

First Bancorp, Inc /ME/
Form 10-K
March 12, 2012

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of The Securities Exchange Act of 1934
For the Fiscal Year ended December 31, 2011

Commission File Number 0-26589

THE FIRST BANCORP, INC.
(Exact name of Registrant as specified in its charter)

MAINE
(State or other jurisdiction of incorporation or
organization)

01-0404322
(I.R.S. Employer Identification No.)

MAIN STREET, DAMARISCOTTA, MAINE
(Address of principal executive offices)

04543
(Zip code)

(207) 563-3195
Registrant's telephone number, including area code

Securities registered pursuant to Section 12(g) of the Act:
Common Stock

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

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated
filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

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Large accelerated filer Accelerated filer Non-accelerated filer

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

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

Common Stock: \$131,301,000

Indicate the number of shares outstanding of each of the registrant's classes of common stock as of March 1, 2012

Common Stock: 9,826,376 shares

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ITEM 1. Discussion of Business

The First Bancorp, Inc. (the “Company”) was incorporated under the laws of the State of Maine on January 15, 1985, for the purpose of becoming the parent holding company of The First National Bank of Damariscotta, which was chartered as a national bank under the laws of the United States on May 30, 1864. At the Company’s Annual Meeting of Shareholders on April 30, 2008, the Company’s name was changed from First National Lincoln Corporation to The First Bancorp, Inc. On January 14, 2005, the acquisition of FNB Bankshares (“FNB”) of Bar Harbor, Maine, was completed, adding seven banking offices and one investment management office in Hancock and Washington counties of Maine. FNB’s subsidiary, The First National Bank of Bar Harbor, was merged into The First National Bank of Damariscotta at closing, and since January 31, 2005, the combined banks have operated under a new name: The First, N.A. (the “Bank”).

As of December 31, 2011, the Company’s securities consisted of one class of common stock, one class of preferred stock, and warrants to purchase common stock. At that date, there were 9,812,180 shares of common stock outstanding. In addition, there were 12,500 shares of cumulative perpetual preferred stock outstanding with a preference value of \$1,000 per share, all of which were issued to the U.S. Treasury under its Capital Purchase Program (the “CPP Shares”). Incident to the issuance of the CPP Shares, the Company issued to the U.S. Treasury warrants to purchase up to 225,904 shares of the Company’s common stock at a price per share of \$16.60 (the “Warrants”). The CPP Shares and the Warrants (and any shares of common stock issuable pursuant to the Warrants) are freely transferable by the U.S. Treasury to third parties and the Company has filed a registration statement with the Securities and Exchange Commission to allow for possible resale of such securities.

The common stock and preferred stock of the Bank are the principal assets of the Company, which has no other subsidiaries. The Bank’s capital stock consists of one class of common stock of which 120,000 shares, par value \$2.50 per share, are authorized and outstanding, and one class of non-cumulative perpetual preferred stock, \$1,000 preference value, of which 12,500 shares are authorized and outstanding. All of the Bank’s common stock and preferred stock is owned by the Company.

The Bank emphasizes personal service, and its customers are primarily small businesses and individuals to whom the Bank offers a wide variety of services, including deposit accounts, consumer and commercial and mortgage loans. The Bank has not made any material changes in its mode of conducting business during the past five years. The banking business in the Bank’s market area is seasonal with lower deposits in the winter and spring and higher deposits in the summer and fall. This swing is predictable and has not had a materially adverse effect on the Bank.

In addition to traditional banking services, the Company provides investment management and private banking services through First Advisors, which is an operating division of the Bank. First Advisors is focused on taking advantage of opportunities created as the larger banks have altered their personal service commitment to clients not meeting established account criteria. First Advisors is able to offer a comprehensive array of private banking, financial planning, investment management and trust services to individuals, businesses, non-profit organizations and municipalities of varying asset size, and to provide the highest level of personal service. The staff includes investment and trust professionals with extensive experience.

The financial services landscape has changed considerably over the past five years in the Bank’s primary market area. Two large out-of-state banks have continued to experience local change as a result of mergers and acquisitions at the regional and national level. Credit unions have continued to expand their membership and the scope of banking services offered. Non-banking entities such as brokerage houses, mortgage companies and insurance companies are offering very competitive products. Many of these entities and institutions have resources substantially greater than those available to the Bank and are not subject to the same regulatory restrictions as the Company and the Bank. The Company believes that there will continue to be a need for a bank in the Bank’s primary market area with local management having decision-making power and emphasizing loans to small and medium-sized businesses and to individuals. The Bank has concentrated on extending business loans to such customers in the Bank’s primary market area and to extending investment and trust services to clients with accounts of all sizes. The Bank’s Management also makes decisions based upon, among other things, the knowledge of the Bank’s employees regarding the communities and customers in the Bank’s primary market area. The individuals employed by the Bank, to a large extent, reside near

the branch offices and thus are generally familiar with their communities and customers. This is important in local decision-making and allows the Bank to respond to customer questions and concerns on a timely basis and fosters quality customer service.

The Bank has worked and will continue to work to position itself to be competitive in its market area. The Bank's ability to make decisions close to the marketplace, Management's commitment to providing quality banking products, the caliber of the professional staff, and the community involvement of the Bank's employees are all factors affecting the Bank's ability to be competitive.

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Supervision and Regulation

The Company is a financial holding company within the meaning of the Bank Holding Company Act of 1956, as amended (the “Act”), and section 225.82 of Regulation Y issued by the Board of Governors of the Federal Reserve System (the “Federal Reserve Board”), and is required to file with the Federal Reserve Board an annual report and other information required pursuant to the Act. The Company is subject to examination by the Federal Reserve Board. The Act requires the prior approval of the Federal Reserve Board for a financial holding company to acquire or hold more than a 5% voting interest in any bank, and controls interstate banking activities. The Act restricts The First Bancorp’s non-banking activities to those which are determined by the Federal Reserve Board to be closely related to banking. The Act does not place territorial restrictions on the activities of non-bank subsidiaries of financial holding companies. Virtually all of the Company’s cash revenues are generally derived from dividends paid to the Company by the Bank. These dividends are subject to various legal and regulatory restrictions which are summarized in Note 17 to the accompanying financial statements. The Bank is regulated by the Office of the Comptroller of the Currency (“OCC”) and is subject to the provisions of the National Bank Act. As a result, it must meet certain liquidity and capital requirements, which are discussed in the following sections.

Dodd-Frank Wall Street Reform and Consumer Protection Act

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Act”) was enacted on July 21, 2010. The Act created a new Consumer Financial Protection Bureau with power to promulgate and enforce consumer protection laws. Smaller institutions, those with \$10 billion or less in assets, are subject to the Consumer Financial Protection Bureau’s rule-writing authority, and existing depository institution regulatory agencies will retain examination and enforcement authority for such institutions. The Act also established a Financial Stability Oversight Council chaired by the Secretary of the Treasury with authority to identify institutions and practices that might pose a systemic risk and, among other things, included provisions affecting (1) corporate governance and executive compensation of all companies whose securities are registered with the SEC, (2) FDIC insurance assessments, (3) interchange fees for debit cards, which would be set by the Federal Reserve under a restrictive “reasonable and proportional cost” per transaction standard, (4) minimum capital levels for bank holding companies, subject to a grandfather clause for financial institutions with less than \$15 billion in assets, (5) derivative and proprietary trading by financial institutions, and (6) the resolution of large financial institutions. Compliance with these new laws and regulations may increase our costs, limit our ability to pursue attractive business opportunities, cause us to modify our strategies and business operations and increase our capital requirements and constraints, any of which may have a material adverse impact on our business, financial condition, liquidity or results of operations.

Customer Information Security

The Federal Deposit Insurance Corporation (“FDIC”), the OCC and other bank regulatory agencies have published guidelines (the “Guidelines”) establishing standards for safeguarding nonpublic personal information about customers that implement provisions of the Graham-Leach-Bliley Act (the “GLBA”). Among other things, the Guidelines require each financial institution, under the supervision and ongoing oversight of its Board of Directors or an appropriate committee thereof, to develop, implement and maintain a comprehensive written information security program designed to ensure the security and confidentiality of customer information, to protect against any anticipated threats or hazards to the security or integrity of such information, and to protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer.

Privacy

The FDIC, the OCC and other regulatory agencies have published privacy rules pursuant to provisions of the GLBA (“Privacy Rules”). The Privacy Rules, which govern the treatment of nonpublic personal information about consumers by financial institutions, require a financial institution to provide notice to customers (and other consumers in some circumstances) about its privacy policies and practices, describe the conditions under which a financial institution may

disclose nonpublic personal information to nonaffiliated third parties, and provide a method for consumers to prevent a financial institution from disclosing that information to most nonaffiliated third parties by “opting-out” of that disclosure, subject to certain exceptions.

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USA Patriot Act

The USA Patriot Act of 2001, designed to deny terrorists and others the ability to obtain anonymous access to the U.S. financial system, has significant implications for depository institutions, broker-dealers and other businesses involved in the transfer of money. The USA Patriot Act, together with the implementing regulations of various federal regulatory agencies, have caused financial institutions, including the Bank, to adopt and implement additional or amend existing policies and procedures with respect to, among other things, anti-money laundering compliance, suspicious activity and currency transaction reporting, customer identity verification and customer risk analysis. The statute and its underlying regulations also permit information sharing for counter-terrorist purposes between federal law enforcement agencies and financial institutions, as well as among financial institutions, subject to certain conditions, and require the Federal Reserve Board (and other federal banking agencies) to evaluate the effectiveness of an applicant in combating money laundering activities when considering applications filed under Section 3 of the Act or under the Bank Merger Act.

The Sarbanes-Oxley Act

The Sarbanes-Oxley Act of 2002 (“SOX”) implements a broad range of corporate governance and accounting measures for public companies (including publicly-held bank holding companies such as the Company) designed to promote honesty and transparency in corporate America and better protect investors from the type of corporate wrongdoings that occurred at Enron and WorldCom, among other companies. SOX’s principal provisions, many of which have been implemented through regulations released and policies and rules adopted by the securities exchanges in 2003 and 2004, provide for and include, among other things:

- The creation of an independent accounting oversight board;
 - Auditor independence provisions which restrict non-audit services that accountants may provide to clients;
- Additional corporate governance and responsibility measures, including the requirement that the chief executive officer and chief financial officer of a public company certify financial statements;
- The forfeiture of bonuses or other incentive-based compensation and profits from the sale of an issuer’s securities by directors and senior officers in the twelve-month period following initial publication of any financial statements that later require restatement;
- An increase in the oversight of, and enhancement of certain requirements relating to, audit committees of public companies and how they interact with the public company’s independent auditors;
- Requirements that audit committee members must be independent and are barred from accepting consulting, advisory or other compensatory fees from the issuer;
- Requirements that companies disclose whether at least one member of the audit committee is a ‘financial expert’ (as such term is defined by the Securities and Exchange Commission (“SEC”)) and if not, why not;
- Expanded disclosure requirements for corporate insiders, including accelerated reporting of stock transactions by insiders and a prohibition on insider trading during pension blackout periods;
- A prohibition on personal loans to directors and officers, except certain loans made by insured financial institutions, such as the Bank, on nonpreferential terms and in compliance with bank regulatory requirements;
 - Disclosure of a code of ethics and filing a Form 8-K in the event of a change or waiver of such code; and
 - A range of enhanced penalties for fraud and other violations.

The Company complies with the provisions of SOX and its underlying regulations. Management believes that such compliance efforts have strengthened the Company’s overall corporate governance structure and does not expect that such compliance has to date had, or will in the future have, a material impact on the Company’s results of operations or financial condition.

Capital Requirements

The OCC has established guidelines with respect to the maintenance of appropriate levels of capital by FDIC-insured banks. The Federal Reserve Board has established substantially identical guidelines with respect to the maintenance of appropriate levels of capital, on a consolidated basis, by bank holding companies. If a banking organization’s capital

levels fall below the minimum requirements established by such guidelines, a bank or bank holding company will be expected to develop and implement a plan acceptable to the FDIC or the Federal Reserve Board, respectively, to achieve adequate levels of capital within a reasonable period, and may be denied approval to acquire or establish additional banks or non-bank businesses, merge with other institutions or open branch facilities until such capital levels are achieved. Federal regulations require federal bank regulators to take “prompt corrective action” with respect to insured depository institutions that fail to satisfy minimum capital requirements and imposes significant restrictions on such institutions. See “Prompt Corrective Action” below.

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Leverage Capital Ratio

The regulations of the OCC require national banks to maintain a minimum “Leverage Capital Ratio” or “Tier 1 Capital” (as defined in the Risk-Based Capital Guidelines discussed in the following paragraphs) to Total Assets of 4.0%. Any bank experiencing or anticipating significant growth is expected to maintain capital well above the minimum levels. The Federal Reserve Board’s guidelines impose substantially similar leverage capital requirements on bank holding companies on a consolidated basis. It is possible that banking regulators may increase minimum capital requirements for banks should the current economic situation persist or worsen.

