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POTOMAC BANCSHARES INC
Form 10QSB
August 07, 2001

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

FORM 10-QSB

(Mark One)

XX Quarterly report under Section 13 or 15(d) of the Securities Exchange Act
---- of 1934

For quarterly period ended June 30, 2001

Transition report under Section 13 or 15(d) of the Exchange Act

For the transition period from _____ to _____

Commission file number 0-24958

Potomac Bancshares, Inc.
(Exact Name of Small Business Issuer as Specified in Its Charter)

West Virginia 55-0732247
(State or Other Jurisdiction of (IRS Employer
Incorporation or Organization) Identification Number)

111 East Washington Street, Charles Town WV 25414-1071
(Address of Principal Executive Offices) (Zip Code)

304-725-8431
(Issuer's Telephone Number, Including Area Code)

NO CHANGE
(Former Name, Former Address and Former Fiscal Year, if Changed
Since Last Report)

Check whether the issuer: (1) filed all reports required to be filed by
Section 13 or 15(d) of the Exchange Act during the past 12 months (or 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 XXX No
--- ---

APPLICABLE ONLY TO ISSUERS INVOLVED IN
BANKRUPTCY PROCEEDINGS DURING THE
PRECEDING FIVE YEARS

Check whether the registrant filed all documents and reports required to be
filed by Section 12, 13 or 15(d) of the Exchange Act after the distribution of
securities under a plan confirmed by a court.

Yes No Not applicable
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APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 600,000 shares

Transitional Small Business Disclosure Format (check one):

Yes No XXX
--- --- ---

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

POTOMAC BANCSHARES, INC.
CONSOLIDATED BALANCE SHEETS
(000 OMITTED)

| | (Unaudited) June 30 2001 ----- | December 31 2000 ----- |
|--|---|------------------------------|
| Assets: | | |
| Cash and due from banks | \$ 9,028 | \$ 6,053 |
| Securities purchased under agreements to resell and federal funds sold | 4,307 | \$ 17,366 |
| Securities held to maturity (fair value of \$21,462 at June 30, 2001 and \$18,105 at December 31, 2000) | 20,977 | 17,928 |
| Securities available for sale, at fair value | 21,531 | 18,162 |
| Loans held for sale | 209 | -- |
| Loans, net of allowance for loan losses of \$1,265 at June 30, 2001 and \$1,268 at December 31, 2000 | 92,501 | 83,179 |
| Other real estate owned | -- | 13 |
| Bank premises and equipment, net | 3,291 | 3,177 |
| Accrued interest receivable | 1,103 | 1,051 |
| Other assets | 1,321 | 1,293 |
| | ----- | ----- |
| Total Assets | \$154,268 ===== | \$148,222 ===== |
| Liabilities and Stockholders' Equity: | | |
| Liabilities: | | |
| Noninterest bearing deposits | \$ 18,354 | \$ 19,423 |
| Interest bearing deposits | 112,772 | 109,522 |
| | ----- | ----- |
| Total Deposits | 131,126 | 128,945 |
| Accrued interest payable | 278 | 303 |
| Federal funds purchased and securities sold under agreements to repurchase | 536 | -- |
| Advances payable to Federal Home Loan Bank | 2,500 | -- |
| Other liabilities | 1,131 | 1,010 |
| | ----- | ----- |
| Total Liabilities | \$135,571 ----- | \$130,258 ----- |

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Stockholders' Equity:

| | | |
|--|-----------|-----------|
| Common stock par value \$1.00 per share (5,000,000 shares authorized, 600,000 shares issued and outstanding) | \$ 600 | \$ 600 |
| Surplus | 5,400 | 5,400 |
| Accumulated other comprehensive income (loss) | 147 | (44) |
| Undivided profits | 12,550 | 12,008 |
| | ----- | ----- |
| Total Stockholders' Equity | 18,697 | 17,964 |
| | ----- | ----- |
| | | |
| Total Liabilities and Stockholders' Equity | \$154,268 | \$148,222 |
| | ===== | ===== |

