additional costs to implement. Any of these laws or regulations may be modified or changed from time to time, and First Bancshares cannot be assured that such modifications or changes will not adversely affect First Bancshares.

14

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*First Bancshares engages in acquisitions of other businesses from time to time.*

On occasion, First Bancshares will engage in acquisitions of other businesses. Acquisitions may result in customer and employee turnover, thus increasing the cost of operating the new businesses. The acquired companies may also have legal contingencies, beyond those that First Bancshares is aware of, that could result in unexpected costs.

*First Bancshares is subject to industry competition which may have an impact upon its success.*

The profitability of First Bancshares depends on its ability to compete successfully. First Bancshares operates in a highly competitive financial services environment. Certain competitors are larger and may have more resources than First Bancshares does. First Bancshares faces competition in its regional market areas from other commercial banks, savings and loan associations, credit unions, internet banks, finance companies, mutual funds, insurance companies, brokerage and investment banking firms, and other financial intermediaries that offer similar services. Some of First Bancshares nonbank competitors are not subject to the same extensive regulations that govern First Bancshares or the Bank and may have greater flexibility in competing for business.

Another competitive factor is that the financial services market, including banking services, is undergoing rapid changes with frequent introductions of new technology-driven products and services. First Bancshares future success may depend, in part, on its ability to use technology competitively to provide products and services that provide convenience to customers and create additional efficiencies in First Bancshares operations.

*Future issuances of additional securities could result in dilution of shareholders ownership.*

First Bancshares may determine from time to time to issue additional securities to raise additional capital, support growth, or to make acquisitions. Further, First Bancshares may issue

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stock options or other stock grants to retain and motivate First Bancshares employees. Such issuances of Company securities will dilute the ownership interests of First Bancshares shareholders.

*Anti-takeover laws and certain agreements and charter provisions may adversely affect share value.*

Certain provisions of state and federal law and First Bancshares articles of incorporation may make it more difficult for someone to acquire control of First Bancshares. Under federal law, subject to certain exemptions, a person, entity, or group must notify the federal banking agencies before acquiring 10% or more of the outstanding voting stock of a bank holding company, including First Bancshares shares. Banking agencies review the acquisition to determine if it will result in a change of control. The banking agencies have 60 days to act on the notice, and take into account several factors, including the resources of the acquiror and the antitrust effects of the acquisition. There also are Mississippi statutory provisions and provisions in First Bancshares articles of incorporation that may be used to delay or block a takeover attempt. As a result, these statutory provisions and provisions in First Bancshares articles of incorporation could result in First Bancshares being less attractive to a potential acquiror.

*Securities issued by First Bancshares, including First Bancshares Common Stock, are not FDIC insured.*

Securities issued by First Bancshares, including First Bancshares Common Stock, are not savings or deposit accounts or other obligations of any bank and are not insured by the FDIC, the Deposit Insurance Fund, or any other governmental agency or instrumentality, or any private insurer, and are subject to investment risk, including the possible loss of principal.

15

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*There can be no assurance that recently enacted legislation will stabilize the U.S. financial system.*

On October 3, 2008, President Bush signed into law the EESA. The legislation was the result of a proposal by the Treasury in response to the financial crises affecting the banking system and financial markets and threats to investment banks and other financial institutions. Pursuant to the EESA, the Treasury has the authority to, among other things, purchase up to \$700 billion of mortgages, mortgage-backed securities and certain other financial instruments from financial institutions for the purpose of stabilizing and providing liquidity to the U.S. financial markets. On October 14, 2008, the Treasury announced the Capital Purchase Program, a program under the EESA pursuant to which it would purchase senior preferred stock and warrants to purchase common stock from participating financial institutions. On November 21, 2008, the FDIC adopted a Final rule with respect to its Temporary Liquidity Guarantee Program pursuant to which the FDIC will guarantee certain newly-issued unsecured debt of banks and certain holding companies and also guarantee, on an unlimited basis, noninterest-bearing bank transaction accounts. On February 17, 2009, President Obama signed into law the ARRA. The purposes of the legislation are to preserve and create jobs, to assist those most impacted by the recession, to provide investments to increase economic efficiency in health services, to invest in transportation, environmental protection and other infrastructure, and to stabilize local and state governments.

Each of these programs was implemented to help stabilize our economy and financial system. There can be no assurance, however, as to the actual impact that the EESA and its implementing regulations, the Capital Purchase Program, the FDIC programs, or any other governmental program will have on the financial markets. The failure of the EESA, the ARRA or the U.S. government to stabilize the financial markets and a continuation or worsening of current financial market conditions could materially and adversely affect the Company's business, financial condition, and results of operations, access to credit or the trading price of the Company's common stock.