Risk-Based Capital Requirements

OCC regulations also require national banks to maintain minimum capital levels as a percentage of a bank’s risk-adjusted assets. A bank’s qualifying total capital (“Total Capital”) for this purpose may include two components: “Core” (Tier 1) Capital and “Supplementary” (Tier 2) Capital. Core Capital consists primarily of common stockholders’ equity, which generally includes common stock, related surplus and retained earnings, certain non-cumulative perpetual preferred stock and related surplus, and minority interests in the equity accounts of consolidated subsidiaries, and (subject to certain limitations) mortgage servicing rights and purchased credit card relationships, less all other intangible assets (primarily goodwill). Supplementary Capital elements include, subject to certain limitations, a portion of the allowance for loan losses, perpetual preferred stock that does not qualify for inclusion in Tier 1 capital, long-term preferred stock with an original maturity of at least 20 years and related surplus, certain forms of perpetual debt and mandatory convertible securities, and certain forms of subordinated debt and intermediate-term preferred stock.

The risk-based capital rules assign a bank’s balance sheet assets and the credit equivalent amounts of the bank’s off-balance sheet obligations to one of four risk categories, weighted at 0%, 20%, 50% or 100%, as applicable. Applying these risk-weights to each category of the bank’s balance sheet assets and to the credit equivalent amounts of the bank’s off-balance sheet obligations and summing the totals results in the amount of the bank’s total Risk-Adjusted Assets for purposes of the risk-based capital requirements. Risk-Adjusted Assets can either exceed or be less than reported balance sheet assets, depending on the risk profile of the banking organization. Risk-Adjusted Assets for institutions such as the Bank will generally be less than reported balance sheet assets because its retail banking activities include proportionally more residential mortgage loans, many of its investment securities have a low risk weighting and there is a relatively small volume of off-balance sheet obligations.

The risk-based capital regulations require all banks to maintain a minimum ratio of Total Capital to Risk-Adjusted Assets of 8.0%, of which at least one-half (4.0%) must be Core (Tier 1) Capital. For the purpose of calculating these ratios: (i) a banking organization’s Supplementary Capital eligible for inclusion in Total Capital is limited to no more than 100% of Core Capital; and (ii) the aggregate amount of certain types of Supplementary Capital eligible for inclusion in Total Capital is further limited. For example, the regulations limit the portion of the allowance for loan losses eligible for inclusion in Total Capital to 1.25% of Risk-Adjusted Assets. The Federal Reserve Board has established substantially identical risk-based capital requirements, which are applied to bank holding companies on a consolidated basis. The risk-based capital regulations explicitly provide for the consideration of interest rate risk in the overall evaluation of a bank’s capital adequacy to ensure that banks effectively measure and monitor their interest rate risk, and that they maintain capital adequate for that risk. A bank deemed by its federal banking regulator to have excessive interest rate risk exposure may be required to maintain additional capital (that is, capital in excess of the minimum ratios discussed above). The Bank believes, based on its level of interest rate risk exposure, that this provision will not have a material adverse effect on it.

On August 24, 2011, the Company repurchased \$12.5 million of the Company’s Fixed Rate Cumulative Perpetual Preferred Stock, Series A, having a liquidation preference of \$1,000 per share. This stock was issued to the United States Treasury on January 9, 2009 under its Capital Purchase Program (the “CPP Shares”). The repurchase transaction was approved by the Federal Reserve Bank of Boston, the Company’s primary regulator, as well as the Bank’s primary regulator, the Office of the Comptroller of the Currency, based on continued strong capital ratios after the repayment. Almost all of the repayment was made from retained earnings accumulated since the CPP Shares were issued in 2009.

After the repurchase, \$12.5 million of the originally issued CPP shares remains outstanding, as do all of the related warrants described above and below.

The CPP Shares call for cumulative dividends at a rate of 5.0% per year for the first five years, and at a rate of 9.0% per year in following years, payable quarterly in arrears on February 15, May 15, August 15 and November 15 of each year. Incident to such issuance, the Company issued to the U.S. Treasury warrants to purchase up to 225,904 shares of the Company's common stock at a price per share of \$16.60 (subject to adjustment). The CPP Shares and the related Warrants (and any shares of common stock issuable pursuant to the Warrants) are freely transferable by the U.S. Treasury to third parties and the Company has filed a registration statement with the SEC to allow for possible resale of such securities. The CPP Shares qualify as Tier 1 capital on the Company's books for regulatory purposes and rank senior to the Company's common stock and senior or at an equal level in the Company's capital structure to any other shares of preferred stock the Company may issue in the future. The Company may redeem the CPP Shares at any time

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using any funds available to the Company, and any redemption would be subject to the prior approval of the Federal Reserve Bank of Boston. The minimum amount that may be redeemed is 25% of the original CPP investment. The CPP Shares are “perpetual” preferred stock, which means that neither the U.S. Treasury nor any subsequent holder would have a right to require that the Company redeem any of the shares.

On December 31, 2011, the Company’s consolidated Total and Tier 1 Risk-Based Capital Ratios were 15.66% and 14.40%, respectively, and its Leverage Capital Ratio was 8.32%. Based on the above figures and accompanying discussion, the Company exceeds all regulatory capital requirements and is considered well capitalized.

Prompt Corrective Action

The Federal Deposit Insurance Corporation Improvement Act of 1991 (“FDICIA”) requires, among other things, that the federal banking regulators take “prompt corrective action” with respect to, and imposes significant restrictions on, any bank that fails to satisfy its applicable minimum capital requirements. FDICIA establishes five capital categories consisting of “well capitalized,” “adequately capitalized,” “undercapitalized,” “significantly undercapitalized” and “critically undercapitalized.” Under applicable regulations, a bank that has a Total Risk-Based Capital Ratio of 10.0% or greater, a Tier 1 Risk-Based Capital Ratio of 6.0% or greater and a Leverage Capital Ratio of 5.0% or greater, and is not subject to any written agreement, order, capital directive or prompt corrective action directive to meet and maintain a specific capital level for any capital measure is deemed to be “well capitalized.” A bank that has a Total Risk-Based Capital Ratio of 8.0% or greater, a Tier 1 Risk-Based Capital Ratio of 4.0% or greater and a Leverage Capital Ratio of 4.0% (or 3% for banks with the highest regulatory examination rating that are not experiencing or anticipating significant growth or expansion) or greater and does not meet the definition of a well-capitalized bank is considered to be “adequately capitalized.” A bank that has a Total Risk-Based Capital Ratio of less than 8.0% or has a Tier 1 Risk-Based Capital Ratio that is less than 4.0%, except as noted above, or a Leverage Capital Ratio of less than 4.0% is considered “undercapitalized.” A bank that has a Total Risk-Based Capital Ratio of less than 6.0%, or a Tier 1 Risk-Based Capital Ratio that is less than 3.0% or a Leverage Capital Ratio that is less than 3.0% is considered to be “significantly undercapitalized,” and a bank that has a ratio of tangible equity to total assets equal to or less than 2% is deemed to be “critically undercapitalized.” A bank may be deemed to be in a capital category lower than is indicated by its actual capital position if it is determined to be in an unsafe or unsound condition or receives an unsatisfactory examination rating. FDICIA generally prohibits a bank from making capital distributions (including payment of dividends) or paying management fees to controlling stockholders or their affiliates if, after such payment, the bank would be undercapitalized.

Under FDICIA and the applicable implementing regulations, an undercapitalized bank will be (i) subject to increased monitoring by its primary federal banking regulator; (ii) required to submit to its primary federal banking regulator an acceptable capital restoration plan (guaranteed, subject to certain limits, by the bank’s holding company) within 45 days of being classified as undercapitalized; (iii) subject to strict asset growth limitations; and (iv) required to obtain prior regulatory approval for certain acquisitions, transactions not in the ordinary course of business, and entries into new lines of business. In addition to the foregoing, the primary federal banking regulator may issue a “prompt corrective action directive” to any undercapitalized institution. Such a directive may (i) require sale or re-capitalization of the bank, (ii) impose additional restrictions on transactions between the bank and its affiliates, (iii) limit interest rates paid by the bank on deposits, (iv) limit asset growth and other activities, (v) require divestiture of subsidiaries, (vi) require replacement of directors and officers, and (vii) restrict capital distributions by the bank’s parent holding company. In addition to the foregoing, a significantly undercapitalized institution may not award bonuses or increases in compensation to its senior executive officers until it has submitted an acceptable capital restoration plan and received approval from its primary federal banking regulator.

No later than 90 days after an institution becomes critically undercapitalized, the primary federal banking regulator for the institution must appoint a receiver or, with the concurrence of the FDIC, a conservator, unless the agency, with the concurrence of the FDIC, determines that the purpose of the prompt corrective action provisions would be better served by another course of action. FDICIA requires that any alternative determination be “documented” and reassessed on a periodic basis. Notwithstanding the foregoing, a receiver must be appointed after 270 days unless the appropriate

federal banking agency and the FDIC certify that the institution is viable and not expected to fail.

Deposit Insurance Assessments

The Bank's deposits are insured by the Bank Insurance Fund of the FDIC to the current legal maximum of \$250,000 generally for each insured depositor. Non-interest bearing checking accounts have unlimited coverage. The Federal Deposit Insurance Act, as amended by the Federal Deposit Insurance Reform Act of 2005, provides that the FDIC shall set deposit insurance assessment rates. In 2006, the former Bank Insurance Fund merged with the Savings Association Insurance Fund to create the Deposit Insurance Fund, or DIF. The Act eliminated the requirement that the FDIC set deposit insurance assessment rates on a semi-annual basis at a level sufficient to increase the ratio of BIF reserves to BIF-insured deposits to at least 1.25%. Under the Act, the FDIC annually sets the designated reserve ratio (DRR) of

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DIF reserves to DIF-insured deposits between 1.15% and 1.50%, subject to public comment, based on appropriate considerations including risk of losses and economic conditions such that the ratio would increase during favorable economic conditions and decrease during less favorable conditions, thus avoiding sharp swings in assessment rates. Past bank failures and reserves against future failures lowered the FDIC insurance fund. To keep the fund from falling to a level that could undermine public confidence, there was a one-time special insurance premium charged to all FDIC-insured banks of 0.05% on each insured depository institution's total assets minus Tier 1 capital as of June 30, 2009. To ensure that the reserve ratio returns to target levels within the statutorily mandated period of time, in 2009 the FDIC Board took the following steps:

Extend to eight years the Amended Restoration Plan to raise the Deposit Insurance Fund reserve ratio to 1.15 percent and require all institutions to prepay, on December 30, 2009, their estimated risk-based assessments for the fourth quarter of 2009 and for all of 2010, 2011, and 2012, at the same time that institutions pay their regular quarterly deposit insurance assessments for the third quarter of 2009. An institution would initially account for the prepaid assessments as a prepaid expense and amortize this amount over a three-year period.

In December 2010, the FDIC Board adopted a final rule establishing the long-term Designated Reserve Ratio at 2.00% of insured deposits. In February 2011, the FDIC Board approved a final rule that changed the assessment base from domestic deposits to average assets minus average tangible equity, adopted a new large-bank pricing assessment scheme, and set a target size for the Deposit Insurance Fund. The changes went into effect beginning with the second quarter of 2011 and the new levels of assessment became payable at the end of September of 2011.

The rule also implements a lower assessment rate schedule when the fund reaches 1.15 percent (so that the average rate over time should be about 8.5 basis points) and, in lieu of dividends, provides for a lower rate schedule when the reserve ratio reaches 2 percent and 2.5 percent. The rule defines tangible equity as Tier 1 capital. The rule requires banks under \$1 billion in assets to report average weekly balances during the calendar quarter, unless they elect to report daily averages.

The rule lowered overall assessment rates in order to generate the same approximate amount of revenue under the new larger base as was raised under the old base. The assessment rates in total will be between 2.5 and 9 basis points on the broader base for banks in the lowest risk category, and 30 to 45 basis points for banks in the highest risk category. The FDIC noted that while the rule is overall revenue neutral, it will, in aggregate, increase the share of assessments paid by large institutions, consistent with the express intent of Congress. Based on September 30, 2010, data, the FDIC said that the share of overall dollar assessments paid to FDIC would increase from 70 to 79 percent for banks over \$10 billion and from 48 percent to 57 percent for banks over with assets over \$100 billion. The FDIC also acknowledged that "many large institutions would experience a significant change in their overall assessment." The FDIC reported that, under the combined effect of both the assessment base change and the new large bank risk-based formula, 51 banks with assets over \$10 billion would pay more and 59 would pay less. The FDIC also noted that only 84 banks with assets under \$10 billion would pay higher assessments.

The final rule also created a scorecard-based assessment system for banks with more than \$10 billion in assets. The scorecards include financial measures that the FDIC believes are predictive of long-term performance. In a change from the earlier proposals, the brokered deposit adjustment does not apply to banks over \$10 billion that are well-capitalized and with CAMELS ratings of 1 or 2, consistent with the treatment for smaller banks.

Brokered Deposits and Pass-Through Deposit Insurance Limitations

Under FDICIA, a bank cannot accept brokered deposits unless it either (i) is "Well Capitalized" or (ii) is "Adequately Capitalized" and has received a written waiver from its primary federal banking regulator. For this purpose, "Well Capitalized" and "Adequately Capitalized" have the same definitions as in the Prompt Corrective Action regulations. See "Prompt Corrective Action" above. Banks that are not in the "Well Capitalized" category are subject to certain limits on the rates of interest they may offer on any deposits (whether or not obtained through a third-party deposit broker).

Pass-through insurance coverage is not available in banks that do not satisfy the requirements for acceptance of brokered deposits, except that pass-through insurance coverage will be provided for employee benefit plan deposits in institutions which at the time of acceptance of the deposit meet all applicable regulatory capital requirements and send

written notice to their depositors that their funds are eligible for pass-through deposit insurance. The Bank currently accepts brokered deposits.