See Accompanying Notes to Consolidated Financial Statements

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POTOMAC BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF INCOME
(000 omitted except for per share data)
(Unaudited)

| | For the Three Months Ended June 30 | | For t |
|---|------------------------------------|---------|-------|
| | 2001 | 2000 | En |
| | ----- | ----- | ----- |
| Interest Income: | | | |
| Interest and fees on loans | \$2,026 | \$1,747 | \$3 |
| Interest on securities held to maturity - Taxable | 282 | 367 | |
| Interest on securities available for sale - Taxable | 301 | 346 | |
| Interest on securities purchased under agreements to resell and federal funds sold | 101 | 111 | |
| Income on other securities | 8 | 7 | |
| Other interest income | 2 | -- | |
| | ----- | ----- | ----- |
| Total Interest Income | \$2,720 | \$2,578 | \$5 |
| Interest Expense: | | | |
| Interest on deposits | 956 | 985 | 1 |
| Interest on federal funds purchased and securities purchased under agreements to resell | 3 | -- | |
| | ----- | ----- | ----- |
| Total Interest Expense | 959 | 985 | 1 |
| Net Interest Income | \$1,761 | \$1,593 | \$3 |
| Provision for Loan Losses | 19 | 50 | |
| | ----- | ----- | ----- |
| Net Interest Income after Provision for Loan Losses | \$1,742 | \$1,543 | \$3 |
| | ----- | ----- | ----- |

Noninterest Income:

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| | | | |
|--|---------|---------|-----|
| Commissions and fees from fiduciary activities | \$ 134 | \$ 146 | \$ |
| Service charges on deposit accounts | 100 | 97 | |
| Net servicing fees | 1 | 1 | |
| Insurance commissions and fees | 22 | 9 | |
| Other noninterest income | 52 | 39 | |
| Gain on sale of equipment | -- | 1 | |
| Gain on sale of other real estate (net) | -- | 11 | |
| | ----- | ----- | |
| Total Noninterest Income | \$ 309 | \$ 304 | \$ |
| | ----- | ----- | |
| Noninterest Expenses: | | | |
| Salaries and employee benefits | \$ 735 | \$ 714 | \$1 |
| Net occupancy expense of premises | 68 | 53 | |
| Furniture and equipment expenses | 106 | 92 | |
| Other operating expenses | 353 | 281 | |
| | ----- | ----- | |
| Total Noninterest Expenses | \$1,262 | \$1,140 | \$2 |
| | ----- | ----- | |
| Income before Income Tax Expense | \$ 789 | \$ 707 | \$1 |
| Income Tax Expense | 289 | 255 | |
| | ----- | ----- | |
| Net Income | \$ 500 | \$ 452 | \$ |
| | ===== | ===== | == |
| Earnings Per Share, basic and diluted | \$.83 | \$.75 | \$ |
| | ===== | ===== | == |

See Accompanying Notes to Consolidated Financial Statements

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POTOMAC BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE SIX MONTHS ENDED JUNE 30, 2001 AND 2000
(000 Omitted)
(Unaudited)

| | Common Stock | Capital Surplus | Undivided Profits | Accumulated Other Comprehensive Income (Loss) | Compr In |
|---|-----------------|--------------------|----------------------|--|-------------|
| | ----- | ----- | ----- | ----- | ----- |
| Balances, December 31, 1999 | \$600 | \$5,400 | \$10,944 | \$(256) | |
| Comprehensive income | | | | | |
| Net income | -- | -- | 845 | -- | \$ 8 |
| Other comprehensive income, unrealized holding gains arising during the period (net of tax, \$4) | -- | -- | -- | 8 | |
| Comprehensive income | | | | | \$ 8 |
| | | | | | ===== |

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| | | | | |
|--|-------|---------|----------|---------|
| Cash dividends | -- | -- | (300) | -- |
| | ---- | ----- | ----- | ----- |
| Balances, June 30, 2000 | \$600 | \$5,400 | \$11,489 | \$(248) |
| | ===== | ===== | ===== | ===== |
| Balances, December 31, 2000 | \$600 | \$5,400 | \$12,008 | \$(44) |
| Comprehensive income | | | | |
| Net income | -- | -- | 872 | -- |
| Other comprehensive income, unrealized holding gains arising during the period (net of tax, \$98) | -- | -- | -- | 191 |
| Comprehensive income | | | | \$ 8 |
| | | | | ----- |
| | | | | \$1,0 |
| | | | | ===== |
| Cash dividends | -- | -- | (330) | -- |
| | ---- | ----- | ----- | ----- |
| Balances, June 30, 2001 | \$600 | \$5,400 | \$12,550 | \$ 147 |
| | ===== | ===== | ===== | ===== |

See Accompanying Notes to Consolidated Financial Statements

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POTOMAC BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(000 Omitted)
(Unaudited)

| | For the Six Months Ended | |
|--|--------------------------|-----------------|
| | June 30 2001 | June 30 2000 |
| | ----- | ----- |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net income | \$ 872 | \$ 845 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for loan losses | 40 | 50 |
| Depreciation | 120 | 101 |
| Deferred tax (benefit) | -- | (2) |
| Discount accretion and premium amortization on securities, net | (16) | (15) |
| (Gain) on sale of real estate | -- | (19) |
| (Gain) on sale of equipment | -- | (1) |
| (Increase) in accrued interest receivable | (52) | (62) |
| (Increase) in other assets | (126) | (181) |
| Fees on loans sold | (5) | -- |
| Proceeds from sale of loans | 227 | -- |
| Purchase of loans for sale | (431) | -- |
| (Decrease) in accrued interest payable | (25) | (15) |
| Increase in other liabilities | 121 | 65 |
| | ----- | ----- |

