HomeTown Bankshares Corp
Form 10-Q
November 15, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x **Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended September 30, 2010.**

Or

¨ **Transition Report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934 for the transition period from ______ to ______.**

Commission File Number: 333-158525

HOMETOWN BANKSHARES CORPORATION

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

Virginia	**26-4549960**
(State or other jurisdiction of Incorporation or organization)	**(I.R.S. Employer Identification No.)**
202 South Jefferson Street,	
Roanoke, Virginia	**24011**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number: (540) 345-6000

(Former name, former address, and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the past 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 ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨ (do not check if a smaller reporting company)	Smaller reporting company x

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

State the number of shares outstanding of each of the issuer s classes of common equity, as of the latest practicable

date:

As of November 15, 2010, 3,241,547 shares of common stock, par value $5.00 per share, of the issuer were outstanding.

HOMETOWN BANKSHARES CORPORATION

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PART 1. FINANCIAL INFORMATION

All schedules have been omitted because they are inapplicable or the required information is provided in the financial statements, including the notes thereto.

HOMETOWN BANKSHARES CORPORATION

Consolidated Balance Sheets

September 30, 2010 and December 31, 2009

In Thousands, Except Share and Per Share Data	Unaudited **September 30, 2010**	**December 31, 2009**
Assets		
Cash and due from banks	$ 12,194	$ 7,051
Federal funds sold	10,455	19,908
Securities available for sale, at fair value	52,145	46,353
Restricted equity securities	2,687	2,547
Loans, net of allowance for loan losses of $4,204 in 2010 and $2,862 in 2009	261,436	249,807
Property and equipment, net	8,858	8,197
Other real estate owned	2,352	707
Accrued income	1,194	1,099
Prepaid FDIC insurance	1,243	1,606
Other assets	744	533
Total assets	$ 353,308	$ 337,808
Liabilities and Stockholders Equity		
Deposits:		
Noninterest-bearing	$ 18,121	$ 20,525
Interest-bearing	274,299	251,124
Total deposits	292,420	271,649
Short term borrowings	681	714
Federal Home Loan Bank borrowings	25,950	30,200
Accrued interest payable	746	1,068
Other liabilities	813	397
Total liabilities	320,610	304,028
Commitments and contingencies		
Stockholders equity		
Preferred stock, $1,000 par value; 10,000 shares of series A and 374 shares of series B authorized, issued and outstanding at September 30, 2010	10,374	10,374
Discount on preferred stock	(304)	(355)
Common stock, $5 par value; authorized 10,000,000 shares, issued and outstanding 3,241,547 in 2010 and 2,939,400 in 2009 (includes 8,207 of restricted shares in 2010)	16,167	14,697
Surplus	15,426	16,856
Retained deficit	(9,836)	(7,414)

Accumulated other comprehensive income (loss)	871	(378)
Total stockholders equity	32,698	33,780
Total liabilities and stockholders equity	$ 353,308	$ 337,808

See Notes to Consolidated Financial Statements

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HOMETOWN BANKSHARES CORPORATION

Consolidated Statements of Operations

For the three and nine months ended September 30, 2010 and 2009

In Thousands, Except Share and Per Share Data	For the Three Months Ended September 30, 2010 (Unaudited)	For the Three Months Ended September 30, 2009 (Unaudited)	For the Nine Months Ended September 30, 2010 (Unaudited)	For the Nine Months Ended September 30, 2009 (Unaudited)
Interest income:				
Loans and fees on loans	$ 3,690	$ 3,399	$ 10,695	$ 9,515
Federal funds sold	10	9	30	13
Taxable investment securities	431	182	1,375	421
Total interest income	4,131	3,590	12,100	9,949
Interest expense:				
Deposits	1,199	1,366	3,735	3,964
Other borrowed funds	139	131	421	414
Total interest expense	1,338	1,497	4,156	4,378
Net interest income	2,793	2,093	7,944	5,571
Provision for loan losses	441	182	4,128	386
Net interest income after provision for loan losses	2,352	1,911	3,816	5,185
Noninterest income:				
Service charges on deposit accounts	114	124	360	308
Mortgage loan brokerage fees	72	37	119	109
Rental income	31	21	92	75
Gain on sale of other real estate			77	
Gain on sale of investment securities				160
Other income	18	13	49	24
Total noninterest income	235	195	697	676
Noninterest expense:				
Salaries and employee benefits	1,214	1,058	3,446	2,916
Occupancy and equipment expense	338	318	958	933
Data processing expense	111	85	330	264

Advertising and marketing expense		64		85		297		218
Professional fees		102		56		302		148
FDIC insurance assessment		129		104		389		352
Loss on disposal of interest in title agency								44
Other expense		319		245		896		686
Total noninterest expense		2,277		1,951		6,618		5,561
Net income (loss) before income taxes		310		155		(2,105)		300
Income tax expense								
Net income (loss)		310		155		(2,105)		300
Dividends accumulated on preferred stock		134		19		400		19
Accretion of discount on preferred stock		16		3		51		3
Net income (loss) available to common shareholders	$	160	$	133	$	(2,556)	$	278
Income (loss) per common share, basic and diluted	$	0.05	$	0.04	$	(0.79)	$	0.09
Weighted average common shares outstanding		3,241,547		3,233,340		3,239,773		3,233,340

See Notes to Consolidated Financial Statements

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HOMETOWN BANKSHARES CORPORATION

Consolidated Statements of Cash Flows

Nine months ended September 30, 2010 and 2009

In Thousands	Unaudited **September 30, 2010**	Unaudited **September 30, 2009**
Cash flows from operating activities:		
Net (loss) income	$ (2,105)	$ 300
Adjustments to reconcile net (loss) income to net cash provided by operations:		
Depreciation and amortization	465	438
Provision for loan losses	4,128	386
Amortization of premium on securities, net	212	3
Gain on sale of other real estate	(77)	
Gain on sale of investment securities, net		(160)
Stock compensation expense	40	25
Changes in assets and liabilities:		
Accrued income	(95)	(277)
Other assets	(1,759)	117
Accrued interest payable	(322)	30
Other liabilities	416	(191)
Net cash flows provided by operating activities	903	671
Cash flows from investing activities:		
Net decrease (increase) in federal funds sold	9,453	(22,945)
Purchases of available for sale securities	(24,683)	(13,027)
Maturities of available for sale securities	19,928	2,117
Purchase of restricted equity securities, net	(140)	(204)
Net increase in loans	(15,757)	(37,479)
Proceeds from sale of other real estate	344	
Purchases of property and equipment	(1,126)	(155)
Net cash flows used in investing activities	(11,981)	(71,693)
Cash flows from financing activities:		
Net (decrease) increase in noninterest-bearing deposits	(2,404)	3,679
Net increase in interest-bearing deposits	23,175	66,034
Net (decrease) increase in short-term borrowings	(33)	104
Net decrease in long-term FHLB borrowings	(4,250)	(5,200)
Preferred stock dividend payment	(267)	
Issuance of preferred stock, net of issuance costs		9,799
Net cash flows provided by financing activities	16,221	74,416