Real Estate Lending Standards

FDICIA requires the federal bank regulatory agencies to adopt uniform real estate lending standards. The FDIC and the OCC have adopted regulations which establish supervisory limitations on Loan-to-Value (“LTV”) ratios in real estate loans by FDIC-insured banks, including national banks. The regulations require banks to establish LTV ratio limitations within or below the prescribed uniform range of supervisory limits.

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Standards for Safety and Soundness

Pursuant to FDICIA the federal bank regulatory agencies have prescribed, by regulation, standards and guidelines for all insured depository institutions and depository institution holding companies relating to: (i) internal controls, information systems and internal audit systems; (ii) loan documentation; (iii) credit underwriting; (iv) interest rate risk exposure; (v) asset growth; and (vi) compensation, fees and benefits. The compensation standards prohibit employment contracts, compensation or benefit arrangements, stock option plans, fee arrangements or other compensatory arrangements that would provide “excessive” compensation, fees or benefits, or that could lead to material financial loss. In addition, the federal bank regulatory agencies are required by FDICIA to prescribe standards specifying: (i) maximum classified assets to capital ratios; (ii) minimum earnings sufficient to absorb losses without impairing capital; and (iii) to the extent feasible, a minimum ratio of market value to book value for publicly-traded shares of depository institutions and depository institution holding companies.

Consumer Protection Provisions

FDICIA also includes provisions requiring advance notice to regulators and customers for any proposed branch closing and authorizing (subject to future appropriation of the necessary funds) reduced insurance assessments for institutions offering “lifeline” banking accounts or engaged in lending in distressed communities. FDICIA also includes provisions requiring depository institutions to make additional and uniform disclosures to depositors with respect to the rates of interest, fees and other terms applicable to consumer deposit accounts.

FDIC Waiver of Certain Regulatory Requirements

The FDIC issued a rule, effective on September 22, 2003, that includes a waiver provision which grants the FDIC Board of Directors extremely broad discretionary authority to waive FDIC regulatory provisions that are not specifically mandated by statute or by a separate regulation.

Impact of Monetary Policy

The monetary policies of regulatory authorities, including the Federal Reserve Board, have a significant effect on the operating results of banks and bank holding companies. Through open market securities transactions and changes in its discount rate and reserve requirements, the Board of Governors exerts considerable influence over the cost and availability of funds for lending and investment. The nature of future monetary policies and the effect of such policies on the future business and earnings of the Company and the Bank cannot be predicted. See Item 7 - Management’s Discussion and Analysis of Financial Condition and Results of Operations, regarding the Bank’s net interest margin and the effect of interest-rate volatility on future earnings.

Employees

At December 31, 2011, the Company had 210 employees and full-time equivalency of 203 employees. The Company enjoys good relations with its employees. A variety of employee benefits, including health, group life and disability income, a defined contribution retirement plan, and an incentive bonus plan, are available to qualifying officers and other employees.

Company Website

The Company maintains a website at www.thefirstbancorp.com where it makes available, free of charge, its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, as well as all Section 16 reports on Forms 3, 4, and 5, as soon as reasonably practicable after such reports are electronically filed with, or furnished to, the SEC. The Company’s reports filed with, or furnished to, the SEC are also available at the SEC’s website at www.sec.gov. Information contained on the Company’s website does not constitute a part of this report. Interactive reports for our 10-K and 10-Q filings are available in XBRL format at the Company’s website.

ITEM 1A. Risk Factors

The risks and uncertainties described below are not the only ones the Company faces. Additional risks and uncertainties that we are unaware of, or that we currently deem immaterial, also may become important factors that affect us and our business. If any of these risks were to occur, our business, financial condition or results of operations could be materially and adversely affected.

The Dodd-Frank Act and related regulations may adversely affect our business, financial condition, liquidity or results of operations.

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Act”) was enacted on July 21, 2010. The Act created a new Consumer Financial Protection Bureau with power to promulgate and enforce consumer protection laws. Smaller institutions, those with \$10 billion or less in assets (such as the Company), are subject to the Consumer Financial Protection Bureau’s rule-writing authority, and existing depository institution regulatory agencies retain examination and enforcement authority for such institutions. The Act also established a Financial Stability Oversight Council chaired by the Secretary of the Treasury with authority to identify institutions and practices that might pose a systemic risk and, among other things, included provisions affecting (1) corporate governance and executive compensation of all companies whose securities are registered with the SEC, (2) FDIC insurance assessments, (3) interchange fees for debit cards, which will be set by the Federal Reserve under a restrictive “reasonable and proportional cost” per transaction standard, (4) minimum capital levels for bank holding companies, subject to a grandfather clause for financial institutions (such as the Company) with less than \$15 billion in assets, and (5) derivative and proprietary trading by financial institutions.

Financial Stability – addressed the core purpose of the bill by creating a new oversight regulator, the Financial Stability Oversight Council. This council of regulators monitors the financial system for “systemic risk” and will determine which entities pose significant systemic risk. Generally speaking, it makes recommendations to regulators for the implementation of the increased risk standards, also known as prudential regulation, to be applied to bank holding companies with total consolidated assets of \$50 billion or more and to designated nonbanks. The Act grandfathers trust preferred securities issued before May 19, 2010 by bank holding companies with less than \$15 billion in total assets.

Orderly Liquidation Authority –established a framework for the liquidation by the Federal Deposit Insurance Corporation (“FDIC”) of large institutions that pose systemic risk. The Treasury supplies liquidity for the liquidation that must be paid back in 60 months.

Enhancing Financial Institution Safety and Soundness – merged the Office of Thrift Supervision (“OTS”) into the Office of the Comptroller of the Currency (“OCC”), the Bank’s primary regulator. The regulatory responsibilities for former OTS banks were spread among other regulators: The Federal Reserve now regulates former OTS savings and loan holding companies, the OCC now regulates former OTS federal savings associations, and the FDIC now regulates former OTS state-chartered savings associations. For the Bank, a key provision in this title changes the assessment base for deposit insurance. Before, the base was domestic deposits less tangible equity. The new base is average consolidated total assets minus average tangible equity. The result is that larger financial institutions, which have more non-deposit liabilities, now pay a greater percentage of the aggregate insurance assessment and smaller banks (such as the Bank) will pay less than they would have. Another key provision for the Bank was the permanent increase in FDIC deposit insurance per depositor in the aggregate from \$100,000 to \$250,000. The Act increases the minimum reserve ratio for the Deposit Insurance Fund from 1.15 percent to 1.35 percent, but exempts institutions (such as the Bank) with assets of less than \$10 billion from the cost of the increase.

Improvements to Regulation of Bank and Savings Association Holding Companies and Depository Institutions –implemented the so-called modified Volcker Rule. The rule limits the ability of certain bank and bank-related entities to engage in proprietary trading or investing in hedge funds and private equity funds to 3 percent of the entity’s Tier 1 capital, among other restrictions. “Proprietary trading” is defined to include the purchase or sale of any security, any derivative, any contract for the sale of a commodity for future delivery, or option on such instrument. The key provisions in this title are a moratorium on deposit insurance applications for three years, ending July 21, 2013, for new credit card banks, industrial loan companies and trust banks owned by commercial companies, the expansion of the definition of affiliate transactions to cover certain kinds of security transactions such as repurchase agreement, derivative transaction and securities borrowing; and the codification of the source of strength doctrine, the long-time

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view of the Federal Reserve that a holding company should serve as a source of financial strength for its subsidiary banks.

Regulation of Over-the-Counter Swaps Markets – imposed exchange trading for derivatives contracts and imposes new capital and margin requirements and various reporting obligations on Over The Counter (“OTC”) swap dealers and major OTC swap participants. For the Bank, the most important provision in this title levels the competitive playing field by prohibiting the Federal Reserve or the FDIC from providing assistance to insured depository institutions involved in the swaps markets, with certain exceptions.

Payment, Clearing, and Settlement Supervision – allowed for a systemic approach to certain financial market payment, payment, clearing and settlement systems. Designation of a large financial institution as “systemically important” will require a two-thirds vote of the Financial Stability Oversight Council.

Investor Protections and Improvements to the Regulation of Securities – has a number of provisions intended to protect investors, including for example: risk retention requirements for certain asset-backed securities; reforms to regulation of credit rating agencies; establishing an Investor Advisory Committee and an Office of Investor Advocate, and requiring the SEC to study whether a fiduciary duty standard of care for broker-dealers providing personalized investment advice to a retail customer should be created. For the Bank, the most important section of this Title established a number of changes to corporate governance procedures for public companies. The most important of these are: proxy access requirements for shareholders; disclosures about the failure to separate the roles of the chair of board and chief executive officer; non-binding shareholder voting on executive compensation; the establishment of an independent compensation committee; executive compensation disclosures and clawbacks. In addition, the Federal Reserve has requested comment on proposed regulations regarding incentive-based pay practices that will apply to institutions (such as the Bank) with more than \$1 billion in assets.

Bureau of Consumer Financial Protection – the most important Title in the Act for the Bank. It has altered in dramatic fashion the way consumer credit is regulated, moving from the previous framework of the federal regulation of disclosure and the state law regulation of fairness and suitability, to an overall, nationwide federal suitability framework. It establishes the Bureau of Consumer Financial Protection, an independent entity housed within the Federal Reserve in order to provide a source of funding (initially \$500 million) and gave the Bureau the authority to prohibit practices that it finds to be “unfair,” “deceptive,” or “abusive” in addition to requiring certain disclosures. The words “unfair” and “deceptive” appear to reference and incorporate similar words in the enabling legislation of the Federal Trade Commission and some state consumer legislation. For the Bank, in addition to creation of the Bureau, this Title also contains a number of other important provisions. It limited interchange fees for debit card transactions (including those involved with certain prepaid card products) to an amount established as reasonable under regulations issued by the Federal Reserve. Cards issued by banks with less than \$10 billion in assets are exempt from this requirement although this exemption has been criticized as being ineffective because small banks may be forced by market dynamics to match the rates being offered by their larger competitors. Another key change for the Bank is the Act’s treatment of preemption. Essentially, the Act will undo recent court decisions and OCC guidance that expanded the application of preemption to subsidiaries of national banks. The standard for the preemption of state law is to return to the one enunciated in a well-known court decision, *Barnet Bank v. Nelson*: “irreconcilable conflict” and “stand as an obstacle to the accomplishment” of the purpose of the federal law. The Act also codified the result in a recent U.S. Supreme Court decision that the visitorial powers provisions of the National Bank Act do not limit the authority of state attorneys general to bring actions against national banks to enforce state consumer protection laws.

Federal Reserve System Revisions – gives the Government Accountability Office authority to conduct a one-time audit of the Federal Reserve’s emergency lending during the credit crisis and gives the GAO other auditing responsibilities over the Federal Reserve. The title also tightens the conditions under which the Fed may provide emergency assistance to institutions and authorizes the FDIC to guarantee debts of banks and bank holding companies.

Improving Access to Mainstream Financial Institutions – is intended to provide alternatives to payday loans. This title is intended to encourage low-and moderate-income individuals to create accounts in insured depository institutions and it creates a program to provide low-cost loans of \$2,500 or less.

Mortgage Reform and Anti-Predatory Lending Act – places new regulations on mortgage originators and imposes new disclosure requirements and appraisal reforms, the most important of which are: the creation of a mortgage originator duty of care, the establishment of certain underwriting requirements so that at the time of origination the consumer has a reasonable ability to repay the loan; the creation of document requirements intended to eliminate “no document” and “low document” loans, the prohibition of steering incentives for mortgage originators; a prohibition on

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yield spread premiums, and prepayment penalties in many cases; and a provision that allows borrowers to assert as a foreclosure defense a contention that the lender violated the anti-steering restrictions or the reasonable repayment requirements.

There can be no assurance that the Dodd-Frank Act and other Government programs will stabilize the U.S. financial system.

There can also be no assurance as to the actual impact that the Dodd-Frank Act and other programs will continue to have on the financial markets, including credit availability. The failure of the Dodd-Frank Act or other programs to stabilize the financial markets and a continuation or worsening of current financial market conditions could materially and adversely affect our business, financial condition, results of operations, access to credit or the trading price of our voting common stock.

There can be no assurance that the Emergency Economic Stabilization Act (“EESA”), the American Recovery and Reinvestment Act of 2009, and other initiatives undertaken by the United States government to restore liquidity and stability to the U.S. financial system will help stabilize and stimulate the U.S. financial system.

Among the purposes of these legislative and regulatory actions is to stabilize the U.S. banking system. The EESA and the other regulatory initiatives described above may not have their desired effects. If the volatility in the markets continues and economic conditions fail to improve or worsen, our business, financial condition and results of operations could be materially and adversely affected. There can be no assurance regarding the actual impact that the EESA or the American Recovery and Reinvestment Act of 2009, or other programs and other initiatives undertaken by the U.S. government, will have on the financial markets; the extreme levels of volatility and limited credit availability currently being experienced may persist. The failure of the EESA or other government programs to help stabilize the financial markets and a continuation or worsening of current financial market conditions could have a material adverse effect on the Company. In the event turmoil in the financial markets continues, we may experience a material adverse effect from (1) continued or accelerated disruption and volatility in financial markets, (2) continued capital and liquidity concerns regarding financial institutions generally and our transaction counterparties specifically, (3) limitations resulting from further governmental action to stabilize or provide additional regulation of the financial system, or (4) recessionary conditions that are deeper or last longer than currently anticipated.

Recent negative developments in the financial services industry and U.S. and global credit markets may adversely impact our operations and results.