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| | | |
|---|-------------|-------------|
| Net cash provided by operating activities | \$ 725 | \$ 766 |
| | ----- | ----- |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Proceeds from maturity of securities held to maturity | \$ 6,000 | \$ 2,000 |
| Proceeds from maturity of securities available for sale | 5,000 | 1,000 |
| Purchase of securities held to maturity | (9,035) | (9,890) |
| Purchase of securities available for sale | (8,078) | -- |
| Net (increase) in loans | (9,362) | (4,941) |
| Purchases of bank premises and equipment | (234) | (920) |
| Proceeds from sale of real estate | 13 | 95 |
| | ----- | ----- |
| Net cash (used in) investing activities | \$ (15,696) | \$ (12,656) |
| | ----- | ----- |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Net increase (decrease) in noninterest bearing deposits | \$ (1,069) | \$ 703 |
| Net increase (decrease) in interest bearing deposits | 3,250 | (2,461) |
| Net increase in securities sold under agreements to repurchase | 536 | -- |
| Net increase in advances payable to Federal Home Loan Bank | 2,500 | -- |
| Cash dividends | (330) | (300) |
| | ----- | ----- |
| Net cash provided by (used in) financing activities | \$ 4,887 | \$ (2,058) |
| | ----- | ----- |
| (Decrease) in cash and cash equivalents | \$ (10,084) | \$ (13,948) |
| CASH AND CASH EQUIVALENTS | | |
| Beginning | 23,419 | 21,054 |
| | ----- | ----- |
| Ending | \$ 13,335 | \$ 7,106 |
| | ===== | ===== |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION | | |
| Cash payments for: | | |
| Interest | \$ 1,973 | \$ 1,975 |
| | ===== | ===== |
| Income taxes | \$ 423 | \$ 526 |
| | ===== | ===== |
| SUPPLEMENTAL SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES | | |
| Unrealized gain on securities available for sale | \$ 289 | \$ 13 |
| | ===== | ===== |

See Accompanying Notes to Consolidated Financial Statements

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POTOMAC BANCSHARES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2001 (UNAUDITED) AND DECEMBER 31, 2000

- In the opinion of management, the accompanying financial statements contain all adjustments (consisting of only normal recurring accruals) necessary to present fairly the financial position as of June 30, 2001, and December 31, 2000, the results of operations for the three months ended June 30, 2001 and 2000, and the results of operations and cash flows for the six months ended June 30, 2001 and 2000. The statements should be read in conjunction with Notes to Consolidated Financial Statements included in the Potomac

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Bancshares, Inc. annual report for the year ended December 31, 2000. The results of operations for the six month periods ended June 30, 2001 and 2000, are not necessarily indicative of the results to be expected for the full year.

2. Securities held to maturity as of June 30, 2001 and December 31, 2000 are summarized below:

| (000 Omitted) June 30, 2001 | | | |
|---|------------------------------|---------------------------------|---------------|
| Amortized Cost | Gross Unrealized Gains | Gross Unrealized (Losses) | Fair Value |
| ----- | | | |
| Securities held to maturity: | | | |
| Obligations of U.S. Government agencies | \$20,977 | \$485 | \$ -- |
| | ===== | ===== | ===== |

| (000 Omitted) December 31, 2000 | | | |
|---|------------------------------|---------------------------------|---------------|
| Amortized Cost | Gross Unrealized Gains | Gross Unrealized (Losses) | Fair Value |
| ----- | | | |
| Securities held to maturity: | | | |
| Obligations of U.S. Government agencies | \$17,928 | \$187 | \$(10) |
| | ===== | ===== | ===== |

Securities available for sale as of June 30, 2001 and December 31, 2000 are summarized below:

| (000 Omitted) June 30, 2001 | | | |
|---|------------------------------|---------------------------------|---------------|
| Amortized Cost | Gross Unrealized Gains | Gross Unrealized (Losses) | Fair Value |
| ----- | | | |
| Securities available for sale: | | | |
| Obligations of U.S. Government agencies | \$21,309 | \$222 | \$ -- |
| | ===== | ===== | ===== |

| (000 Omitted) December 31, 2000 | | | |
|------------------------------------|------------------------------|---------------------------------|---------------|
| Amortized Cost | Gross Unrealized Gains | Gross Unrealized (Losses) | Fair Value |
| ----- | | | |
| | | | |