Net increase in cash and cash equivalents		5,143		3,394
Cash and cash equivalents, beginning		7,051		3,186
Cash and cash equivalents, ending	$	12,194	$	6,580
Supplemental disclosure of cash flow information:				
Cash payments for interest	$	4,478	$	4,348
Cash payments for income taxes	$		$	
Supplemental disclosure of noncash investing activities:				
Unrealized gain (loss) on securities available for sale	$	1,249	$	(382)
Transfer from loans to other real estate	$	1,835	$	256

See Notes to Consolidated Financial Statements

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Notes to Consolidated Financial Statements

Note 1. Organization and Summary of Significant Accounting Policies

Organization

On September 4, 2009, Hometown Bankshares Corporation (the Company) acquired all outstanding stock of Hometown Bank (the Bank) in an exchange for shares of the Registrant on a one-for-one basis to become a single-bank holding company with the Bank becoming a wholly-owned subsidiary. The Bank was organized and incorporated under the laws of the State of Virginia on November 9, 2004 and commenced operations on November 14, 2005. The Bank currently serves Roanoke City, Virginia, the County of Roanoke, Virginia, the City of Salem, Virginia, Christiansburg, Virginia, and surrounding areas. As a state chartered bank which is a member of the Federal Reserve System, the Bank is subject to regulation by the Virginia Bureau of Financial Institutions, the Federal Deposit Insurance Corporation and the Federal Reserve Board.

Basis of Presentation

The consolidated financial statements as of September 30, 2010 and for the periods ended September 30, 2010 and 2009 included herein, have been prepared by HomeTown Bankshares Corporation, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, the information furnished in the interim consolidated financial statements reflects all adjustments necessary to present fairly the Company s financial position, results of operations and cash flows for such interim periods. Management believes that all interim period adjustments are of a normal recurring nature. These consolidated financial statements should be read in conjunction with the Company s audited financial statements and the notes thereto as of December 31, 2009, included in the Company s Form 10-K for the year ended December 31, 2009. Interim results are not necessarily indicative of 2010 year end results.

The accounting and reporting policies of the Company follow generally accepted accounting principles and general practices within the financial services industry.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary HomeTown Bank. All significant intercompany accounts and transactions associated with the Company s wholly-owned subsidiary have been eliminated.

Our accounting policies and basic principles have not changed since the summary disclosure of these in our Annual Report on Form 10-K. Please refer to the Form 10-K for these policies.

On May 18, 2010, the Company declared a 10% stock split, whereby each stockholder received one additional share for each ten shares owned. The shares were distributed on July 19, 2010 to stockholders of record at the close of business on June 18, 2010. All applicable share and per-share amounts in the consolidated financial statements and related disclosures have been retroactively adjusted to reflect this stock dividend.

Note 2. Investment Securities

The amortized cost and fair value of securities available for sale as of September 30, 2010 and December 31, 2009, are as follows:

	September 30, 2010			
(Dollars In Thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U. S. Government agency securities	$ 21,119	$ 533	$ (3)	$ 21,649
Mortgage backed securities	29,081	358	(8)	29,431
Municipal securities	1,074		(9)	$ 1,065
	$ 51,274	$ 891	$ (20)	$ 52,145

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(Dollars In Thousands)	December 31, 2009 Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U. S. Government agency securities	$ 21,444	$ 71	$ (203)	$ 21,312
Mortgage backed securities	25,287		(246)	25,041
	$ 46,731	$ 71	$ (449)	$ 46,353

As of September 30, 2010, there were no individual securities that had been in a continuous loss position for more than 12 months.

The following table demonstrates the unrealized loss position of securities available for sale at September 30, 2010.

	September 30, 2010					
	Less than 12 months		12 months or more		Total	
(Dollars In Thousands)	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
U. S. Government agency securities	$ 1,646	$ (3)	$	$	$ 1,646	$ (3)
Mortgage backed securities	1,917	(8)			1,917	(8)
Municipal securities	1,065	(9)			1,065	(9)
	$ 4,628	$ (20)	$	$	$ 4,628	$ (20)

All bonds are considered AAA rated government or government-sponsored agency bonds. The Company has adopted ASC 320-10-65 (formerly FAS 115-2 and FAS 124-2) Recognition and Presentation of Other-Than-Temporary Impairment that amended other-than-temporary impairment (OTTI) guidance for debt securities regarding recognition and disclosure. The major change in the guidance was that an impairment is other-than-temporary if any of the following conditions exists: the entity intends to sell the security; it is more likely than not that the entity will be required to sell the security before recovery of its amortized cost basis; or, the entity does not expect to recover the security s entire amortized cost basis (even if the entity does not intend to sell). If a credit loss exists, but an entity does not intend to sell the impaired debt security and is not more likely than not to be required to sell before recovery, the impairment is other-than-temporary and should be separated into a credit portion to be recognized in earnings and the remaining amount relating to all other factors recognized as other comprehensive loss.

At September 30, 2010, the Bank does not consider any bond in an unrealized loss position to be other than temporarily impaired.

The bank had no realized gain or loss on sale of securities in the first nine months of 2010 and a $160 thousand realized gain on sale of its available for sale securities for the nine months ended September 30, 2009.

The amortized cost and estimated fair values of investment securities available for sale at September 30, 2010 are as follows:

(Dollars In Thousands)	Amortized Cost	Estimated Fair Value
Over five through ten years	$ 14,981	$ 15,460
Greater than 10 years	36,293	36,685
	$ 51,274	$ 52,145

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Note 3. Loans Receivable

The major components of loans in the balance sheets at September 30, 2010 and December 31, 2009 are as follows:

(In Thousands)	2010	2009
Loans secured by real estate:		
Construction and land development	$ 36,467	$ 46,157
Secured by 1-4 family residential	68,012	53,662
Nonfarm, non 1-4 family residential	122,696	112,174
Loans to farmers	344	370
Commercial loans	32,814	34,849
Loans to individuals	5,307	5,457
Total Loans	265,640	252,669
Less: Allowance for loan losses	4,204	2,862
Loans, net	$ 261,436	$ 249,807

Note 4. Allowance for Loans Losses

Changes in the allowance for loan losses are as follows:

(Dollars In Thousands)	Nine Months Ended September 30, 2010	Year Ended December 31, 2009
Balance, beginning	$ 2,862	$ 2,862
Provision charged to operating expense	4,128	725
Recoveries of amounts charged off	1	9
Loans charged off	(2,787)	(734)
Balance, ending	$ 4,204	$ 2,862
Ratio of net charge-offs to average loans, annualized	1.42%	0.31%
Ratio of allowance for loan losses to loans	1.58%	1.13%

(Dollars In Thousands)	Nine Months Ended September 30, 2010	Year Ended December 31, 2009
Impaired loans without a valuation allowance	$ 22,018	$ 16,095
Impaired loans with a valuation allowance	6,292	4,682
Total impaired loans	$ 28,310	$ 20,777
Valuation allowance related to impaired loans	$ 924	$ 538

Total non-accrual loans	4,949	3,925
Total loans past-due ninety days or more and still accruing interest	1,317	553

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(Dollars In Thousands)	Nine Months Ended September 30, 2010	Year Ended December 31, 2009
Average investment in impaired loans	$ 22,996	$ 7,064
Interest income recognized on impaired loans	$ 747	$ 344
Interest income recognized on a cash basis on impaired loans	$ 747	$ 344