*The failure of other financial institutions could adversely affect the Company.*

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The Company's ability to engage in routine funding transactions could be adversely affected by the actions and potential failures of other financial institutions. Financial institutions are interrelated as a result of trading, clearing, counterparty and other relationships. As a result, defaults by, or even rumors or concerns about, one or more financial institutions or the financial services industry generally have led to market-wide liquidity problems and could lead to losses or defaults by the Company or by other institutions.

*Concern by customers over deposit insurance may cause a decrease in deposits and changes in the mix of funding sources available to the Company.*

With recent increased concerns about bank failures, customers increasingly are concerned about the extent to which their deposits are insured by the FDIC. Customers may withdraw deposits in an effort to ensure that the amount they have on deposit with their bank is fully insured and some may seek deposit products or other bank savings and investment products that are collateralized. Decreases in deposits and changes in the mix of funding sources may adversely affect the Company's funding costs and net income.

*As a result of the Company's participation in the Capital Purchase Program (CPP), the Company may face additional regulation and cannot predict the cost or effects of compliance at this time.*

In connections with the Company's participation in the CPP, the Company and the Bank may face additional regulations and/or reporting requirements, including, but not limited to, the following:

- o Section 5.3 of the standardized Securities Purchase Agreement that the Company provides, in part, that the Treasury "may unilaterally amend any provision of the Agreement required to comply with any changes after the Signing Date in applicable federal law. The Treasury could give Congress the ability to impose "after-the-fact" terms and conditions on the Agreement. As a participant in the CPP, the Company would be subject to any such retroactive regulation. The Company cannot predict whether or in what form any proposed regulation or statute will be enacted or the extent to which its business may be affected by any new regulation or statute.
- o Most recently, the ARRA included additional restrictions on the operations of banks that do not participate in the various TARP programs. Because some of these restrictions are retroactive, ARRA also provided the opportunity for recipients of funds under the TARP to not participate in the CPP. At this time, the conditions of its participation are not yet final and there are additional regulations that may be taken in connection with ARRA and the CPP, the Company has not yet made a decision to continue its participation in the CPP.

16

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### **ITEM 1B. UNRESOLVED STAFF COMMENTS**

The Company is currently in correspondence with the SEC concerning additional disclosures. The additional disclosures are included in the 2008 Annual Report.

### **ITEM 2. PROPERTIES**

The First has a main office located west of the city of Hattiesburg, Mississippi, in Lamar County. The main office is located in a 13,000 square foot facility which the Company constructed and opened in January 1997 on a two acre plot of land at the southwest corner of U.S. Highway 98 and Old Highway 11. The First also has a branch office located on Highway 15 North in the city of Laurel, Mississippi, one on Highway 589 in the city of Purvis, Mississippi, which is in Lamar County, a fourth office in a 3,300 square foot facility located at the intersection of Lincoln Road and South 28th Avenue in Hattiesburg, a fifth office located in an 11,700 square foot building located at 110 S. 40th Ave. in Hattiesburg, a sixth office located

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on Hwy 43 South, Picayune, MS in a 3,800 sq. ft. facility , a seventh office located at 1126 Jackson Ave in Pascagoula, MS, an eighth office located at Hwy 90 in Bay St. Louis, MS, a ninth location on Border Ave. in Wiggins, MS, as well as a tenth location located at Hwy 49 and O Neal Rd. in Gulfport, MS.

The Company believes that the Bank s facilities will adequately serve their needs.

### **ITEM 3. LEGAL PROCEEDINGS.**

From time to time the Company and/or the Bank may be named as defendants in various lawsuits arising out of the normal course of business. On October 8, 2007 The First Bancshares, Inc. (the Company ) and its subsidiary, The First, A National Banking Association (the Bank ) were formally named as defendants and served with a First Amended Complaint in litigation styled Nick D. Welch v. Oak Grove Land Company, Inc., Fred McMurry, David E. Johnson, J. Douglas Seidenburg, The First, a National Banking Association, The First Bancshares, Inc., and John Does 1 through 10, Civil Action No. 2006-236-CV4, pending in the Circuit Court of Jones County, Mississippi, Second Judicial District (the First Amended Complaint ).