Negative developments between 2007 and 2011 in the capital markets have resulted in uncertainty in the financial markets in general with the expectation of the general economic downturn continuing in 2012 and perhaps beyond 2012. The impact of this situation, together with concerns regarding the financial strength of financial institutions, has led to distress in credit markets and issues relating to liquidity among financial institutions. Some financial institutions around the world and the United States have failed; others have been forced to seek acquisition partners. Loan portfolio value has deteriorated at many institutions resulting from, amongst other factors, a weak economy and a decline in the value of the collateral supporting their loans. The competition for our deposits has increased significantly due to liquidity concerns at many of these same institutions. Stock prices of bank holding companies, like ours, have been negatively affected by the current condition of the financial markets, as has our ability, if needed, to raise capital or borrow in the debt markets compared to recent years. The United States and other governments have taken unprecedented steps to try to stabilize the financial system, including investing in financial institutions. Negative developments in the financial services industry and the impact of new legislation in response to those developments could negatively impact our operations by restricting our business operations, including our ability to originate or sell loans, and adversely impact our financial performance.

The downgrade of the U.S. credit rating and Europe's debt crisis could have a material adverse effect on our business, financial condition and liquidity.

Standard & Poor's lowered its long term sovereign credit rating on the United States of America from AAA to AA+ on August 5, 2011. A further downgrade or a downgrade by other rating agencies could have a material adverse impact on financial markets and economic conditions in the United States and worldwide. Any such adverse impact could have a material adverse effect on our liquidity, financial condition and results of operations. Many of our investment securities are issued by U.S. government agencies and U.S. government sponsored entities. In addition, the possibility that certain European Union ("EU") member states will default on their debt obligations have negatively impacted economic conditions and global markets. The continued uncertainty over the outcome of international and the EU's financial support programs and the possibility that other EU member states may experience similar financial troubles could further disrupt global markets. The negative impact on economic conditions and global markets could also have a material adverse effect on our liquidity, financial condition and results of operations.

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Lack of loan demand may impact net interest income.

During the past two years the loan portfolio has decreased \$70.0 million. Loan demand in the Bank's market area has been limited as a result of continued weak economic conditions. This has had the greatest impact on the commercial loan portfolio. In addition, in order to reduce the Bank's exposure to interest rate risk, the Bank has sold residential mortgages to the secondary market that have been refinanced by borrowers seeking to take advantage of lower interest rates. Should this trend continue, net interest income may be negatively impacted if loans are replaced by lower-yielding investment securities or if the balance sheet is allowed to shrink.

The soundness of other financial services institutions may adversely affect our credit risk.

We rely on other financial services institutions through trading, clearing, counterparty, and other relationships. We maintain limits and monitor concentration levels of our counterparties as specified in our internal policies. Our reliance on other financial services institutions exposes us to credit risk in the event of default by these institutions or counterparties. These losses could adversely affect our results of operations and financial condition.

Declines in value may adversely impact the investment portfolio.

As of December 31, 2011, we had \$286.2 million and \$122.7 million in available for sale and held to maturity investment securities, respectively. We may be required to record impairment charges on our investment securities if they suffer a decline in value that is considered other-than-temporary. Numerous factors, including lack of liquidity for re-sales of certain investment securities, absence of reliable pricing information for investment securities, adverse changes in business climate, adverse actions by regulators, or unanticipated changes in the competitive environment could have a negative effect on our investment portfolio in future periods. If an impairment charge is significant enough it could affect the ability of the Bank to renew funding. This could have a material adverse effect on our liquidity and the Bank's ability to upstream dividends to the Company and for the Company to then pay dividends to shareholders. It could also negatively impact our regulatory capital ratios and result in our not being classified as "well-capitalized" for regulatory purposes.

Our business has been and may Continue to be adversely affected by conditions in the financial markets and economic conditions generally.

Negative developments in 2008 and 2009 in the financial services industry have resulted in uncertainty in the financial markets in general and a related general economic downturn, which have continued into 2012. In addition, as a consequence of the recent U.S. recession, businesses across a wide range of industries have faced serious difficulties due to the decrease in consumer spending, reduced consumer confidence brought on by deflated home values, among other things, and reduced liquidity in the credit markets. Unemployment also increased significantly over the past several years.

As a result of these financial and economic crises, many lending institutions, including us, have experienced in recent years declines in the performance of their loans, including construction, land development and land loans, commercial real estate loans and other commercial and consumer loans (see "Credit & Credit Risk" in ITEM 7: Management's Discussion and Analysis of Financial Condition and Results of Operations). Moreover, competition among depository institutions for core deposits and quality loans has increased significantly. In addition, the values of real estate collateral supporting many commercial loans and home mortgages have declined and may continue to decline. Banks and bank holding company stock prices have been negatively affected, and the ability of banks and bank holding companies to raise capital or borrow in the debt markets has been more difficult compared to years prior to the

economic downturn. As a result, bank regulatory agencies have been and are expected to continue to be very aggressive in responding to concerns and trends identified in examinations, including the issuance of formal or informal enforcement actions or orders. The impact of new legislation in response to these developments may negatively impact our operations by restricting our business operations, including our ability to originate or sell loans, and adversely impact our financial performance or our stock price.

In addition, further negative market developments may affect consumer confidence levels and may cause adverse changes in payment patterns, causing increases in delinquencies and default rates, which may impact our charge-offs and provision for credit losses. A worsening of these conditions would likely exacerbate the adverse effects of these difficult market conditions on us and others in the financial services industry.

Overall, during the past four years, the general business environment has had an adverse effect on our business, and there can be no assurance that the environment will improve in the near term. Until conditions improve, we expect our business, financial condition and results of operations to be adversely affected.

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Regulation.

Bank holding companies and nationally chartered banks operate in a highly regulated environment and are subject to supervision and examination by various regulatory agencies. The Company is subject to the Bank Holding Company Act of 1956, as amended, and to regulation and supervision by the Federal Reserve Board. The Bank is subject to regulation and supervision by the Office of the Comptroller of the Currency, or the OCC. The cost of compliance with regulatory requirements may adversely affect our results of operations or financial condition. Federal and state laws and regulations govern numerous matters including: changes in the ownership or control of banks and bank holding companies; maintenance of adequate capital and the financial condition of a financial institution; permissible types, amounts and terms of extensions of credit and investments; permissible non-banking activities; the level of reserves against deposits; and restrictions on dividend payments. The OCC possesses cease and desist powers to prevent or remedy unsafe or unsound practices or violations of law by banks subject to their regulation, and the Federal Reserve Board possesses similar powers with respect to bank holding companies. These and other restrictions limit the manner in which we may conduct our business and obtain financing.

Under regulatory capital adequacy guidelines and other regulatory requirements, we must meet guidelines that include quantitative measures of assets, liabilities, and certain off-balance sheet items, subject to qualitative judgments by regulators about components, risk weightings and other factors. If we fail to meet these minimum capital guidelines and other regulatory requirements, our financial condition would be materially and adversely affected. Our failure to maintain the status of “well-capitalized” under our regulatory framework could affect the confidence of our customers in us, thus compromising our competitive position.

We are subject to credit risk.

There are inherent risks associated with our lending activities. These risks include, among other things, the impact of changes in interest rates and changes in the economic conditions in the markets where we operate as well as those across the United States and abroad. Increases in interest rates and/or weakening economic conditions could adversely impact the ability of borrowers to repay outstanding loans or the value of the collateral securing these loans. We seek to mitigate the risks inherent in our loan portfolio by adhering to specific underwriting practices. Although we believe that our underwriting criteria are appropriate for the various kinds of loans we make, we may incur losses on loans that meet our underwriting criteria, and these losses may exceed the amounts set aside as reserves in our allowance for loan losses.

Allowance for loan losses may be insufficient.

The Bank maintains an allowance for loan losses based on, among other things, national and regional economic conditions, historical loss experience and delinquency trends. We make various assumptions and judgments about the collectability of our loan portfolio, including the creditworthiness of borrowers and the value of the real estate and other assets serving as collateral for the repayment of loans. In determining the size of the allowance for loan losses, we rely on our experience and our evaluation of economic conditions. However, we cannot predict loan losses with certainty, and we cannot provide assurance that charge-offs in future periods will not exceed the allowance for loan losses. During 2011, the Bank experienced incremental increases in both non-performing loans and net loan charge-offs, as compared to prior periods. No assurance can be given that the relevant economic and market conditions will improve or will not further deteriorate. Hence, the persistence or worsening of such conditions could result in an increase in delinquencies, could cause a decrease in our interest income, or could continue to have an adverse impact on our loan loss experience, which, in turn, may necessitate increases to our allowance for loan losses. If net charge-offs exceed the Bank’s allowance, its earnings would decrease. In addition, regulatory agencies review the Bank’s allowance for loan losses and may require additions to the allowance based on their judgment about

information available to them at the time of their examination. Management could also decide that the allowance for loan losses should be increased.

We may be required to charge off additional loans in the future and make further increases in our Provision for Loan Losses which could adversely affect our results of operations.

We maintain an allowance for loan losses, which is a reserve established through a provision for loan losses charged to expense, that represents management's best estimate of probable incurred losses within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated loan losses and risks inherent in the loan portfolio. The level of the allowance reflects management's continuing evaluation of specific credit risks; loan loss experience; current loan portfolio quality; present economic, political and regulatory conditions; industry concentrations; and other unidentified losses inherent in the current loan portfolio. The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and judgment and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material changes. Changes in economic conditions affecting borrowers, new information regarding existing loans, identification of additional

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problem loans and other factors, both within and outside of our control, may require an increase in the allowance for loan losses. Increases in nonperforming loans have a significant impact on our allowance for loan losses. Generally, our nonperforming loans and assets reflect operating difficulties of individual borrowers resulting from weakness in both the national and coastal Maine economies. If the real estate valuation trends of the past several years continue, we could continue to experience delinquencies and credit losses, particularly with respect to commercial real estate loans.

If charge-offs in future periods exceed the allowance for loan losses, we will need additional provisions to increase the allowance for loan losses. Furthermore, growth in the loan portfolio would generally lead to an increase in the provision for loan losses. Any increases in the allowance for loan losses will result in a decrease in net income and capital, and may have a material adverse effect on our financial condition, results of operations and cash flows. See the section captioned "Allowance for Loan Losses" in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations, located elsewhere in this report for further discussion related to our process for determining the appropriate level of the allowance for loan losses.

We are subject to interest rate risk.

Our earnings and cash flows are largely dependent upon our net interest income. Net interest income is the difference between interest income earned on interest-earning assets, such as loans and securities, and interest expense paid on interest-bearing liabilities, such as deposits and borrowed funds. Interest rates are highly sensitive to many factors that are beyond our control, including general economic conditions, demand for loans, securities and deposits, and policies of various governmental and regulatory agencies and, in particular, the Board of Governors of the Federal Reserve System. Changes in monetary policy, including changes in interest rates, could influence not only the interest we receive on loans and securities and the amount of interest we pay on deposits and borrowings, but such changes could also affect (i) our ability to originate loans and obtain deposits, (ii) the fair value of our financial assets and liabilities and (iii) the average duration of our loans and securities that are collateralized by mortgages. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, our net interest income, and therefore earnings, could be adversely affected. Earnings could also be adversely affected if the interest rates received on loans and other investments fall more quickly than the interest rates paid on deposits and other borrowings. If interest rates decline our higher-rate loans and investments may be subject to prepayment risk, which could negatively impact our net interest margin. Conversely, if interest rates increase, our loans and investments may be subject to extension risk, which could negatively impact our net interest margin as well. Any substantial, unexpected, prolonged change in market interest rates could have a material adverse effect on our financial condition, results of operations and cash flows. See Item 7A. Quantitative and Qualitative Disclosures about Market Risk located elsewhere in this report for further discussion related to our management of interest rate risk.

Liquidity risk could impair our ability to fund operations and jeopardize our financial condition.

Liquidity is essential to our business. An inability to raise funds through traditional deposits, brokered deposit renewals or rollovers, secured or unsecured borrowings, the sale of securities or loans and other sources could have a substantial negative effect on our liquidity. Our access to funding sources in amounts adequate to finance our activities could be impaired by factors that affect us specifically or the financial services industry or economy in general, or could be available only under terms which are unacceptable to us. Factors that could detrimentally impact our access to liquidity sources include a decrease in the level of our business activity as a result of a downturn in the markets in which our loans are concentrated or adverse regulatory action against us. Our ability to borrow could also be impaired by factors that are not specific to us, such as a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry in light of the recent turmoil faced by banking

organizations and the continued deterioration in credit markets. We rely primarily on commercial and retail deposits and to a lesser extent, brokered deposit renewals and rollovers, advances from the Federal Home Loan Bank of Boston (“FHLB”) and other secured and unsecured borrowings to fund our operations. Although we have historically been able to replace maturing deposits and advances as necessary, we might not be able to replace such funds in the future if, among other things, our results of operations or financial condition or the results of operations or financial condition of the FHLB or market conditions were to change. In addition, if we fall below the FDIC’s thresholds to be considered “well capitalized”, we will be unable to continue to rollover or renew brokered funds, and the interest rate paid on deposits would be restricted.

Loss of lower-cost funding sources.