Note 5. Stock Based Compensation

The Company has a 2005 Stock Option Plan (the Plan) pursuant to which the Company s Board of Directors may grant stock options to directors, officers and employees. The Plan authorizes grants of options to purchase up to 550,000 shares of the Company s authorized but unissued common stock. Accordingly, options for the purchase of 492,360 shares of authorized common stock have been issued under the Plan and 57,640 shares of authorized common stock are available for issue under the Plan. There are options for 492,360 shares granted currently outstanding as of September 30, 2010, of which, 478,951 options are vested. All stock options have been granted with an exercise price equal to the stock s fair market value at the date of the grant. As of September 30, 2010, no options have been exercised and no options were granted in 2010. The Company recorded compensation expense of $40 thousand for the nine months ended September 30, 2010 and $25 thousand for the same period in 2009. The aggregate intrinsic value of outstanding stock options was $0 at September 30, 2010. The weighted average remaining contractual term of outstanding options was 5.8 years at September 30, 2010.

The Board of Directors adopted a Restricted Stock Plan (the Plan) in September 2009 whereby 132,000 shares of the Company s authorized but unissued common stock was set aside to be granted by the Board of Directors in its discretion. The principal purpose of the Plan was to make shares available for issue to the executive officers of the Company and the Bank in payment of incentives earned under the Incentive Compensation Plan. Because the Company is a TARP participant, the Company s most highly paid employee cannot be paid a cash bonus. However, the Treasury regulations permit payment of such a bonus in restricted stock. Even though the restriction would only apply to the CEO in the case of the Company and the Bank, each of the executive officers of the Company and the Bank have elected to take their bonuses in stock rather than cash.

The restrictions attached to stock issued under the Plan restrict transfer of the shares on a graduated scale during the time TARP funding is outstanding and provide for vesting over a five-year period. During the first quarter of 2010, the Company issued 8,207 shares of stock under the Plan.

The remaining unamortized compensation expense for stock options and restricted stock was $162 thousand at September 30, 2010 and will be recognized over the next 4 years.

All share amounts have been restated to reflect the stock split.

Note 6. Fair Value Measurement

The Company uses a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company s market assumptions. The three levels of the fair value hierarchy based on these two types of inputs are as follows:

Level 1- Valuation is based on quoted prices in active markets for identical assets and liabilities.

Level 2- Valuation is based on observable inputs including quoted prices in active markets for similar assets and liabilities, quoted prices for identical or similar assets and liabilities in less active markets, and model-based valuation techniques for which significant assumptions can be derived primarily from or corroborated by observable data in the market.

Level 3- Valuation is based on model-based techniques that use one or more significant inputs or assumptions that are unobservable in the market.

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The following describes the valuation techniques used by the Company to measure certain financial assets and liabilities recorded at fair value on a recurring basis in the financial statements:

Securities available for sale: Securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are derived primarily from or corroborated by observable market data. Third party vendors compile prices from various sources and may determine the fair value of identical or similar securities by using pricing models that considers observable market data (Level 2).

Derivative assets: Derivative assets are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are derived primarily from or corroborated by observable market data. Third party vendors compile prices from various sources and may determine the fair value of identical or similar assets by using pricing models that considers observable market data (Level 2).

Derivative liabilities: Derivative liabilities are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are derived primarily from or corroborated by observable market data. Third party vendors compile prices from various sources and may determine the fair value of identical or similar liabilities by using pricing models that considers observable market data (Level 2).

The following table presents the balances of financial assets and liabilities measured at fair value on a recurring basis as of September 30, 2010 and December 31, 2009:

		Carrying value at September 30, 2010		
Description	Balance as of Sept. 30, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Available for sale securities	$ 52,145		$ 52,145	
Interest rate swap agreements	348		348	
Liabilities:				
Interest rate swap agreements	$ 348		$ 348	

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Description	Balance as of December 31, 2009	Carrying value at December 31, 2009 Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Available for sale securities	$ 46,353		$ 46,353	
Interest rate swap agreements	274		274	
Liabilities:				
Interest rate swap agreements	$ 274		$ 274	

Certain assets are measured at fair value on a nonrecurring basis in accordance with GAAP. Adjustments to the fair value of these assets usually result from the application of lower-of-cost-or-market accounting or writedowns of individual assets.

The following describes the valuation techniques used by the Company to measure certain assets recorded at fair value on a nonrecurring basis in the financial statements:

Impaired Loans: Loans are designated as impaired when, in the judgment of management based on current information and events, it is probable that all amounts due according to the contractual terms of the loan agreement will not be collected. The measurement of loss associated with impaired loans can be based on either the observable market price of the loan or the fair value of the collateral. Fair value is measured based on the value of the collateral securing the loans. Collateral may be in the form of real estate or business assets including equipment, inventory, and accounts receivable. The vast majority of the collateral is real estate. The value of real estate collateral is determined utilizing an income or market valuation approach based on an appraisal conducted by an independent, licensed appraiser outside of the Company using observable market data (Level 2). However, if the collateral is a house or building in the process of construction or if an appraisal of the real estate property is over two years old, then the fair value is considered Level 3. The value of business equipment is based upon an outside appraisal if deemed significant, or the net book value on the applicable business financial statements if not considered significant using observable market data. Likewise, values for inventory and accounts receivables collateral are based on financial statement balances or aging reports (Level 3). Impaired loans allocated to the Allowance for Loan Losses are measured at fair value on a nonrecurring basis. Any fair value adjustments are recorded in the period incurred as provision for loan losses on the Statements of Operations.

Other Real Estate Owned (OREO): Foreclosed assets are adjusted to fair value upon transfer of the loans to OREO. Subsequently, OREO is carried at the lower of carrying value or fair market value less selling costs. Fair value is based upon independent market prices, appraised values of the collateral or management s estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Corporation records the OREO as nonrecurring Level 2. When the appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Corporation records the OREO as nonrecurring Level 3.

The following table summarizes the Company s assets that were measured at fair value on a nonrecurring basis as of September 30, 2010 and December 31, 2009.

Description	Balance as of Sept. 30, 2010	Carrying value at September 30, 2010 Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)

Assets:				
Impaired Loans, net	$	5,368	$	5,368
Other real estate owned	$	2,352	$	2,352

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Description	Balance as of December 31, 2009	Carrying value at December 31, 2009 Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Impaired Loans, net	$ 4,144		$ 4,144	
Other real estate owned	$ 707		$ 707	

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments:

Cash and due from banks: The carrying amounts reported in the balance sheet for cash and due from banks approximate their fair values.

Federal funds sold: Federal funds sold consist of overnight loans to other financial institutions and mature within one to three days. Management believes the carrying value of federal funds sold approximates estimated market value.

Available-for-sale and restricted equity securities: Fair values for securities, excluding restricted equity securities, are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments. The carrying values of restricted equity securities approximate fair values, based on the redemption provisions of the entities.

Loans receivable: For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying amounts. The fair values for other loans are estimated using discounted cash flow analysis, based on interest rates currently being offered for loans with similar terms to borrowers of similar credit quality.