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Securities available for sale:

| | | | | |
|---|-------------------|----------------|-----------------|-------------------|
| Obligations of U.S. Government agencies | \$18,229 ===== | \$ 15 ===== | \$(82) ===== | \$18,162 ===== |
|---|-------------------|----------------|-----------------|-------------------|

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3. The consolidated loan portfolio, stated at face amount, is composed of the following:

Real estate loans:

- Construction and land development
- Secured by farmland
- Secured by 1-4 family residential
- Other real estate loans
- Loans to farmers (except those secured by real estate)
- Commercial and industrial loans (except those secured by real estate)
- Loans to individuals for personal expenditures
- All other loans

Less: Allowance for loan losses

Total loans

4. The following is a summary of transactions in the allowance for loan losses:

Balance at beginning of period

- Provision charged (credited) to operating expense
- Recoveries added to the allowance
- Loan losses charged to the allowance

Balance at end of period

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5. Information about impaired loans as of June 30, 2001 and December 31, 2000 is as follows:

Impaired loans for which an allowance has been provided
Impaired loans for which no allowance has been provided

Total impaired loans

Allowance provided for impaired loans, included in the
allowance for loan losses

Average balance in impaired loans

Interest income recognized

There were no loans on nonaccrual status at June 30, 2001 or at December 31, 2000.

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

Between December 31, 2000 and June 30, 2001, total assets increased \$6,000,000. Total securities (held to maturity and available for sale) have increased \$6,000,000. Loans have increased \$9,300,000. The increases in these asset categories account for the \$13,000,000 decrease in securities purchased under agreements to resell and federal funds sold. Total deposits increased approximately \$2,200,000.

The June 30 annualized return on average assets is 1.15% compared to 1.25% at December 31. At June 30 the annualized return on average equity is 9.51% compared to 10.46% at December 31. The leverage capital (equity to assets) ratio is 12.12% at June 30 compared to 12.32% at December 31.

The table shown below is an analysis of the Corporation's allowance for loan losses. Net charge-offs for the Corporation have been very low when compared with the size of the total loan portfolio. Management monitors the loan portfolio on a continual basis with procedures that allow for problem loans and potentially problem loans to be highlighted and watched. Written reports detailing this loan information are prepared on a quarterly basis. Based on experience, the loan policies, and the current monitoring program, management believes the loan loss allowance is very adequate.

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(000 Omitted)

June 30, 2001

| | |
|--|---------|
| Balance at beginning of period | \$1,268 |
| Charge-offs: | |
| Commercial, financial and agricultural | 8 |
| Real estate - construction | -- |
| Real estate - mortgage | 6 |
| Consumer | 43 |
| | ----- |
| Total charge-offs | 57 |
| | ----- |
| Recoveries: | |
| Commercial, financial and agricultural | -- |
| Real estate - construction | -- |
| Real estate - mortgage | -- |
| Consumer | 14 |
| | ----- |
| Total recoveries | 14 |
| | ----- |
| Net charge-offs | 43 |
| Additions charged to operations | 40 |
| | ----- |
| Balance at end of period | \$1,265 |
| | ===== |
| Ratio of net charge-offs during the period to average loans outstanding during the period | .0483% |
| | ===== |

Loans are placed on nonaccrual status when a loan is specifically determined to be impaired or when principal or interest is delinquent for 90 days or more. Interest income generally is not recognized on specific impaired loans unless the likelihood of further loss is remote. Interest income on other nonaccrual loans is recognized only to the extent of interest payments received. Following is a table showing the risk elements in the loan portfolio.

| | |
|---|---------------|
| | (000 Omitted) |
| | June 30, 2001 |
| | ----- |
| Nonaccrual loans | \$ -- |
| Restructured loans | -- |
| Foreclosed properties | -- |
| | ----- |
| Total nonperforming assets | \$ -- |
| | ===== |
| Loans past due 90 days accruing interest | \$ 18 |
| | ===== |
| Allowance for loan losses to period end loans | 1.35% |
| | ===== |
| Nonperforming assets to period end loans and foreclosed properties | -- |
| | ===== |

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There were no loans on nonaccrual status at June 30, 2001.

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At June 30, 2001, other potential problem loans totalled \$26,907. Loans are viewed as potential problem loans according to the ability of such borrowers to comply with current repayment terms. These loans are subject to constant management attention, and their status is reviewed on a regular basis. Management has allocated a portion of the allowance for loan losses for these loans according to the review of the potential loss in each loan situation.