Checking and savings, NOW, and money market deposit account balances and other forms of customer deposits can decrease when customers perceive alternative investments, such as the stock market, as providing a better risk/return tradeoff. If customers move money out of bank deposits and into other investments, we could lose a relatively low-cost source of funds, increasing our funding costs and reducing our net interest income and net income. Advances from the FHLB are currently a relatively low-cost source of funding. The availability of qualified collateral on the Bank’s

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balance sheet determines the level of advances available from FHLB and a deterioration in quality in the Bank's loan portfolio can adversely impact the availability of this source of funding.

Competition in the financial services industry.

We face substantial competition in all areas of our operations from a variety of different competitors, many of which are larger and may have more financial resources than we do. We compete with other providers of financial services such as commercial and savings banks, savings and loan associations, credit unions, money market and mutual funds, mortgage companies, asset managers, insurance companies and a wide array of other local, regional and national institutions which offer financial services. Mergers between financial institutions within Maine and in neighboring states have added competitive pressure. If we are unable to compete effectively, we will lose market share and our income generated from loans, deposits, and other financial products will decline.

We may elect or be compelled to seek additional capital in the future, but capital may not be available when needed.

We are required by federal and state regulatory authorities to maintain adequate levels of capital to support our operations. In addition, we may elect to raise additional capital to support our business or to finance acquisitions, if any, or we may otherwise elect to raise additional capital. In that regard, a number of financial institutions have recently raised considerable amounts of capital as a result of deterioration in their results of operations and financial condition arising from the turmoil in the mortgage loan market, deteriorating economic conditions, declines in real estate values and other factors, which may diminish our ability to raise additional capital.

Our ability to raise additional capital, if needed or desired (including to repurchase the remaining outstanding CPP Shares before the dividend payable thereunder increases to 9% per annum), will depend on conditions in the capital markets, economic conditions and a number of other factors, many of which are outside our control, and on our financial performance. Accordingly, we cannot be assured of our ability to raise additional capital if needed or on terms acceptable to us. If we cannot raise additional capital when needed, we may become subject to increased regulatory supervision and the imposition of restrictions on our growth and our business, which may have a material adverse effect on our financial condition, results of operations and prospects.

The value of our investment securities portfolio may be negatively affected by disruptions in securities markets.

The market for some of the investment securities held in our portfolio has become volatile over the past several years. Volatile market conditions may detrimentally affect the value of these securities due to the perception of heightened credit and liquidity risks. There can be no assurance that the declines in market value associated with these disruptions will not result in other than temporary impairments of these assets, which would lead to accounting charges that could have a material adverse effect on our net income and capital levels. Our mortgage-backed portfolio may be subject to extension risk as interest rates rise and borrowers are unable to refinance their current mortgages into lower rate mortgages, extending the average life of the bonds.

The soundness of other financial institutions could adversely affect us.

Since mid-2007, the financial services industry as a whole, as well as the securities markets generally, have been materially and adversely affected by very significant declines in the values of nearly all asset classes and by a very serious lack of liquidity. Financial institutions in particular have been subject to increased volatility and an overall loss in investor confidence.

Our ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial services companies are interrelated as a result of trading, clearing,

counterparty, or other relationships. We have exposure to many different industries and counterparties, and we routinely execute transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, investment banks, mutual and hedge funds, and other institutional clients. As a result, defaults by, or even rumors or questions about, one or more financial services companies, or the financial services industry generally, have led to market-wide liquidity problems and could lead to losses or defaults by us or by other institutions. Many of these transactions expose us to credit risk in the event of default of our counterparty or client. In addition, our credit risk may be exacerbated when the collateral held by us cannot be realized or is liquidated at prices not sufficient to recover the full amount of the loan or derivative exposure due us. There is no assurance that any such losses would not materially and adversely affect our business, financial condition or results of operations.

Changes in primary market area could adversely impact results of operations and financial condition.

Most of the Bank's lending is in Mid-Coast and Down East Maine. As a result of this geographic concentration, a significant broad-based deterioration in economic conditions in this area or Northern New England could have a material adverse impact on the quality of the Bank's loan portfolio, and accordingly, our results of operations. Such a decline in economic conditions could impair borrowers' ability to pay outstanding principal and interest on loans when

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due and, consequently, adversely affect the cash flows of our business.

The Bank's loan portfolio is largely secured by real estate collateral. A substantial portion of the real and personal property securing the loans in the Bank's portfolio is located in Mid-Coast and Down East Maine. Conditions in the real estate market in which the collateral for the Bank's loans is located strongly influence the level of the Bank's non-performing loans and results of operations. The recent decline in the Mid-Coast and Down East Maine area real estate values, as well as other external factors, could adversely affect the Bank's loan portfolio.

We may not be able to attract and retain skilled people.

Our success depends, in large part, on our ability to attract and retain key people. Competition for the best people in most activities in which we are engaged can be intense, and we may not be able to retain or hire the people we want and/or need. In order to attract and retain qualified employees, we must compensate such employees at market levels. Typically, those levels have caused employee compensation to be our greatest expense. If we are unable to continue to attract and retain qualified employees, or do so at rates necessary to maintain our competitive position, our performance, including our competitive position, could suffer, and, in turn, have a material adverse effect on us. Although we have incentive compensation plans aimed, in part, at long-term employee retention, the unexpected loss of services of one or more of our key personnel could still occur, and such events may have a material adverse effect on us because of the loss of the employee's skills, knowledge of our market, years of industry experience and the difficulty of promptly finding qualified replacement personnel for our talented executives and/or relationship managers.

Pursuant to the standardized terms of the CPP, among other things, we agreed to institute certain restrictions on the compensation of certain senior executive management positions that could have an adverse effect on our ability to hire or retain the most qualified senior executives. Other restrictions were imposed under the Recovery Act, the Dodd-Frank Act and other legislation or regulations. Our ability to attract and/or retain talented executives and/or relationship managers may be affected by these developments or any new executive compensation limits, and such restrictions could have a material adverse effect on us.

We have operational risk.

We face the risk that the design of our controls and procedures, including those to mitigate the risk of fraud by employees or outsiders, may prove to be inadequate or are circumvented, thereby causing delays in detection of errors or inaccuracies in data and information. Management regularly reviews and updates our internal controls, disclosure controls and procedures, and corporate governance policies and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Any failure or circumvention of our controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on our business, results of operations and financial condition.

We may also be subject to disruptions of our systems arising from events that are wholly or partially beyond our control (including, for example, computer viruses or electrical or telecommunications outages), which may give rise to losses in service to customers and to financial loss or liability. We are further exposed to the risk that our external vendors may be unable to fulfill their contractual obligations (or will be subject to the same risk of fraud or operational errors by their respective employees, or others, as are we) and to the risk that our (or our vendors') business continuity and data security systems prove to be inadequate.

Our information systems may experience an interruption or breach in security.

We rely heavily on communications and information systems to conduct our business. Any failure, interruption or breach in security of these systems could result in failures or disruptions in our customer relationship management, general ledger, deposit, loan and other systems. While we have policies and procedures designed to prevent or limit the effect of the possible failure, interruption or security breach of our information systems, there can be no assurance that any such failure, interruption or security breach will not occur or, if any does occur, that it will be adequately addressed. The occurrence of any failure, interruption or security breach of our information systems could damage our reputation, result in a loss of customer business, subject us to additional regulatory scrutiny, or expose us to civil litigation and possible financial liability, any of which could have a material adverse effect on us.

We regularly review and update our internal controls, disclosure controls and procedures, and corporate governance policies and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Any failure or circumvention of our controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on us.

We continually encounter technological change.

The financial services industry is continually undergoing rapid technological change with frequent introductions of new

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technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and to reduce costs. Our future success depends, in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies in our operations. Our largest competitors have substantially greater resources to invest in technological improvements. We may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers. Failure to successfully keep pace with technological change affecting the financial services industry could have a material adverse effect on us.

In particular, we are subject to security, transactional and operational risks relating to the use of technology that could damage our reputation and our business.

We rely heavily on communications and information systems to conduct our business serving both internal and customer constituencies. Any failure, interruption or breach in security of these systems could result in failures or disruptions in our customer relationship management, general ledger, deposit, loan, and other systems. While we have policies and procedures, security applications and fraud mitigation applications, designed to prevent or limit the effect of the failure, interruption, fraud attacks or security breach of our information systems, there can be no assurance that any such failures, interruptions, fraud attacks or security breaches will not occur or, if they do occur, that they will be adequately addressed. Additionally, we outsource our data processing to a third party. If our third party provider encounters difficulties or if we have difficulty in communicating with such third party, it will significantly affect our ability to adequately process and account for customer transactions, which would significantly affect our business operations. Furthermore, breaches of such third party's technology may also cause reimbursable loss to our consumer and business customers, through no fault of our own. Fraud attacks targeting customer-controlled devices, plastic payment card terminals, and merchant data collection points provide another source of potential loss, again through no fault of our own. The occurrence of any failures, interruptions or security breaches of information systems used to process customer transactions could damage our reputation, result in a loss of customer business, subject us to additional regulatory scrutiny, or expose us to civil litigation and possible financial liability, any of which could have a material adverse effect on our financial condition, results of operations and cash flows.

Claims and litigation pertaining to fiduciary responsibility or lender liability.

From time to time as part of our normal course of business, customers make claims and take legal action against the Bank based on actions or inactions of the Bank. If such claims and legal actions are not resolved in a manner favorable to us, they may result in financial liability and/or adversely affect the market perception of the Company and its products and services. This may also impact customer demand for the Company's products and services. Any financial liability or reputation damage could have a material adverse effect on our business, which, in turn, could have a material adverse effect on our financial condition and results of operations.

There may not be a robust trading market for the common stock.

Although our common stock is traded on the NASDAQ Global Select market, the trading volume of the common stock has historically not been substantial. Over the five-year period ending December 31, 2011, for example, the average monthly trading volume of our common stock has been 335,409 shares or approximately 3.43% of the outstanding common stock. Due to the limited trading volume in our common stock, the intraday spread between bid and ask prices of the shares can be quite high. There can be no assurance that a more robust, active or economical trading market for our common stock will develop. The market value and liquidity of our common stock may, as a result, be adversely affected.

The price of our common stock may fluctuate.

The price of our common stock on the NASDAQ Global Select Market constantly changes and recently, given the uncertainty in the financial markets, has fluctuated widely. We expect the market price of our common stock will continue to fluctuate. Holders of our common stock will be subject to the risk of volatility and changes in prices. Our common stock price can fluctuate as a result of many factors which are beyond our control, including:

- quarterly fluctuations in our operating and financial results;
- operating results that vary from the expectations of Management, securities analysts and investors;
- changes in expectations as to our future financial performance, including financial estimates by securities analysts;
- events negatively impacting the financial services industry which result in a general decline for the industry;
 - announcements of material developments affecting our operations or our dividend policy;
 - future sales of our equity securities;
- new laws or regulations or new interpretations of existing laws or regulations applicable to our business;

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- changes in accounting standards, policies, guidance, interpretations or principles; and
 - general domestic economic and market conditions.

In addition, recently the stock market generally has experienced extreme price and volume fluctuations, and industry factors and general economic and political conditions and events, such as economic slowdowns or recessions, interest rate changes or credit loss trends, could also cause our stock price to decrease regardless of our operating results.

Future offerings of debt or other securities may adversely affect the market price of our stock.

In the future, we may attempt to increase our capital resources or, if our or the Bank's capital ratios approach or fall below the required minimums, we or the Bank could be forced to raise additional capital by making additional offerings of debt or preferred equity securities, including medium-term notes, trust preferred securities, senior or subordinated notes and preferred stock. Upon liquidation, holders of our debt securities and shares of preferred stock and lenders with respect to other borrowings will receive distributions of our available assets prior to the holders of our common stock. Additional equity offerings may dilute the value for existing Shareholders or reduce the market price of our common stock, or both. Holders of our common stock are not entitled to preemptive rights or other protections against dilution.

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ITEM 1B. Unresolved Staff Comments

None

ITEM 2. Properties

The principal office of the Company and the Bank is located in Damariscotta, Maine. The Bank operates 14 full-service banking offices in four counties in the Mid-Coast and Down East regions of Maine:

Lincoln County	Knox County	Hancock County	Washington County
Boothbay Harbor	Camden	Bar Harbor	Eastport
Damariscotta	Rockland	Blue Hill	Calais
Waldoboro	Rockport	Ellsworth	
Wiscasset		Northeast Harbor	
		Southwest Harbor	

First Advisors, the investment management and trust division of the Bank, operates from three offices in Bar Harbor, Ellsworth and Damariscotta. The Bank also maintains an Operations Center in Damariscotta. The Company owns all of its facilities except for the land on which the Ellsworth branch is located, and except for the Camden office and the Southwest Harbor drive-up facility, for which the Bank has entered into long-term leases. Management believes that the Bank's current facilities are suitable and adequate in light of its current needs and its anticipated needs over the near term.

ITEM 3. Legal Proceedings

There are no material pending legal proceedings to which the Company or the Bank is a party or to which any of its property is subject, other than routine litigation incidental to the business of the Bank. None of these proceedings is expected to have a material effect on the financial condition of the Company or of the Bank.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Market for Registrant's Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities

The common stock of The First Bancorp (ticker symbol FNLC) trades on the NASDAQ Global Select Market System. As of December 31, 2011, there were 9,812,180 shares outstanding and held of record by approximately 2,686 shareholders. The following table reflects the high and low prices of actual sales in each quarter of 2011 and 2010. Such quotations do not reflect retail mark-ups, mark-downs or brokers' commissions.