Deposit liabilities: The fair values disclosed for demand and savings deposits are, by definition, equal to the amount payable on demand at the reporting date. The fair values for certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates of deposit to a schedule of aggregated contractual maturities on such time deposits.

Short term borrowings: Short term borrowings consist of overnight borrowings and mature within one to three days.

Management believes the carrying value of securities sold under agreements to repurchase approximates estimated market value.

FHLB borrowings: The fair values for long term borrowings are estimated using a discounted cash flow calculation that applies interest rates currently being offered on long term borrowings to the contractual maturities on such long term borrowings.

Accrued interest: The carrying amount of accrued interest receivable and payable approximates its fair value.

Off-balance sheet financial instruments: The fair values of commitments to extend credit and standby letters of credit are estimated using the fees currently charged to enter into similar agreements. At September 30, 2010, and December 31, 2009, the fair value of loan commitments and standby letters of credit were deemed to be immaterial.

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The carrying amounts and approximate fair values of the Company s financial instruments are as follows at September 30, 2010 and December 31, 2009:

	September 30, 2010	
(Dollars in Thousands)	Carrying Amounts	Estimated Fair Values
Financial assets		
Cash and due from banks	$ 12,194	$ 12,194
Federal funds sold	10,455	10,455
Securities available-for-sale	52,145	52,145
Loans, net	261,436	261,008
Accrued income	1,194	1,194
Financial liabilities		
Total deposits	292,420	292,788
Short term borrowings	681	681
FHLB borrowings	25,950	26,694
Accrued interest payable	746	709

	December 31, 2009	
(Dollars in Thousands)	Carrying Amounts	Estimated Fair Values
Financial assets		
Cash and due from banks	$ 7,051	$ 7,051
Federal funds sold	19,908	19,908
Securities available-for-sale	46,353	46,353
Loans, net	249,807	249,398
Accrued income	1,099	1,099
Financial liabilities		
Total deposits	271,649	272,056
Short term borrowings	714	714
FHLB borrowings	30,200	31,375
Accrued interest payable	1,068	1,068

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ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Forward-looking Statements

HomeTown Bankshares makes forward-looking statements in this report. These forward-looking statements may include: statements of goals, intentions, earnings expectations, and other expectations; estimates of risks and of future costs and benefits; assessments of probable loan and lease losses; assessments of market risk; and statements of the ability to achieve financial and other goals. Forward-looking statements are typically identified by words such as believe, expect, anticipate, intend, outlook, estimate, forecast, project and other similar words expressions. Forward-looking statements are subject to numerous assumptions, risks and uncertainties, which change over time. Forward-looking statements speak only as of the date they are made. The Company does not assume any duty and does not undertake to update its forward-looking statements. Because forward-looking statements are subject to assumptions and uncertainties, actual results or future events could differ, possibly materially, from those that the Company anticipated in its forward-looking statements, and future results could differ materially from historical performance.

The Company s forward-looking statements are subject to the following principal risks and uncertainties: general economic conditions and trends, either nationally or locally; conditions in the securities markets; changes in interest rates; changes in deposit flows, and in the demand for deposit, loan, and investment products and other financial services; changes in real estate values; changes in the quality or composition of the Company s loan or investment portfolios; changes in competitive pressures among financial institutions or from non-financial institutions; the Company s ability to retain key members of management; changes in legislation, regulation, and policies; and a variety of other matters which, by their nature, are subject to significant uncertainties. The Company provides greater detail regarding some of these factors in its Form 10-K for the year ended December 31, 2009. The Company s forward-looking statements may also be subject to other risks and uncertainties, including those that it may discuss elsewhere in this report or in its other filings with the SEC.

In May 2010, the Company declared a stock split, whereby each stockholder received one additional share for each ten shares owned. The shares were distributed on July 19, 2010 to stockholders of record at the close of business on June 18, 2010. All applicable share and per share data in this Management s Discussion and Analysis of Financial Condition and Results of Operations have been retroactively adjusted to give effect to this stock split.

Our Business

HomeTown Bankshares provides a full complement of consumer and commercial banking services to its primary service area which includes the City of Roanoke, Roanoke County, Christiansburg, and Salem, Virginia and contiguous counties, including Bedford and Franklin, Virginia. We place an emphasis on personal service and offer a broad range of commercial and retail banking products and services including checking, savings and time deposits, individual retirement accounts, residential and commercial mortgages, home equity loans, consumer installment loans, commercial loans, lines and letters of credit. In addition to its main office, the Company has offices in Franklin County, Virginia at Westlake, in Roanoke County at the intersection of Colonial Avenue and Virginia Route 419, Virginia and in the City of Roanoke at 3521 Franklin Road.

In June of 2008, we opened a full service branch office and a separate loan production office in Christiansburg, Virginia. These offices operate under the trade name NewRiver Bank, a branch of HomeTown Bank. In connection with our entry into the New River Valley market, we completed a $5.5 million private placement of common stock on June 30, 2008.

The following is a discussion of factors that significantly affected the financial condition and results of operations of HomeTown Bankshares Corporation. This discussion should be read in connection with the financial statements presented herein.

Critical Accounting Policies

The Company s significant accounting policies are set forth in Note 1 of the Notes to Financial Statements in the Annual Report for the year ended December 31, 2009. The Company s financial position and results of operations are affected by management s application of accounting policies, including estimates, assumptions and judgments made to arrive at the carrying value of assets and liabilities and amounts reported for revenues and expenses.

The allowance for loan losses is an estimate of the losses that may be sustained in our loan portfolio. The allowance is based on two basic principles of accounting: (i) that losses be accrued when they are probable of occurring and are capable of estimation and (ii) that losses on impaired loans be accrued based on the differences between the value of collateral, present value of future cash flows or values that are observable in the secondary market and the loan balance. The allowance for loan losses is maintained at a level, which, in management s judgment, is adequate to absorb credit losses inherent in the loan portfolio.

The amount of the allowance is based on management s evaluation of the collectability of the loan portfolio, including the nature of the portfolio, credit concentrations, trends in historical loss experience, specific impaired loans, economic conditions, and other risks inherent in the portfolio. Management reviews the past due reports and risk-rated loans and discusses individually the loans on these reports with the responsible loan officers. Management uses these tools and provides a detailed quarterly analysis of the allowance based on our historical loan loss experience, risk-rated loans, past dues, concentrations of credit, unsecured loans, loan exceptions, and the economic trend. These are generally grouped by homogeneous loan pools. Allowances for impaired loans are generally determined based on collateral values or the present value of estimated cash flows. This allowance, then, is designated as a specific reserve. Although management uses available information to recognize losses on loans, because of uncertainties associated with local economic conditions, collateral values, and future cash flows on impaired loans, it is reasonably possible that a material change could occur in the allowance for loan losses in the near term. However, the amount of the change that is reasonably possible cannot be estimated. The allowance is increased by a provision for loan losses, which is charged to expense, and reduced by charge-offs, net of recoveries. Changes in the allowance relating to impaired loans are charged or credited to the provision for loan losses. Past due status is determined based on contractual terms.