The allegations by Welch against the Company and the Bank include counts of 1) Intentional Misrepresentation and Omission; 2) Negligent Misrepresentation and/or Omission; 3) Breach of Fiduciary Duty; 4) Breach of Duty of Good Faith and Fair Dealing; and 5) Civil Conspiracy. The First Amended Complaint served by Welch on October 8, 2007 added the Company and the Bank as defendants in this ongoing litigation. The First Amended Complaint seeks damages from all the defendants, including \$2,420,775.00, annual dividends for the year 2006 in the amount of \$.30 per share, punitive damages, and attorneys fees and costs, and is more fully described in Form 8-K filed by the Company on October 10, 2007. Each of the Company and the Bank deny any liability to Welch, and they intend to defend vigorously against this lawsuit.

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

No matter was submitted to a vote of security holders during the fourth quarter of the fiscal year covered by this report.

## **PART II**

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

In response to this Item, the information contained on page 56 of the Company s Annual Report to Shareholders for the year ended December 31, 2008, is incorporated herein by reference.

17

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### **ITEM 6. SELECTED FINANCIAL DATA**

In response to this Item, the information contained on page 7 of Management s Discussion and Analysis for the year ended December 31, 2008, is incorporated herein by reference.

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

In response to this Item, the information contained on pages 6 through 26 of the Company s Annual Report to Shareholders for the year ended December 31, 2008, is incorporated herein by reference.

### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Not applicable.

**ITEM 8. FINANCIAL STATEMENTS.**

In response to this Item, the information contained on pages 28 through 32 of the Company's Annual Report to Shareholders for the year ended December 31, 2008, is incorporated herein by reference.

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

Not applicable.

**ITEM 9A(T). CONTROLS AND PROCEDURES**

The Company's principal executive officer and principal financial officer have concluded, based upon their evaluation of the Company's disclosure controls and procedures as of December 31, 2008, that the Company's disclosure controls and procedures were effective. During the quarter ended December 31, 2008, no changes have occurred in the Company's internal control over financial reporting that have materially affected or are reasonably likely to materially affect the Company's internal control over financial reporting.

**The First Bancshares, Inc.  
Management's Report on Internal Control Over Financial Reporting**

Management of The First Bancshares, Inc. and subsidiary (the Company) is responsible for establishing and maintaining effective internal control over financial reporting. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles.

Under the supervision and with the participation of management, including the principal executive officer and principal financial officer, the Company conducted an evaluation of the effectiveness of internal control over financial reporting based on the framework in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management of the Company has concluded the Company maintained effective internal control over financial reporting, as such term is defined in Securities Exchange Act of 1934 Rules 12a-15(f), as of December 31, 2008.

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting can also be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. These inherent limitations, however, are known features of the financial reporting process. It is possible, therefore, to design into the process safeguards to reduce, though not eliminate, this risk.

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This annual report does not include an attestation report of the Company's independent registered public accounting firm regarding internal control over financial reporting. The Company's registered public accounting firm was not required to issue an attestation report on internal controls over financial reporting pursuant to temporary rules of the Securities and Exchange Commission.

/s/ David E. Johnson

/s/ Dee Dee Lowery

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Chairman of the Board and CEO  
March 26, 2009

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Executive VP and Chief Financial Officer  
March 26, 2009

**ITEM 9B. OTHER INFORMATION**

Not applicable.

**PART III**

**ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT**

In response to this Item, the information contained under the captions, Election of Directors and Additional Information Concerning Directors and Officers of the Company's Proxy Statement for the Annual Meeting of Shareholders to be held on May 21, 2009, is incorporated herein by reference.

*Code of Ethics*

The Company's Board of Directors has adopted a Code of Ethics that applies to the Company's principal executive officer, principal financial officer, principal accounting officer, or persons performing similar functions. A copy of this Code of Ethics can be found at the Company's internet website at [www.thefirstbank.com](http://www.thefirstbank.com). The Company intends to disclose any amendments to its Code of Ethics, and any waiver from a provision of the Code of Ethics granted to the Company's principal executive officer, principal financial officer, principal accounting officer, or persons performing similar functions, on the Company's internet website within five business days following such amendment or waiver. The information contained on or connected to the Company's internet website is not incorporated by reference into this Form 10-K and should not be considered part of this or any other report that we file with or furnish to the SEC.

*Audit Committee*

The information contained under the caption Committees of the Board of Directors of the Company's Proxy Statement for the Annual Meeting of Shareholders to be held on May 21, 2009, is incorporated herein by reference. The Board of Directors has determined that there is at least one independent audit committee financial expert, J. Douglas Seidenburg, serving on the Audit Committee, as the terms independent and audit committee financial expert are used in pertinent Securities and Exchange Commission laws and regulations.