	2011		2010	
	High	Low	High	Low
1st Quarter	\$15.95	\$13.40	\$16.26	\$13.11
2nd Quarter	15.96	13.79	16.37	13.07
3rd Quarter	15.30	11.69	14.48	12.27
4th Quarter	15.95	11.75	16.00	13.40

The last transaction in the Company's stock on NASDAQ during 2011 was on December 30 at \$15.37 per share. There are no warrants outstanding with respect to the Company's common stock other than warrants to purchase up to 225,904 shares of its common stock (subject to adjustment) at \$16.60 per share issued to the U.S. Treasury incident to the Company's participation in the CPP program. The Company has no securities outstanding which are convertible into common equity.

The ability of the Company to pay cash dividends depends on receipt of dividends from the Bank. Dividends may be declared by the Bank out of its net profits as the directors deem appropriate, subject to the limitation that the total of all dividends declared by the Bank in any calendar year may not exceed the total of its net profits of that year plus retained net profits of the preceding two years. The amount available for dividends in 2012 will be that year's net income plus \$6.9 million. The payment of dividends from the Bank to the Company may be additionally restricted if the payment of such dividends resulted in the Bank failing to meet regulatory capital requirements. The Bank is also required to maintain minimum amounts of capital-to-total-risk-weighted-assets, as defined by banking regulators. At December 31, 2011, the Bank was required to have minimum Tier 1 and Tier 2 risk-based capital ratios of 4.00% and 8.00%, respectively. The Bank's actual ratios were 14.11% and 15.37%, respectively, as of December 31, 2011. The table below sets forth the cash dividends declared in the last two fiscal years:

Date Declared	Amount Per Share	Date Payable
March 18, 2010	\$0.195	April 30, 2010
June 17, 2010	\$0.195	July 30, 2010
September 16, 2010	\$0.195	October 29, 2010
December 16, 2010	\$0.195	January 28, 2011
March 17, 2011	\$0.195	April 29, 2011
June 15, 2011	\$0.195	July 29, 2011
September 15, 2011	\$0.195	October 28, 2011
December 15, 2011	\$0.195	January 31, 2012

Repurchase of Shares and Use of Proceeds

As a consequence of the Company's issuance of securities under the U.S. Treasury's CPP program, its ability to repurchase stock while such securities remain outstanding is restricted to purchases from employee benefit plans. During the year ended December 31, 2011, the Company repurchased no common stock.

Unregistered Sales of Equity Securities

The Company had no unregistered sales of equity securities in 2011.

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Securities Authorized for Issuance Under Equity Compensation Plans

The following table lists the amount and weighted-average exercise price of securities authorized for issuance under equity compensation plans:

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders	51,000	\$ 16.47	392,500
Equity compensation plans not approved by security holders	-	\$ -	-
Total	51,000	\$ 16.47	392,500

Performance Graph

Set forth below is a line graph comparing the five-year cumulative total return of \$100.00 invested in the Company's common stock ("FNLC"), assuming reinvestment of all cash dividends and retention of all stock dividends, with a comparable amount invested in the Standard & Poor's 500 Index ("S&P 500") and the NASDAQ Combined Bank Index ("NASD Bank"). The NASD Bank index is a capitalization-weighted index designed to measure the performance of all NASDAQ stocks in the banking sector.

	2006	2007	2008	2009	2010	2011
FNLC	100.00	91.31	131.21	104.97	113.50	116.10
S&P 500	100.00	105.46	66.44	84.03	96.68	98.72
NASD Bank	100.00	80.19	62.96	52.86	60.34	54.01

ITEM 6. Selected Financial Data

The First Bancorp, Inc. and Subsidiary

Years ended December 31,

Dollars in thousands,
except for per share amounts

	2011	2010	2009	2008	2007
Summary of Operations					
Interest Income	\$55,702	\$57,260	\$62,569	\$71,372	\$71,721
Interest Expense	14,709	16,671	18,916	33,669	39,885
Net Interest Income	40,993	40,589	43,653	37,703	31,836
Provision for Loan Losses	10,550	8,400	12,160	4,700	1,432
Non-Interest Income	11,750	9,135	12,754	9,646	10,145
Non-Interest Expense	26,038	25,130	26,658	22,994	22,183
Net Income	12,364	12,116	13,042	14,034	13,101
Per Common Share Data					
Net Income					
Basic	\$1.14	\$1.10	\$1.22	\$1.45	\$1.34
Diluted	1.14	1.10	1.22	1.44	1.34
Cash Dividends (Declared)	0.780	0.780	0.780	0.765	0.690
Book Value	14.12	12.80	12.66	12.09	11.58
Tangible Book Value	11.30	9.97	9.82	9.23	8.73
Market Value	15.37	15.79	15.42	19.89	14.64
Financial Ratios					
Return on Average Equity ¹	9.37	% 9.53	% 10.66	% 12.02	% 11.89
Return on Average Tangible Equity ^{1,2}	10.70	10.83	12.54	15.75	15.89
Return on Average Assets ¹	0.87	0.89	0.96	1.10	1.13
Average Equity to Average Assets	10.72	11.20	10.85	9.14	9.53
Average Tangible Equity to Average Assets ²	8.77	9.15	8.80	6.98	7.13
Net Interest Margin Tax-Equivalent ^{1,2}	3.27	3.38	3.66	3.33	3.13
Dividend Payout Ratio (Declared)	68.42	70.91	63.93	52.76	51.49
Allowance for Loan Losses/Total Loans	1.50	1.50	1.43	0.90	0.74
Non-Performing Loans to Total Loans	3.21	2.39	1.95	1.27	0.31
Non-Performing Assets to Total Assets	2.32	1.87	1.80	1.31	0.56
Efficiency Ratio ² (Tax-equivalent)	49.75	48.15	43.39	46.07	50.16
At Year End					
Total Assets	\$1,372,867	\$1,393,802	\$1,331,394	\$1,325,744	\$1,223,250
Total Loans	864,988	887,596	952,492	979,273	920,164
Total Investment Securities	424,306	416,052	287,818	247,839	208,585
Total Deposits	941,333	974,518	922,667	925,736	781,280
Total Borrowings	265,663	257,330	249,778	272,074	316,719
Total Shareholders' Equity	150,858	149,848	147,938	117,181	112,453
				High	Low
Market price per common share of stock during 2011				\$15.96	\$11.69

¹Annualized using a 365-day basis²These ratios use non-GAAP financial measures. See Management's Discussion and Analysis of Financial Condition and Results of Operations for additional disclosures and information.

ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The First Bancorp, Inc. (the "Company") was incorporated in the State of Maine on January 15, 1985, and is the parent holding company of The First, N.A. (the "Bank"). At the Company's Annual Meeting of Shareholders on April 30, 2008, the Company's name was changed to The First Bancorp, Inc. from First National Lincoln Corporation.

The Company generates almost all of its revenues from the Bank, which was chartered as a national bank under the laws of the United States on May 30, 1864. The Bank, which has fourteen offices along coastal Maine, emphasizes personal service to the communities it serves, concentrating primarily on small businesses and individuals.

The Bank offers a wide variety of traditional banking services and derives the majority of its revenues from net interest income – the spread between what it earns on loans and investments and what it pays for deposits and borrowed funds. While net interest income typically increases as earning assets grow, the spread can vary up or down depending on the level and direction of movements in interest rates. Management believes the Bank has modest exposure to changes in interest rates, as discussed in "Interest Rate Risk Management" elsewhere in Management's Discussion. The banking business in the Bank's market area historically has been seasonal with lower deposits in the winter and spring and higher deposits in the summer and fall. This seasonal swing is fairly predictable and has not had a materially adverse effect on the Bank.

Non-interest income is the Bank's secondary source of revenue and includes fees and service charges on deposit accounts, income from the sale and servicing of mortgage loans, and income from investment management and private banking services through First Advisors, a division of the Bank.

Forward-Looking Statements

This report contains statements that are "forward-looking statements." We may also make written or oral forward-looking statements in other documents we file with the SEC, in our annual reports to Shareholders, in press releases and other written materials, and in oral statements made by our officers, directors or employees. You can identify forward-looking statements by the use of the words "believe", "expect", "anticipate", "intend", "estimate", "assume", "outlook", "will", "should", "may", "might", "could", and other expressions that predict or indicate future events or trends and which do not relate to historical matters. You should not rely on forward-looking statements, because they involve known and unknown risks, uncertainties and other factors, some of which are beyond the control of the Company. These risks, uncertainties and other factors may cause the actual results, performance or achievements of the Company to be materially different from the anticipated future results, performance or achievements expressed or implied by the forward-looking statements.

Some of the factors that might cause these differences include the following: changes in general national, regional or international economic conditions or conditions affecting the banking or financial services industries or financial capital markets, volatility and disruption in national and international financial markets, government intervention in the U.S. financial system, reductions in net interest income resulting from interest rate volatility as well as changes in the balance and mix of loans and deposits, reductions in the market value of wealth management assets under administration, changes in the value of securities and other assets, reductions in loan demand, changes in loan collectibility, default and charge-off rates, changes in the size and nature of the Company's competition, changes in legislation or regulation and accounting principles, policies and guidelines, and changes in the assumptions used in making such forward-looking statements. In addition, the factors described under "Risk Factors" in Item 1A of this Annual Report on Form 10-K, may result in these differences. You should carefully review all of these factors, and you should be aware that there may be other factors that could cause these differences. These forward-looking statements were based on information, plans and estimates at the date of this annual report, and we assume no obligation to update any forward-looking statements to reflect changes in underlying assumptions or factors, new information, future events or other changes.

Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, actual results may differ materially from the results discussed in these forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof.

The Company undertakes no obligation to republish revised forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. Readers are also urged to carefully review and consider the various disclosures made by the Company, which attempt to advise interested parties of the factors that affect the Company's business.

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Critical Accounting Policies

Management's discussion and analysis of the Company's financial condition is based on the consolidated financial statements which are prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of such financial statements requires Management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. On an ongoing basis, Management evaluates its estimates, including those related to the allowance for loan losses, goodwill, the valuation of mortgage servicing rights, and other-than-temporary impairment on securities. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis in making judgments about the carrying values of assets that are not readily apparent from other sources. Actual results could differ from the amount derived from Management's estimates and assumptions under different assumptions or conditions.

Allowance for Loan Losses. Management believes the allowance for loan losses requires the most significant estimates and assumptions used in the preparation of the consolidated financial statements. The allowance for loan losses is based on Management's evaluation of the level of the allowance required in relation to the estimated loss exposure in the loan portfolio. Management believes the allowance for loan losses is a significant estimate and therefore regularly evaluates it to determine the appropriate level by taking into consideration factors such as prior loan loss experience, the character and size of the loan portfolio, business and economic conditions and Management's estimation of potential losses. The use of different estimates or assumptions could produce different provisions for loan losses.

Goodwill. Management utilizes numerous techniques to estimate the value of various assets held by the Company, including methods to determine the appropriate carrying value of goodwill as required under Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 350 "Intangibles – Goodwill and Other." In addition, goodwill from a purchase acquisition is subject to ongoing periodic impairment tests, which include an evaluation of the ongoing assets, liabilities and revenues from the acquisition and an estimation of the impact of business conditions.

Mortgage Servicing Rights. The valuation of mortgage servicing rights is a critical accounting policy which requires significant estimates and assumptions. The Bank often sells mortgage loans it originates and retains the ongoing servicing of such loans, receiving a fee for these services, generally 0.25% of the outstanding balance of the loan per annum. Mortgage servicing rights are recognized at fair value when they are acquired through the sale of loans, and are reported in other assets. They are amortized into non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. The rights are subsequently carried at the lower of amortized cost or fair value. Management uses an independent firm which specializes in the valuation of mortgage servicing rights to determine the fair value. The most important assumption is the anticipated loan prepayment rate, and increases in prepayment speed results in lower valuations of mortgage servicing rights. The valuation also includes an evaluation for impairment based upon the fair value of the rights, which can vary depending upon current interest rates and prepayment expectations, as compared to amortized cost. Impairment is determined by stratifying rights by predominant characteristics, such as interest rates and terms. The use of different assumptions could produce a different valuation. All of the assumptions are based on standards the Company believes would be utilized by market participants in valuing mortgage servicing rights and are consistently derived and/or benchmarked against independent public sources.

Other-Than-Temporary Impairment on Securities. One of the significant estimates related to investment securities is the evaluation of other-than-temporary impairments. The evaluation of securities for other-than-temporary impairments is a quantitative and qualitative process, which is subject to risks and uncertainties and is intended to determine whether declines in the fair value of investments should be recognized in current period earnings. The risks and uncertainties include changes in general economic conditions, the issuer's financial condition and/or future prospects, the effects of changes in interest rates or credit spreads and the expected recovery period of unrealized losses. Securities that are in an unrealized loss position are reviewed at least quarterly to determine if

other-than-temporary impairment is present based on certain quantitative and qualitative factors and measures. The primary factors considered in evaluating whether a decline in value of securities is other-than-temporary include: (a) the length of time and extent to which the fair value has been less than cost or amortized cost and the expected recovery period of the security, (b) the financial condition, credit rating and future prospects of the issuer, (c) whether the debtor is current on contractually obligated interest and principal payments, (d) the volatility of the securities' market price, (e) the intent and ability of the Company to retain the investment for a period of time sufficient to allow for recovery, which may be at maturity and (f) any other information and observable data considered relevant in determining whether other-than-temporary impairment has occurred, including the expectation of receipt of all principal and interest when due.