Discussion of Operations

Nine Months Ended September 30, 2010

The Company recorded a net loss of $2.1 million for the nine months ended September 30, 2010 compared with net income of $300 thousand for the nine months ended September 30, 2009. After net accumulated dividends on preferred stock of $451 thousand in 2010, the company had a net loss available to common shareholders of $(.79) per share, compared with $.09 net income per share in 2009.

The $2.1 million loss for the nine months ended September 30, 2010 is due mainly to $4.1 million in provision for loan losses, compared to $386 thousand for the same period in 2009, an increase of $3.69 million. For the nine months ended September 30, 2010, the company experienced net loan charge offs of $2.8 million compared to $647 thousand for the same period in 2009. The significant increase in charged off loans experienced in 2010 raised the company s annualized net charge offs to average loans ratio from .31% at December 31, 2009 to 1.42% at September 30, 2010. The loan charge off ratio is one of the components used to determine the level of loan loss reserves for pools of loans that do not have identified specific loan loss reserves. The increase in the loan charge off ratio to 1.42% at September 30, 2010 caused a significant increase in the level of loan loss reserves for loans without identified specific loan loss reserves. Impaired loans increased from $20.8 million at December 31, 2009 to $28.3 million at September 30, 2010, an increase of $7.5 million or 36%. Specific reserves on impaired loans increased $386 thousand from $538 thousand at December 31, 2009 to $924 thousand at September 30, 2010. The increase in the level of impaired loans, the increasing historical loan loss experience and other environmental factors necessitated the increase in the level of the allowance for loan losses.

For the nine months ended September 30, 2010, net interest income increased $2.4 million from $5.57 million in 2009 to $7.9 million in 2010. This increase in net interest income is due to average earning assets increasing by $75.5 million in 2010 compared to 2009 and improvement in the net interest margin of 28 basis points to 3.22% for the nine months ended September 30, 2010 compared to the same period in 2009. The improvement in the net interest margin is primarily due to the reduction in the cost of funds from 2.53% in 2009 to 1.89% in 2010.

In the first nine months of 2010, noninterest income increased slightly to $697 thousand in 2010 from $676 thousand. In 2009 non recurring income from gains on the sale of investment securities totaled $160 thousand. In 2010, non recurring income for gains on the sale of other real estate owned totaled $77 thousand. In recurring other income categories, service charges on deposit accounts increased from $308 thousand in 2009 to $360 thousand in 2010, an increase of $52 thousand or 17%. Mortgage loan brokerage fees increased by $10 thousand from the first nine months of 2009 due to homeowners taking advantage of the lower mortgage rates by refinancing. Rental income increased $17 thousand to $92 thousand in 2010 compared with the same period in 2009.

Noninterest expense increased $1.06 million or 19% for the nine months ended September 30, 2010 when compared to the same period in 2009. Salaries and employee benefits increased $530 thousand or 18% from $2.9 million in 2009 to $3.4 million in 2010. This increase is due to growth in staffing as the company has grown, increases in the cost of health insurance and a reduction in the amount of salary and benefit costs that is deferred for the origination of loans. At September 30, 2010, total loans increased $13 million from December 31, 2009 compared to an increase of $36.3 million for the same period of time in 2009. The reduction in volume of loans decreased the amount of salaries and benefits that were deferred in 2010 compared to 2009.

Occupancy and equipment expense increased $25 thousand to $958 thousand from $933 thousand for the nine months ended September 30, 2010 compared to 2009. Data processing expense increased $66 thousand or 25% from 2009 to 2010 due to the growth in the volume of customer accounts and the cost of some new enhancements to our core system software. Advertising and marketing expense increased $79 thousand or 36% in 2010 compared to 2009 due to new advertising campaigns conducted in the second quarter of 2010. Professional fees increased from $148 thousand in 2009 to $302 thousand in 2010 due to increases in legal costs associated with the collection and workout of loans, increased auditing and accounting fees and fees paid to a consultant evaluating our core banking software. Other expense increased from $686 thousand in 2009 to $896 thousand in 2010, an increase of $210 thousand or 31%. This increase is due to a number of factors; including software expense, which increased $50 thousand due mainly to network software enhancements and loan portfolio management and credit underwriting software, Bank franchise tax expense, which increased $21 thousand due to a higher level of capital in 2010 compared to 2009, and loan related and other real estate expenses, which increased $39 thousand.

Three Months Ended September 30, 2010

The Company recorded a net income of $310 million for the three months ended September 30, 2010 compared with net income of $155 thousand for the same period in 2009. After net accumulated dividends on preferred stock of $150 thousand in 2010, the company had net income available to common shareholders of $0.05 per share, compared with net income of $0.04 per share in 2009.

Net Income of $310 thousand for the three months ended September 30, 2010 was recorded in spite of the $259 thousand increase of provision for loan loss expense when compared to the same period in 2009. For the three months ended September 30, 2010, the provision expense totaled $441 thousand compared to $182 thousand for the same period in 2009, and increase of 142%. The significant increase in charged off loans experienced in 2010 raised the company s annualized net charge offs to average loans ratio from .31% at December 31, 2009 to 1.42% at September 30, 2010. The loan charge off ratio is one of the components used to determine the level of loan loss reserves for pools of loans that do not have identified specific loan loss reserves. The increase in the loan charge off ratio to 1.42% at September 30, 2010 caused a significant increase in the level of loan loss reserves for loans without identified specific loan loss reserves. Impaired loans increased from $20.8 million at December 31, 2009 to $28.3 million at September 30, 2010, an increase of $7.5 million or 36%. Specific reserves on impaired loans increased $386 thousand from $538 thousand at December 31, 2009 to $924 thousand at September 30, 2010. The increase in the level of impaired loans, the increasing historical loan loss experience and other environmental factors necessitated the increase in the level of the allowance for loan losses during the third quarter of 2010 and in prior quarters.

Net interest income increased $700 thousand or 33% for the three months ended September 30, 2010 compared to the same period in 2009. This increase in net interest income is due to average earning assets increasing by $55.6 million in the third quarter of 2010 compared to 2009 and improvement in the net interest margin of 34 basis points to 3.31% for the three months ended September 30, 2010 compared to the same period in 2009. The improvement in the net interest margin is primarily due to the reduction in the cost of funds from 2.35% in 2009 to 1.76% in 2010.

Noninterest income increased in the third quarter from $195 thousand in 2009 to $235 thousand. This increase is mainly due to mortgage loan brokerage fees increasing from $37 thousand in 2009 to $72 thousand in 2010, an increase $35 thousand or 95%. Service charges on deposit accounts decreased by $10 thousand from the same period in 2009 while rental income increased by that same amount, $10 thousand.

Noninterest expense increased $326 thousand or 17% for the three months ended September 30, 2010 when compared to the same period in 2009. Salaries and employee benefits increased $156 thousand or 15% from $1.1

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million in 2009 to $1.2 million in 2010. This increase is due to growth in staffing as the company has grown, increases in the cost of health insurance and a reduction in the amount of salary and benefit costs that is deferred for the origination of loans. At September 30, 2010, total loans increased $13 million from December 31, 2009 compared to an increase of $36.3 million for the same period of time in 2009. The reduction in volume of loans decreased the amount of salaries and benefits that were deferred in 2010 compared to 2009.