Although the overall increase in deposits at June 30 compared to December 31 was only \$2,200,000, the balances in the different types of deposit accounts fluctuated in various directions. Noninterest bearing accounts decreased \$1,000,000. Now accounts increased \$800,000, which included over \$500,000 in selected business accounts participating in our new daily cash management product. Daily these account balances are swept and invested in securities sold under agreements to repurchase, a product that pays higher interest than a regular Now account. Select checking balances decreased \$650,000. Money market balances increased \$200,000. Savings account balances increased \$1,850,000. Certificates of deposit balances increased \$1,000,000.

The comparison of the income statements for the three months and six months ended June 30, 2001 and 2000 shows similar changes in all income and expense categories. Net interest income in 2001 increased almost 9% when comparing the six month figures to 2000. Interest income has increased due to increased loan fees and increased loan volume. Interest expense has decreased slightly due to decreased interest rates. Net income for the six month period in 2001 has increased over 3% when compared to 2000.

Noninterest income has increased over 1.5% in 2001 compared to 2000. The increase is due to increased fees in certain areas and additional commissions on insurance due to increased sales of insurance. These increases were enough to counteract the over 5% decrease in fiduciary fees.

Noninterest expense increased over 10% in 2001 compared to 2000 for the six month period. Salaries and benefits increased due to annual salary increases, additional personnel, and increased insurance claims. Occupancy and furniture and equipment expenses increased due to the building and renovation projects completed in 2000. Advertising expense is up 46% in 2001 compared to 2000 due to creation of a new bank logo and replacement expense that accompanies such a change. Telephone expense has increased 14% in 2001 compared to 2000 due to increased service requirements because of growth and increased use of the internet system.

Liquid assets of the Corporation include cash and due from banks, securities purchased under agreements to resell, securities available for sale, and loans and investments maturing within one year. The Corporation's statement of cash flows details this liquidity. Net income after certain adjustments for noncash transactions provided cash from operating activities. Funds from maturity of investment securities, existing cash and financing activities were used to fund investing activities. Financing activities included increased deposits, increased securities sold under agreements to repurchase, and an advance from the Federal Home Loan Bank. Cash and cash equivalents decreased during this period, however liquidity of the Corporation is more than adequate to meet present and future financial obligations.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

There are no material legal proceedings to which the Registrant or its subsidiary, directors or officers is a party or by which they, or any of them, are threatened. All legal proceedings presently pending or threatened against Potomac Bancshares, Inc. and its subsidiary involve routine litigation incidental to the business of the Company or the subsidiary and are either not material in respect to the amount in controversy or fully covered by insurance.

Item 4. Submission of Matters to a Vote of Security-Holders.

The annual meeting of security-holders was held on April 24, 2001 and the following matters were submitted to the security-holders for a vote:

1. To elect a class of directors for a term of three years.
2. To ratify the selection by the board of directors of Yount, Hyde & Barbour, P.C., as independent Certified Public Accountants for the year 2001.
3. Any other business which may properly be brought before the meeting or any adjournment thereof.

Results of the voting in regard to the above listed matters were as follows:

| | Votes For | Votes Against | Votes Withheld | Total |
|--------------------------------|-----------|---------------|----------------|---------|
| | ----- | ----- | ----- | ----- |
| 1. J. Scott Boyd | 339,594 | None | 26,580 | 366,174 |
| John P. Burns, Jr. | 339,694 | None | 26,480 | 366,174 |
| 2. Ratification of accountants | 357,531 | 7,960 | 683 | 366,174 |

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

(a) Exhibits:

2. Plan of acquisition, reorganization, arrangement, liquidation or succession.
Not applicable
4. Instruments defining the rights of security holders, including indentures.
Not applicable
10. Material contracts.
Not applicable
11. Statement re: computation of per share earnings.
Not applicable
15. Letter on unaudited interim financial information.
Not applicable
18. Letter on change in accounting principles.

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Not applicable

19. Reports furnished to security holders.
Not applicable

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22. Published report regarding matters submitted to vote of security holders.
Not applicable

23. Consent of experts and counsel.
Not applicable

24. Power of attorney.
Not applicable

99. Additional exhibits.
Not applicable

(b) Reports on Form 8-K:

NONE

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SIGNATURES

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

POTOMAC BANCSHARES, INC.

Date August 6, 2001

/s/ Robert F. Baronner, Jr.

Robert F. Baronner, Jr., President & CEO

Date August 6, 2001

/s/ L. Gayle Marshall Johnson

L. Gayle Marshall Johnson, Vice
President & Chief Financial Officer