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Use of Non-GAAP Financial Measures

Certain information in Management's Discussion and Analysis of Financial Condition and Results of Operations and elsewhere in this Report contains financial information determined by methods other than in accordance with accounting principles generally accepted in the United States of America ("GAAP"). Management uses these "non-GAAP" measures in its analysis of the Company's performance and believes that these non-GAAP financial measures provide a greater understanding of ongoing operations and enhance comparability of results with prior periods as well as demonstrating the effects of significant gains and charges in the current period. The Company believes that a meaningful analysis of its financial performance requires an understanding of the factors underlying that performance. Management believes that investors may use these non-GAAP financial measures to analyze financial performance without the impact of unusual items that may obscure trends in the Company's underlying performance. These disclosures should not be viewed as a substitute for operating results determined in accordance with GAAP, nor are they necessarily comparable to non-GAAP performance measures that may be presented by other companies.

In several places in this report, net interest income is presented on a fully taxable equivalent basis. Specifically included in interest income was tax-exempt interest income from certain investment securities and loans. An amount equal to the tax benefit derived from this tax exempt income has been added back to the interest income total, which adjustments increased net interest income accordingly. Management believes the disclosure of tax-equivalent net interest income information improves the clarity of financial analysis, and is particularly useful to investors in understanding and evaluating the changes and trends in the Company's results of operations. Other financial institutions commonly present net interest income on a tax-equivalent basis. This adjustment is considered helpful in the comparison of one financial institution's net interest income to that of another institution, as each will have a different proportion of tax-exempt interest from its earning assets. Moreover, net interest income is a component of a second financial measure commonly used by financial institutions, net interest margin, which is the ratio of net interest income to average earning assets. For purposes of this measure as well, other financial institutions generally use tax-equivalent net interest income to provide a better basis of comparison from institution to institution. The Company follows these practices. The following table provides a reconciliation of tax-equivalent financial information to the Company's consolidated financial statements, which have been prepared in accordance with GAAP. A 35.0% tax rate was used in 2011, 2010 and 2009.

Dollars in thousands	Years ended December 31,		
	2011	2010	2009
Net interest income as presented	\$40,993	\$40,589	\$43,653
Effect of tax-exempt income	2,710	2,281	2,395
Net interest income, tax equivalent	\$43,703	\$42,870	\$46,048

The Company presents its efficiency ratio using non-GAAP information. The GAAP-based efficiency ratio is noninterest expenses divided by net interest income plus noninterest income from the Consolidated Statements of Income. The non-GAAP efficiency ratio excludes securities losses and other-than-temporary impairment charges from noninterest expenses, excludes securities gains from noninterest income, and adds the tax-equivalent adjustment to net interest income. The following table provides a reconciliation of between the GAAP and non-GAAP efficiency ratio:

In thousands of dollars	Years ended December 31,		
	2011	2010	2009
Non-interest expense, as presented	\$26,038	\$25,130	\$26,658
Net securities losses	-	-	(150)
Other than temporary impairment charge	-	-	(916)
Adjusted non-interest expense	26,038	25,130	25,592

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Net interest income, as presented	40,993		40,589		43,653	
Effect of tax-exempt income	2,710		2,281		2,395	
Non-interest income, as presented	11,750		9,135		12,754	
Effect of non-interest tax-exempt income	182		193		185	
Net securities gains	(3,293)		(2)		-	
Adjusted net interest income plus non-interest income	\$52,342		\$52,196		\$58,987	
Non-GAAP efficiency ratio	49.75	%	48.15	%	43.39	%
GAAP efficiency ratio	49.37	%	50.54	%	47.26	%

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The Company presents certain information based upon average tangible common shareholders' equity instead of total average shareholders' equity. The difference between these two measures is the Company's intangible assets, specifically goodwill from prior acquisitions, and preferred stock. Management, banking regulators and many stock analysts use the tangible common equity ratio and the tangible book value per common share in conjunction with more traditional bank capital ratios to compare the capital adequacy of banking organizations with significant amounts of goodwill or other intangible assets, typically stemming from the use of the purchase accounting method in accounting for mergers and acquisitions. The following table provides a reconciliation of tangible average shareholders' equity to the Company's consolidated financial statements, which have been prepared in accordance with GAAP:

In thousands of dollars	Years ended December 31,		
	2011	2010	2009
Average shareholders' equity as presented	\$ 152,254	\$ 151,739	\$ 146,854
Less preferred stock (average)	(20,290)	(24,606)	(24,452)
Less intangible assets	(27,684)	(27,684)	(27,684)
Average tangible common shareholders' equity	\$ 104,280	\$ 99,449	\$ 94,718

Executive Summary

Net income for the year ended December 31, 2011 was \$12.4 million, up \$248,000 or 2.0% from the \$12.1 million posted for the year ended December 31, 2010. Earnings per common share on a fully diluted basis were \$1.14 for the year ended December 31, 2011, up \$0.04 or 3.6% from the \$1.10 posted for the year ended December 31, 2010. Net interest income on a tax-equivalent basis was up \$833,000 or 1.9% for the year ended December 31, 2011 compared to the year ended December 31, 2010. This increase was attributable to average earning assets in 2011 running \$68.0 million or 5.4% above the level seen in 2010, adding \$2.2 million to net interest income. This increase more than offset our net interest margin slipping from 3.38% in 2010 to 3.27% in 2011.

During 2011, total assets decreased \$20.9 million or 1.5%. The loan portfolio was down \$22.6 million or 2.5%. The investment portfolio was up \$8.3 million or 2.0% for the year. On the liability side of the balance sheet, low-cost deposits have increased \$18.4 million or 6.2% for the year, and local certificates of deposit decreased \$8.2 million or 6.90%.

We continue to be in the longest and worst economic downturn since the Great Depression of the 1930's. The slump in the housing market is continuing and the national unemployment rate was 8.5% at December 31, 2011. Fortunately, the unemployment rate in Maine at December 31, 2011, at 7.0%, was much better than the national average and ranks as the nineteenth-best state in the country. Unemployment numbers, however, do not reflect the number of people experiencing reduced incomes from wage cutbacks and loss of overtime.

Non-performing loans stood at 3.21% of total loans on December 31, 2011 compared to 2.39% of total loans on December 31, 2010. This compares to nonperforming loans at 2.57% for our Uniform Bank Performance Report peer group ("UBPR peer group") as of December 31, 2011. Net chargeoffs were \$10.9 million or 1.23% of average loans in 2011 compared to net charge offs of \$8.7 million or 0.94% of average loans in 2010. Net charge offs for the UBPR peer group in 2011 were 0.94% of average loans. We provisioned \$10.6 million for loan losses in 2011, up \$2.2 million from the \$8.4 million provision made during 2010. Although the allowance for loan losses decreased \$316,000 during the year, year-over-year the allowance as a percentage of loans outstanding was unchanged at 1.50%

Remaining well capitalized continues to be a top priority for The First Bancorp. In 2009, we received a \$25 million preferred stock investment from the U.S. Treasury Capital Purchase Program which enabled the Company to obtain additional capital at a relatively low cost, and it provided us with greater ability to ride out the current economic storm and allows us more flexibility to work with individuals and businesses as they too struggle through these adverse economic conditions. In the third quarter of 2011, we repaid half of this preferred stock investment to the U.S.

Treasury. Even after the repayment, the Company's total risk-based capital ratio remains very strong at 15.66%, well above the well-capitalized threshold of 10.0% set by the FDIC.

The Company's operating ratios remain good, with a return on average tangible common equity of 10.70% for the year ended December 31, 2011 compared to 10.83% for the year ended December 31, 2010. Our return on average tangible equity was in the top 40% of all banks in the UBPR peer group, which had an average return of 7.26% for the year. Our efficiency ratio continues to be an important component in our overall performance; it slipped to 49.75% in 2011 compared to 48.15% in 2010. This was the result of higher operating expenses. As of December 31, 2011, the average efficiency ratio for our UBPR peer group was 66.26%, which put us in the top 12% of all banks in the UBPR peer group.

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Results of Operations

Net Interest Income

Net interest income on a tax-equivalent basis increased 1.9% or \$0.8 million to \$43.7 million for the year ended December 31, 2011 from the \$42.9 million reported for the year ended December 31, 2010. A higher level of average earning assets in 2011 was responsible for \$2.2 million of this change while several factors, including the decrease in the net interest margin from 3.38% in 2010 to 3.27% in 2011, reduced the increase in net interest income by \$1.4 million.

Total interest income in 2011 was \$55.7 million, a decrease of \$1.6 million or 2.7% from the \$57.3 million posted by the Company in 2010. Total interest expense in 2011 was \$14.7 million, a decrease of \$2.0 million or 11.8% from the \$16.7 million posted by the Company in 2010. The decrease in both interest income and interest expense was attributable to lower interest rates. Tax-exempt interest income amounted to \$5.0 million for the year ended December 31, 2011, \$4.2 million for the year ended December 31, 2010 and \$4.4 million for the year ended December 31, 2009. The following tables present changes in interest income and expense attributable to changes in interest rates, volume, and rate/volume¹ for interest-earning assets and interest-bearing liabilities. Tax-exempt income is calculated on a tax-equivalent basis, using a 35.0% tax rate.

Year ended December 31, 2011 compared to 2010

Dollars in thousands	Volume	Rate	Rate/Volume ¹	Total
Interest on earning assets				
Interest-bearing deposits	\$315	\$(6)	\$(303)	\$6
Investment securities	4,913	(1,403)	(455)	3,055
Loans held for sale	(127)	(13)	10	(130)
Loans	(2,078)	(2,080)	98	(4,060)
Total interest income	3,023	(3,502)	(650)	(1,129)
Interest expense				
Deposits	516	(1,016)	(51)	(551)
Borrowings	303	(1,636)	(78)	(1,411)
Total interest expense	819	(2,652)	(129)	(1,962)
Change in net interest income	\$2,204	\$(850)	\$(521)	\$833

Year ended December 31, 2010 compared to 2009

Dollars in thousands	Volume	Rate	Rate/Volume ¹	Total
Interest on earning assets				
Interest-bearing deposits	\$(1)	\$(1)	\$ 1	\$(1)
Investment securities	3,420	(2,555)	(587)	278
Loans held for sale	33	(7)	(1)	25
Loans	(2,813)	(3,086)	174	(5,725)
Total interest income	639	(5,649)	(413)	(5,423)
Interest expense				
Deposits	129	(1,685)	(19)	(1,575)
Borrowings	(492)	(191)	13	(670)
Total interest expense	(363)	(1,876)	(6)	(2,245)
Change in net interest income	\$1,002	\$(3,773)	\$(407)	\$(3,178)

¹ Represents the change attributable to a combination of change in rate and change in volume.

The following table presents the interest earned on or paid for each major asset and liability category, respectively, for the years ended December 31, 2011, 2010, and 2009, as well as the average yield for each major asset and liability category, and the net yield between assets and liabilities. Tax-exempt income has been calculated on a tax-equivalent basis using a 35% rate. Unrecognized interest on non-accrual loans is not included in the amount presented, but the average balance of non-accrual loans is included in the denominator when calculating yields.

Dollars in thousands	2011		2010		2009	
	Amount of interest	Average Yield/Rate	Amount of interest	Average Yield/Rate	Amount of interest	Average Yield/Rate
Interest on earning assets						
Interest-bearing deposits	\$12	0.25 %	\$1	0.25 %	\$1	0.25 %
Investment securities	18,220	4.07 %	15,170	4.49 %	14,893	5.42 %
Loans held for sale	30	4.63 %	150	4.73 %	125	4.99 %
Loans	40,150	4.55 %	44,220	4.77 %	49,945	5.09 %
Total interest-earning assets	58,412	4.37 %	59,541	4.70 %	64,964	5.16 %
Interest-bearing liabilities						
Deposits	9,746	1.04 %	10,297	1.15 %	11,872	1.35 %
Borrowings	4,963	2.05 %	6,374	2.76 %	7,044	2.84 %
Total interest-bearing liabilities	14,709	1.25 %	16,671	1.48 %	18,916	1.67 %
Net interest income	\$43,703		\$42,870		\$46,048	
Interest rate spread		3.12 %		3.22 %		3.49 %
Net interest margin		3.27 %		3.38 %		3.66 %

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Average Daily Balance Sheets

The following table shows the Company's average daily balance sheets for the years ended December 31, 2011, 2010 and 2009.