Occupancy and equipment expense increased $20 thousand to $338 thousand from $318 thousand for the three months ended September 30, 2010 compared to 2009 mainly due to new lease agreement for branch expansion signed in May of 2010. Data processing expense increased $26 thousand or 31% from 2009 to 2010 due to the growth in the volume of customer accounts and the cost of some new enhancements to our core system software. Advertising and marketing expense decreased $21 thousand in the second quarter of 2010 compared to 2009. Professional fees increased from $56 thousand in 2009 to $102 thousand in 2010 due to increases in legal costs associated with the collection and workout of loans, increased auditing and accounting fees and fees paid to a consultant evaluating our core banking software. FDIC insurance assessment expense increased from $104 thousand in the third quarter of 2009 to $129 thousand for the same period in 2010 due to the growth in deposits in 2010.

Financial Condition

At September 30, 2010, the Company had total assets of $353 million compared to $338 million at December 31, 2009. Total assets increased $15.5 million or 4.6% since year end 2009. At September 30, 2010, assets were comprised principally of loans, cash and due from banks, federal funds sold, and investment securities. Net loans increased $11.6 million, or 4.7%, to $261.4 million at September 30, 2010. Federal funds sold decreased to $10.5 million from $19.9 million at December 31, 2009. Investment securities increased $5.8 million to $52.1 million.

The Company s liabilities at September 30, 2010 totaled $321 million compared to $304 million at December 31, 2009, an increase of $16.6 million or 5.5%. Noninterest-bearing deposits decreased by $2.4 million, and interest-bearing deposits increased $23.2 million, or 9.23%, to $274.3 million.

At September 30, 2010 and December 31, 2009, the Company had stockholders equity of $32.7 million and $33.8 million, respectively, a decrease of $1.1 million or 3.2%. Changes to stockholders equity in the first nine months included a net loss of $2.1 million and a charge to retained earnings of $317 thousand for payments of preferred stock dividends, net. These decreases were offset by a $1.2 million gain in the market value of investment securities available for sale.

On September 18, 2009, as part of the Troubled Asset Relief Program-Capital Purchase Program, the Company entered into a Letter Agreement and Securities Purchase Agreement with the United States Department of the Treasury pursuant to which the Company issued 10 thousand shares of the Company s Fixed Rate Cumulative Perpetual Preferred Stock, Series A for a purchase price of $10 million in cash and issued a warrant to purchase 374.37437 shares of the Company s Fixed Rate Cumulative Perpetual Preferred Stock, Series B for a per share price of $1.00 per share, which was exercised immediately.

On May 18, 2010, the company declared a stock split to its shareholders of record as of June 18, 2010.

Management believes the Company has sufficient capital to fund its operations. At September 30, 2010, the Company was in compliance with all regulatory capital requirements. Management believes that the Company has sufficient liquidity on a short-term basis to meet any funding needs it may have, and expects that its long term liquidity needs can be achieved through deposit growth, however there can be no assurance that such growth will develop.

Non-performing Assets

Non-performing assets consist of loans past-due ninety days or more and still accruing interest, non-accrual loans and repossessed and foreclosed assets. The Company had two loans past due ninety days or more and still accruing interest totaling $1.3 million, twelve nonaccrual loans totaling $4.9 million as well as $2.4 million of other real estate owned at September 30, 2010.

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Allowance for Loan Losses

The allowance for loan losses is increased by charges to income and decreased by charge-offs, net of recoveries. Management s periodic evaluation of the adequacy of the allowance is based on the Company s past loan loss experience, peer group loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower s ability to repay, the estimated value of any underlying collateral, and current economic conditions.

The Company uses its own loss experience for pools of loans where losses have been incurred and for pools of loans with no loss history, peer bank loss experience is used. At September 30, 2010, the Company s own historical loss experience factors used in our evaluation reflected significant increases resulting in an increase in this component of the general reserves. This increase in the general reserves, loan charge offs of $2.8 million along with a $386 thousand increase in specific reserves for impaired loans resulted in a provision for loan losses of $441 thousand in the third quarter of 2010 compared to $182 thousand in 2009. Based on this evaluation, the percentage of the allowance for loan losses to total loans was 1.58% at September 30, 2010 and 1.13% at December 31, 2009.

Liquidity

Liquidity represents the ability to meet present and future financial obligations through either the sale or maturity of existing assets or with borrowings from correspondent banks or other deposit markets. Liquid assets include cash, interest-bearing and noninterest-bearing deposits with banks, federal funds sold, investment securities and loans maturing within one year. As a result of the Company s management of liquid assets and the ability to generate liquidity through liability funding, management believes that the Company maintains overall liquidity sufficient to satisfy its depositors requirements and to meet its customers borrowing needs.

At September 30, 2010, cash, interest-bearing and noninterest-bearing deposits with banks, federal funds sold, loans maturing within one year, and expected maturities, calls and principal repayments from the securities portfolio within one year totaled $106 million. At September 30, 2010, 30.9% or $82 million of the loan portfolio would mature within one year. At September 30, 2010, non-deposit sources of available funds totaled $27.2 million, which includes $10.2 million immediately available from the Federal Home Loan Bank of Atlanta (FHLB) with additional credit availability of $33.4 million provided qualifying collateral is pledged. During the first nine months of 2010, other borrowing activity included a principal pay down of $4.25 million of FHLB borrowings.

Capital Requirements

The maintenance of appropriate levels of capital is a priority and is continually monitored. Banks are subject to various regulatory capital requirements administered by the federal and state banking agencies. Quantitative measures established by regulations to ensure capital adequacy require the Company to maintain minimum capital ratios. Failure to meet minimum capital ratios can initiate certain mandatory, and possibly additional discretionary actions by regulators that, if undertaken, could have a material effect on the consolidated financial statements. The following are the Company s and Bank s capital ratios:

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
September 30, 2010						
Total Capital (to Risk-Weighted Assets)						
Consolidated	$ 35,206	13.0%	$ 21,599	8.0%	$ 26,998	10.0%
HomeTown Bank	$ 32,866	12.2%	$ 21,605	8.0%	$ 27.006	10.0%
Tier I Capital (to Risk-Weighted Assets)						
Consolidated	$ 31,828	11.8%	$ 10,798	4.0%	$ 16,197	6.0%
HomeTown Bank	$ 29,488	10.9%	$ 10,801	4.0%	$ 16,020	6.0%
Tier I Capital (to Average Assets)						
Consolidated	$ 31,828	9.0%	$ 14,177	4.0%	$ 17,722	5.0%

HomeTown Bank	$ 29,488	8.3%	$ 14,177	4.0%	$ 17,721	5.0%
December 31, 2009						
Total Capital (to Risk-Weighted Assets)						
Consolidated	$ 37,019	14.1%	$ 21,004	8.0%	$ 26,255	10.0%
HomeTown Bank	$ 31,846	12.1%	$ 21,055	8.0%	$ 26,319	10.0%
Tier I Capital (to Risk-Weighted Assets)						
Consolidated	$ 34,157	13.0%	$ 10,502	4.0%	$ 15,753	6.0%
HomeTown Bank	$ 28,984	11.0%	$ 10,540	4.0%	$ 15,809	6.0%
Tier I Capital (to Average Assets)						
Consolidated	$ 34,157	10.4%	$ 13,100	4.0%	$ 16,374	5.0%
HomeTown Bank	$ 28,984	8.9%	$ 13,027	4.0%	$ 16,283	5.0%

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Financial Instruments With Off-Balance-Sheet Risk

In the normal course of business to meet the financing needs of its customers, the Company is a party to financial instruments with off-balance-sheet risk. These financial instruments involve commitments to extend credit. These instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the consolidated balance sheets.