*Corporate Governance*

The information contained under the caption Additional Information Concerning Directors and Officers of the Company's Proxy Statement for the Annual Meeting of Shareholders to be held on May 21, 2009, is incorporated herein by reference.

19

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**ITEM 11. EXECUTIVE COMPENSATION.**

In response to this Item, the information contained under the caption Compensation Discussion and Analysis of the Company's Proxy Statement for the Annual Meeting of Shareholders to be held on May 21, 2009, is incorporated herein by reference.

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

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In response to this Item, the information contained under the caption Security Ownership of Certain Beneficial Owners and Management of the Company s Proxy Statement for the Annual Meeting of Shareholders to be held on May 21, 2009, is incorporated herein by reference.

### ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

In response to this Item, the information contained under the caption Certain Relationships and Related Transactions of the Company s Proxy Statement for the Annual Meeting of Shareholders to be held on May 21, 2009, is incorporated herein by reference.

### ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES.

In response to this Item, the information contained under the caption Principal Accountant Fees and Services of the Company s Proxy Statement for the Annual meeting of Shareholders to be held on May 21, 2009, is incorporated herein by reference.

## PART IV

### ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

The following exhibits are furnished (or incorporated by reference):

| Exhibit Number | Description  |
|----------------|--|
| 3.1            | Amended and Restated Articles of Incorporation (incorporated by reference to the Company's Registration Statement No. 33-94288 on Form S-1).   |
| 3.2            | Bylaws (incorporated by reference to Exhibit 3.2 to the Company's Registration Statement No. 33-94288 on Form S-1).  |
| 4.1            | Provisions in the Company's Articles of Incorporation and Bylaws defining the Company's Common Stock (incorporated by reference to Exhibit 4.1 to the Company's Registration Statement No. 33-94288 on Form S-1).                                      |
| 4.2            | Form of Certificate of Common Stock (incorporated by reference to Exhibit 4.2 to the Company's Registration Statement No. 33-94288 on Form S-1).   |
| 10.5           | Amended and restated employment agreement dated November 20, 1995, by and between the Company and the Company (incorporated by reference to Exhibit 10.7 of the Company's Form 10-KSB for the fiscal year ended December 31, 1995, File No. 33-94288). |
| 10.6           | First Bancshares, Inc. 1997 Stock Option Plan as of March 18, 1997 (incorporated by reference to Exhibit 10.7 of the Company's Form 10-KSB for the fiscal year ended December 31, 1995, File No. 33-94288).  |
| 10.7           | Agreement to Repurchase Stock by and among The First Bancshares, Inc., Johnson (incorporated by reference to Exhibit 10.9 to the Company's Form 10-KSB for the fiscal year ended December 31, 1995, File No. 33-94288).                                |
| 13             | The Company's 2008 Annual Report   |
| 21             | Subsidiaries of the Company  |
| 23             | Consent of Independent Registered Public Accounting Firm   |
| 31             | Rule 13a-14(a)/15d-14(a) Certifications  |



**SIGNATURES**

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

THE FIRST BANCSHARES, INC.

Date: March 26, 2009

By: /s/ David E. Johnson

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 David E. Johnson  
 Chief Executive Officer (Principal Executive Officer)

Date: March 26, 2009

By: /s/ Dee Dee Lowery

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 Dee Dee Lowery  
 Executive VP and Chief Financial Officer (Principal Financial and Principal Accounting Officer)

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

**SIGNATURES**

**CAPACITIES**

-----  
 /s/ E. Ricky Gibson

Director

March 26, 2009

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 /s/ Charles R. Lightsey

Director

March 26, 2009

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 /s/ Ralph T. Simmons

Director

March 26, 2009

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 /s/ J. Douglas Seidenburg

Director

March 26, 2009

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 /s/ Andy Stetelman

Director

March 26, 2009

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 David W. Bomboy

Director

March 26, 2009

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 /s/ Ted E. Parker

Director

March 26, 2009

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 /s/ Michael W. Chancellor

Director

March 26, 2009

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 /s/ Fred McMurry

Director

March 26, 2009

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|                                       |   |       |
|---------------------------------------|---|-------|
| Dennis L. Pierce<br>-----             | Director  | Marco |
| /s/ Gregory Mitchell<br>-----         | Director  | Marco |
| /s/ M. Ray "Hoppy" Cole, Jr.<br>----- | President and Director  | Marco |
| /s/ David E. Johnson<br>-----         | CEO and Director<br>(Principal Executive Officer)   | Marco |
| /s/ Dee Dee Lowery<br>-----           | Executive VP & Chief Financial Officer<br>(Principal Financial and<br>Accounting Officer) | Marco |