The Company s exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit is represented by the contractual amount of those instruments. The same credit policy is used in making commitments as is used for on-balance-sheet risk.

At September 30, 2010 outstanding commitments to extend credit including letters of credit were $39.6 million. There are no commitments to extend credit on impaired loans.

Commitments to extend credit are agreements to lend to a customer as long as there is no breach of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The commitments may expire without ever being drawn upon; therefore, the total commitment amounts do not necessarily represent future cash outlays for the Company.

Recent Developments

On October 3, 2008, Congress passed the Emergency Economic Stabilization Act of 2008 (EESA), which provides the U. S. Treasury with broad authority to implement certain actions to help restore stability and liquidity to U.S. markets. Under the EESA, the basic limit on federal deposit insurance coverage was temporarily increased from $100,000 to $250,000 per depositor, until December 31, 2009. On October 14, 2008, the Department of the Treasury announced it would purchase equity stakes in a wide variety of banks and thrifts. Under this program, known as the Troubled Asset Relief Program Capital Purchase Program, or CPP, from the $700 billion authorized by the EESA, the Treasury will make $250 billion of capital available to U.S. financial institutions in the form of perpetual preferred stock. The preferred stock would qualify as Tier 1 capital. In conjunction with the purchase of preferred stock, the Treasury will receive warrants to purchase common stock.

The CPP program is voluntary and requires an institution to comply with a number of restrictions and provisions. Participation in the program is subject to approval by the Treasury department. On September 18, 2009, as part of the CPP program, the Company entered into a Letter Agreement and Securities Purchase Agreement with the United States Department of the Treasury pursuant to which the Company issued 10 thousand shares of the Company s Fixed Rate Cumulative Perpetual Preferred Stock, Series A for a purchase price of $10 million in cash and issued a warrant to purchase 374.37437 shares of the Company s Fixed Rate Cumulative Perpetual Preferred Stock, Series B for a per share price of $1.00 per share, which was exercised immediately.

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Recent Accounting Pronouncements

In June 2009, the FASB issued new guidance relating to the accounting for transfers of financial assets. The new guidance, which was issued as SFAS No. 166, Accounting for Transfers of Financial Assets, an amendment to SFAS No. 140 , was adopted into Codification in December 2009 through the issuance of Accounting Standards Update (ASU) 2009-16. The new standard provides guidance to improve the relevance, representational faithfulness, and comparability of the information that an entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor s continuing involvement, if any, in transferred financial assets. ASU 2009-16 was effective for transfers on or after January 1, 2010. The adoption of the new guidance did not have a material impact on the Company s consolidated financial statements.

In June 2009, the FASB issued new guidance relating to variable interest entities. The new guidance, which was issued as SFAS No. 167, Amendments to FASB Interpretation No. 46(R), was adopted into Codification in December 2009. The objective of the guidance is to improve financial reporting by enterprises involved with variable interest entities and to provide more relevant and reliable information to users of financial statements. SFAS No. 167 was effective as of January 1, 2010. The adoption of the new guidance did not have a material impact on the Company s consolidated financial statements.

In October 2009, the FASB issued ASU 2009-15, Accounting for Own-Share Lending Arrangements in Contemplation of Convertible Debt Issuance or Other Financing. ASU 2009-15 amends Subtopic 470-20 to expand accounting and reporting guidance for own-share lending arrangements issued in contemplation of convertible debt issuance. ASU 2009-15 is effective for fiscal years beginning on or after December 15, 2009 and interim periods within those fiscal years for arrangements outstanding as of the beginning of those fiscal years. The adoption of the new guidance did not have a material impact on the Company s consolidated financial statements.

In January 2010, the FASB issued ASU 2010-04, Accounting for Various Topics Technical Corrections to SEC Paragraphs. ASU 2010-04 makes technical corrections to existing SEC guidance including the following topics: accounting for subsequent investments, termination of an interest rate swap, issuance of financial statements - subsequent events, use of residential method to value acquired assets other than goodwill, adjustments in assets and liabilities for holding gains and losses, and selections of discount rate used for measuring defined benefit obligation. The adoption of the new guidance did not have a material impact on the Company s consolidated financial statements.

In January 2010, the FASB issued ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements. ASU 2010-06 amends Subtopic 820-10 to clarify existing disclosures, require new disclosures, and includes conforming amendments to guidance on employers disclosures about postretirement benefit plan assets. ASU 2010-06 is effective for interim and annual periods beginning after December 15, 2009, except for disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. The adoption of the new guidance did not have a material impact on the Company s consolidated financial statements

In February 2010, the FASB issued ASU 2010-09, Subsequent Events (Topic 855): Amendments to Certain Recognition and Disclosure Requirements. ASU 2010-09 addresses both the interaction of the requirements of Topic 855 with the SEC s reporting requirements and the intended breadth of the reissuance disclosures provisions related to subsequent events. An entity that is an SEC filer is not required to disclose the date through which subsequent events have been evaluated. ASU 2010-09 is effective immediately. The adoption of the new guidance did not have a material impact on the Company s consolidated financial statements

In July 2010, the FASB issued ASU 2010-20, Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses. The new disclosure guidance will significantly expand the existing requirements and will lead to greater transparency into a company s exposure to credit losses from lending arrangements. The extensive new disclosures of information as of the end of a reporting period will become effective for both interim and annual reporting periods ending on or after December 15, 2010. Specific disclosures regarding activity that occurred before the issuance of the ASU, such as the allowance rollforward and modification disclosures, will be required for periods beginning or or after December 15, 2010. The Company is currently assessing the impact that ASU 2010-20 will have on its consolidated financial statements.

On September 15, 2010, the SEC issued Release No. 33-9142, Internal Control Over Financial Reporting In Exchange Act Periodic Reports of Non-Accelerated Filers. This release issued a final rule adopting amendments to its rules and forms to conform them to Section 404(c) of the Sarbanes-Oxley Act of 2002 (SOX), as added by Section 989G of the Dodd-Frank Wall Street Reform and Consumer Protection Act. SOX Section 404(c) provides that Section 404(b) shall not apply with respect to any audit report prepared for an issuer that is neither an accelerated filer nor a large accelerated filer as defined in Rule 12b-2 under the Securities Exchange Act of 1934. Release No. 33-9142 was effective September 21, 2010.

On September 17, 2010, the SEC issued Release No. 33-9144, Commission Guidance on Presentation of Liquidity and Capital Resources Disclosures in Management s Discussion and Analysis. This interpretive release is intended to improve discussion of liquidity and capital resources in Management s Discussion and Analysis of Financial Condition and Results of Operations in order to facilitate understanding by investors of the liquidity and funding risks facing the registrant. This release was issued in conjunction with a proposed rule, Short-Term Borrowings Disclosures, that would require public companies to disclose additional information to investors about their short-term borrowing arrangements. Release No. 33-9144 was effective on September 28, 2010.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK
Not applicable to smaller reporting companies.

ITEM 4T. CONTROLS AND PROCEDURES
Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures, as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the Exchange Act), which are designed to ensure that information required to be disclosed in reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating its disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable assurance that the objectives of the disclosure controls and procedures are met. Additionally, in designing disclosure controls and procedures, management necessarily was required to apply its judgment in evaluating the cost benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Based on their evaluation as of the end of the period covered by this quarterly report on Form 10-Q, the Chief Executive Officer and Chief Financial Officer have concluded that the disclosure controls and procedures were effective at the reasonable assurance level.

Internal Controls

The Company maintains internal accounting controls as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, that are designed to provide reasonable assurance that assets are safeguarded and that transactions are executed in accordance with management s authorization and properly recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements. There were no significant changes to the Company s internal controls or in other factors that could significantly affect those controls subsequent to the date of the most recent evaluation by the Chief Executive Officer and Chief Financial Officer.

PART II OTHER INFORMATION

Item 1. Legal Proceedings.
In the normal course of business, the Company becomes involved in litigation arising from the banking, financial and other activities it conducts. Management, after consultation with legal counsel, does not anticipate that the ultimate liability, if any, arising from these matters will have a material effect on the Company s financial condition, operating results or liquidity.

Item 1A. Risk Factors.
Not applicable to smaller reporting companies.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds
None

Item 3. Defaults Upon Senior Securities

None

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Item 4. (Removed and Reserved)

Item 5. Other Information

None

Item 6. Exhibits

(a) Exhibits

Exhibit No.	
3.1	Certificate of Amendment and Articles of Amendment for the Series A Preferred Stock, incorporated herein by reference to Exhibit 3.1 to Form 8-K filed September 24, 2009.
3.2	Certificate of Amendment and Articles of Amendment for the Series B Preferred Stock, incorporated herein by reference to Exhibit 3.1 to Form 8-K filed September 24, 2009.
4.1	Form of Certificate for the Series A Preferred Stock, incorporated herein by reference to Exhibit 4.1 to Form 8-K filed September 24, 2009.
4.2	Form of Certificate for the Series B Preferred Stock, incorporated herein by reference to Exhibit 4.2 to Form 8-K filed September 24, 2009.
10.2*	Employment Agreement dated March 1, 2006 between HomeTown Bank and S. K. Still, incorporated herein by reference to Exhibit 10.2 to Form 10QSB for the quarter ended March 31, 2006.
10.3*	Employment Agreement dated March 1, 2006 between HomeTown Bank and W. C. Moses, incorporated herein by reference to Exhibit 10.3 to Form 10QSB for the quarter ended March 31, 2006.
10.4	HomeTown Bank 2005 Stock Option Plan, incorporated herein by reference to Exhibit 10.4 to Form 10QSB for the quarter ended June 30, 2006.
10.5	Real estate purchase contract, incorporated herein by reference to Exhibit 10.5 to Form 10QSB for the quarter ended June 30, 2006.
10.6*	Employment Agreement dated May 1, 2006 between HomeTown Bank and C. W. Maness, Jr., incorporated herein by reference to Exhibit 10.4 to Form 10QSB for the quarter ended June 30, 2006.
10.7	Lease agreement, incorporated herein by reference to Exhibit 10.7 to form 10QSB for the quarter ended September 30, 2006.
10.8	Hometown Bankshares Corporation Restricted Stock Plan, Incorporated herein by reference to Exhibit 10.1 to Form 8-K filed September 16, 2010.
10.9	Letter Agreement, including Schedule A, and Securities Purchase Agreement, dated September 18, 2009, between HomeTown Bankshares Corporation and United States Department of the Treasury, with respect to the issuance and sale of the Series A Preferred Stock and Series B Preferred Stock, incorporated herein by reference to Exhibit 10.1 to Form 8-K filed September 24, 2009.
10.10	Form of Compensation Modification Agreement and Waiver, executed by Senior Executive Officers of HomeTown Bankshares Corporation , incorporated herein by reference to Exhibit 10.2 to Form 8-K filed September 24, 2009.
31.1	Certification of Chief Executive of Officer (302 Certification).
31.2	Certification of Chief Financial Officer (302 Certification).
32	Certification pursuant to 18 U.S.C. Section 1350 (906 Certification).
99.1	TARP Chief Executive Officer Certification
99.2	TARP Chief Financial Officer Certification

* Denotes management contract

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Reports on form 8-K

On August 12, 2010, the Company announced its earnings for the quarter-ended June 30, 2010.

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SIGNATURES

Pursuant to the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

HOMETOWN BANKSHARES CORPORATION

Date: November 15, 2010	By:
	/s/ Susan K. Still Susan K. Still President Chief Executive Officer
Date: November 15, 2010	By:
	/s/ Charles W. Maness, Jr. Charles W. Maness, Jr. Executive Vice President Chief Financial Officer

HOMETOWN BANKSHARES CORPORATION

FORM 10-Q

INDEX TO EXHIBITS

Exhibit	Description
3 (i)	Articles of Incorporation of Hometown Bank, incorporated by reference to Exhibit 3 (i) of the Current Report on Form 10-SB dated April 27, 2006 and Form S-4 filed April 10, 2009.
3 (ii)	Bylaws of Hometown Bank, incorporated by reference to Exhibit 3 (ii) of the Current Report on Form 10-SB dated April 27, 2006 and as appendix B of Form S-4 filed April 10, 2009.
10.2*	Employment Agreement dated March 1, 2006 between HomeTown Bank and S. K. Still, incorporated herein by reference to Exhibit 10.2 to Form 10QSB for the quarter ended March 31, 2006 and as Exhibit 10.1 to Form S-4 filed April 10, 2009.
10.3*	Employment Agreement dated March 1, 2006 between HomeTown Bank and W. C. Moses, incorporated herein by reference to Exhibit 10.3 to Form 10QSB for the quarter ended March 31, 2006 and as Exhibit 10.3 to Form S-4 filed April 10, 2009.
10.4	HomeTown Bankshares 2005 Stock Option Plan, incorporated herein by reference to Exhibit 10.4 to Form 10QSB for the quarter ended June 30, 2006.
10.5	Real estate purchase contract, incorporated herein by reference to Exhibit 10.5 to Form 10QSB for the quarter ended June 30, 2006.
10.6*	Employment Agreement dated May 1, 2006 between HomeTown Bank and C. W. Maness, Jr., incorporated herein by reference to Exhibit 10.6 to Form 10QSB for the quarter ended June 30, 2006 and as Exhibit 10.2 to Form S-4 filed April 10, 2009.
10.7	Lease Agreement by and between James Paul Poulos and Rita Ann Poulos, Trustees, under that certain Trust Agreement with James Paul Poulos and Hometown Bank dated August 1, 2006, incorporated herein by reference to Exhibit 10.7 to Form 10QSB for the quarter ended September 30, 2006 and as Exhibit 10.7 to Form S-4 filed April 10, 2009.
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.