Dollars in thousands	Years ended December 31,		
	2011	2010	2009
Assets			
Cash and cash equivalents	\$ 13,405	\$ 15,722	\$ 14,288
Interest bearing deposits in other banks	4,710	88	407
Securities available for sale	315,255	178,116	29,040
Securities to be held to maturity	117,020	144,601	245,972
Federal Reserve Bank stock, at cost	1,412	1,412	783
Federal Home Loan Bank stock, at cost	14,031	14,031	14,031
Loans held for sale (fair value approximates cost)	648	3,173	2,506
Loans	882,806	926,338	981,628
Allowance for loan losses	(14,418)	(14,393)	(11,277)
Net loans	868,388	911,945	970,351
Accrued interest receivable	5,180	5,397	6,027
Premises and equipment, net of accumulated depreciation	18,690	18,463	18,024
Other real estate owned	5,772	5,276	2,652
Goodwill	27,684	27,684	27,684
Other assets	27,680	29,159	21,752
Total Assets	\$ 1,419,875	\$ 1,355,067	\$ 1,353,517
Liabilities & Shareholders' Equity			
Demand deposits	\$ 76,686	\$ 69,260	\$ 65,567
NOW deposits	123,377	118,400	106,895
Money market deposits	74,945	78,155	108,922
Savings deposits	109,561	97,484	87,921
Certificates of deposit	628,855	597,982	578,713
Total deposits	1,013,424	961,281	948,018
Borrowed funds – short term	135,500	127,160	149,601
Borrowed funds – long term	106,427	103,775	98,690
Dividends payable	989	989	953
Other liabilities	11,281	10,123	9,401
Total Liabilities	1,267,621	1,203,328	1,206,663
Shareholders' Equity:			
Preferred stock	20,290	24,606	24,452
Common stock	98	97	97
Additional paid-in capital	45,652	45,187	44,807
Retained earnings	83,469	81,288	78,072
Accumulated other comprehensive income (loss)			
Net unrealized gains (losses) on available-for-sale securities	2,807	762	(310)
Net unrealized loss on post-retirement benefit costs	(62)	(201)	(264)
Total Shareholders' Equity	152,254	151,739	146,854
Total Liabilities & Shareholders' Equity	\$ 1,419,875	\$ 1,355,067	\$ 1,353,517

Non-Interest Income

Non-interest income in 2011 was \$11.8 million, an increase of \$2.6 million or 28.6% from the \$9.1 million reported in 2010. This increase was attributable to the realignment of the available for sale portfolio. As a result of the sale of \$140.4 million of securities, the Company booked a \$3.3 million gain on investments. There was also a decline of \$658,000 in mortgage origination income due to a lower level of loans sold to the secondary market in 2011 than in 2010.

Non-Interest Expense

Non-interest expense in 2011 was \$26.0 million, an increase of 3.6% from the \$25.1 million reported in 2010. This increase was attributable to salaries and employee benefits and expenses related to other real estate owned and foreclosure costs. There was also a \$540,000 decrease in FDIC insurance premiums.

Provision to the Allowance for Loan Losses

The Company's provision to the allowance for loan losses was \$10.6 million in 2011 compared to \$8.4 million in 2010. This was 0.74% of average assets in 2011, compared to 0.55% of average assets for our peer group. The level of provision in 2011 was to maintain the allowance for loan losses at an appropriate level given the size of our loan portfolio and our overall asset quality. Although the allowance for loan losses decreased by \$316,000 in 2011 from the 2010 level, year-over-year the allowance as a percentage of loans outstanding was unchanged at 1.50%. Given the number of economic uncertainties at this time, Management believes it is prudent to continue to provide for loan losses and that the current level is directionally consistent with the credit quality seen in the portfolio. A further discussion of asset and credit quality can be found in "Assets and Asset Quality".

Net Income

Net income for 2011 was \$12.4 million, up 2.0% or \$248,000 from net income of \$12.1 million that was posted in 2010. Earnings per share on a fully diluted basis were \$1.14, up \$0.04 or 3.6% from the \$1.10 reported for the year ended December 31, 2010.

Key Ratios

Return on average assets in 2011 was 0.87%, down from the 0.89% posted in 2010. Return on average tangible common equity was 10.70% in 2011, compared to 10.83% in 2010 and 12.54% in 2009. In 2011, the Company's dividend payout ratio (dividends declared per share divided by earnings per share) was 68.42%, compared to 70.91% in 2010 and 63.93% in 2009. The Company's efficiency ratio – a benchmark measure of the amount spent to generate a dollar of income – was 49.75% in 2011 compared to 66.26% for the Bank's peer group, on average. In 2010, the Bank's efficiency ratio was 48.15% compared to 67.23% for the Bank's peer group, on average. The rise in the efficiency ratio for 2011 was the result of an increase in operating expenses, primarily in credit-related costs.

Investment Management and Fiduciary Activities

As of December 31, 2011, First Advisors, the Bank's private banking and investment management division, had assets under management with a market value of \$619.3 million, consisting of 730 trust accounts, estate accounts, agency accounts, and self-directed individual retirement accounts. This compares to December 31, 2010, when 674 accounts with a market value of \$562.6 million were under management.

Assets and Asset Quality

Total assets of \$1.373 billion decreased 1.5% or \$20.9 million in 2011 from \$1.394 billion at December 31, 2010. The investment portfolio increased \$8.3 million or 2.0% over December 31, 2010, while the loan portfolio decreased \$22.6 million or 2.5%. Although total assets decreased year-over-year, average assets were up \$64.8 million in 2011 over 2010. Average loans in 2011 were \$43.5 million lower than in 2010, but average investments in 2011 were \$109.5 million higher than in 2010.

While the weaknesses in the national and global economies have not impacted coastal Maine as much as some other parts of the country, we nevertheless experienced a deterioration in asset quality in our loan portfolio. Non-performing assets to total assets stood at 2.32% at December 31, 2011, an increase over 1.87% at December 31, 2010. This increase is attributable to the impact that the weakened economy is having on our borrowers. Small businesses are seeing revenue/sales decreases and some are struggling to meet their obligations with a declining revenue base. A number of consumers have lost their jobs or seen a reduction in hours worked and/or overtime, thereby creating strained finances resulting in payment issues on their loans. In Management's opinion, the Company's long-standing approach to working with borrowers and ethical loan underwriting standards helps alleviate some of the payment problems on customers' loans and in the end minimizes actual loan losses.

Net charge offs in 2011 were \$10.9 million or 1.23% of average loans outstanding. This compares to net charge offs in 2010 of \$8.7 million or 0.94% of average loans outstanding and net charge offs for our UBPR peer group in 2011 of 0.94%. Residential real estate term loans represent 39.5% of the total loan portfolio, and this loan category generally has a lower level of losses in comparison to other loan types. In 2011, the loss ratio for residential mortgages was 0.39% compared to 1.23% for the entire loan portfolio. The Company does not have a credit card portfolio or offer dealer consumer loans which generally carry more risk and therefore higher losses.

The allowance for loan losses ended the year at \$13.0 million and stood at 1.50% of total loans outstanding compared to \$13.3 million and 1.50% of total loans outstanding at December 31, 2010. A \$10.6 million provision for losses was made in 2011 and net charge offs totaled \$10.9 million, resulting in the allowance for loan losses decreasing \$316,000 or 2.4% from December 31, 2010. Management believes the allowance for loan losses is appropriate as of December 31, 2011. In Management's opinion, the level of the provision for loan losses is directionally consistent with the overall credit quality of our loan portfolio and corresponding levels of nonperforming loans and unallocated reserves, as well as with the performance of the national and local economies, high levels of unemployment and the outlook for economic weakness continuing for some time to come.

Investment Activities

During 2011, the investment portfolio increased 2.0% to end the year at \$424.3 million compared to \$416.1 million at December 31, 2010. Average investments in 2011 were \$109.5 million higher than in 2010. During the second and fourth quarters, the Company realigned the available for sale portfolio resulting in a \$3.3 million gain on investments as the result of the sale of \$140.4 million of securities. The Company's investment securities are classified into two categories: securities available for sale and securities to be held to maturity. Securities available for sale consist primarily of debt securities which Management intends to hold for indefinite periods of time. They may be used as part of the Company's funds management strategy, and may be sold in response to changes in interest rates, prepayment risk and liquidity needs, to increase capital ratios, or for other similar reasons. Securities to be held to maturity consist primarily of debt securities that the Company has acquired solely for long-term investment purposes, rather than for trading or future sale. For securities to be categorized as held to maturity, Management must have the intent and the Company must have the ability to hold such investments until their respective maturity dates. The Company does not hold trading account securities.

All investment securities are managed in accordance with a written investment policy adopted by the Board of Directors. It is the Company's general policy that investments for either portfolio be limited to government debt obligations, time deposits, and corporate bonds or commercial paper with one of the three highest ratings given by a

nationally recognized rating agency. The portfolio is currently invested primarily in U.S. Government sponsored agency securities and tax-exempt obligations of states and political subdivisions. The individual securities have been selected to enhance the portfolio's overall yield while not materially adding to the Company's level of interest rate risk. The following table sets forth the Company's investment securities at their carrying amounts as of December 31, 2011, 2010, and 2009.

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Dollars in thousands	2011	2010	2009
Securities available for sale			
U.S. Government sponsored agencies	\$-	\$16,045	\$30,959
Mortgage-backed securities	198,232	234,414	31,148
State and political subdivisions	85,726	41,524	18,514
Corporate securities	811	866	818
Other equity securities	1,433	380	399
	286,202	293,229	81,838
Securities to be held to maturity			
U.S. Government sponsored agencies	19,390	2,190	39,099
Mortgage-backed securities	56,800	55,710	90,193
State and political subdivisions	46,171	49,330	61,095
Corporate securities	300	150	150
	122,661	107,380	190,537
Non-marketable Securities			
Federal Reserve Bank Stock	1,412	1,412	1,412
Federal Home Loan Bank Stock	14,031	14,031	14,031
	15,443	15,443	15,443
Total securities	\$424,306	\$416,052	\$287,818

The following table sets forth information on the yields and expected maturities of the Company's investment securities as of December 31, 2011. Yields on tax-exempt securities have been computed on a tax-equivalent basis using a tax rate of 35%. Mortgage-backed securities are presented according to their contractual maturity date, while the yield takes into effect intermediate cashflows from repayment of principal which results in a much shorter average life.

Dollars in thousands	Available For Sale		Held to Maturity			
	Fair Value	Yield to maturity	Amortized Cost	Yield to maturity		
U.S. Government Sponsored Agencies						
Due in 1 year or less	\$-	0.00 %	\$-	0.00 %		
Due in 1 to 5 years	-	0.00 %	-	0.00 %		
Due in 5 to 10 years	-	0.00 %	5,000	3.00 %		
Due after 10 years	-	0.00 %	14,390	3.19 %		
Total	-	0.00 %	19,390	3.14 %		
Mortgage-Backed Securities						
Due in 1 year or less	6,578	1.30 %	3,692	2.56 %		
Due in 1 to 5 years	16,677	3.38 %	4,028	3.53 %		
Due in 5 to 10 years	22,931	3.08 %	2,326	5.06 %		
Due after 10 years	152,046	3.20 %	46,754	4.57 %		
Total	198,232	3.14 %	56,800	4.39 %		
State & Political Subdivisions						
Due in 1 year or less	195	6.85 %	1,487	6.08 %		
Due in 1 to 5 years	2,796	6.92 %	5,757	6.60 %		
Due in 5 to 10 years	1,134	6.17 %	15,701	6.33 %		
Due after 10 years	81,601	6.29 %	23,226	6.27 %		
Total	85,726	6.31 %	46,171	6.33 %		
Corporate Securities						
Due in 1 year or less	-	0.00 %	-	0.00 %		

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Due in 1 to 5 years	-	0.00	%	300	1.25	%
Due in 5 to 10 years	-	0.00	%	-	0.00	%
Due after 10 years	811	1.48	%	-	0.00	%
Total	811	1.48	%	300	1.25	%
Equity Securities	1,433	3.76	%	-	-	
	\$286,202	4.09	%	\$122,661	4.91	%

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Impaired Securities

The securities portfolio contains certain securities, the amortized cost of which exceeds fair value, which at December 31, 2011 amounted to an excess of \$0.8 million, or 0.19% of the amortized cost of the total securities portfolio. At December 31, 2010 this amount represented an excess of \$5.9 million, or 1.45% of the total securities portfolio. As a part of the Company's ongoing security monitoring process, the Company identifies securities in an unrealized loss position that could potentially be other-than-temporarily impaired. If a decline in the fair value of an available-for-sale security is judged to be other-than-temporary, a charge is recorded in net realized securities losses equal to the difference between the fair value and cost or amortized cost basis of the security.

The Company's evaluation of securities for impairment is a quantitative and qualitative process intended to determine whether declines in the fair value of investment securities should be recognized in current period earnings. The primary factors considered in evaluating whether a decline in the fair value of securities is other-than-temporary include: (a) the length of time and extent to which the fair value has been less than cost or amortized cost and the expected recovery period of the security, (b) the financial condition, credit rating and future prospects of the issuer, (c) whether the debtor is current on contractually obligated interest and principal payments, (d) the volatility of the securities market price, (e) the intent and ability of the Company to retain the investment for a period of time sufficient to allow for recovery, which may be at maturity, and (f) any other information and observable data considered relevant in determining whether other-than-temporary impairment has occurred.

The Company's best estimate of cash flows uses severe economic recession assumptions due to market uncertainty. The Company's assumptions include but are not limited to delinquencies, foreclosure levels and constant default rates on the underlying collateral, loss severity ratios, and constant prepayment rates. If the Company does not expect to receive 100% of future contractual principal and interest, an other-than-temporary impairment charge is recognized. Estimating future cash flows is a quantitative and qualitative process that incorporates information received from third party sources along with certain internal assumptions and judgments regarding the future performance of the underlying collateral.

As of December 31, 2011, the Company had temporarily impaired securities with a fair value of \$23.9 million and unrealized losses of \$0.8 million, as identified in the table below. Securities in a continuous unrealized loss position more than twelve-months amounted to \$9.3 million as of December 31, 2011, compared with \$7.6 million at December 31, 2010. The Company has concluded that these securities were not other-than-temporarily impaired. This conclusion was based on the issuers' continued satisfaction of their obligations in accordance with their contractual terms and the expectation that the issuers will continue to do so, Management's intent and ability to hold these securities for a period of time sufficient to allow for any anticipated recovery in fair value which may be at maturity, the expectation that the Company will receive 100% of future contractual cash flows, as well as the evaluation of the fundamentals of the issuers' financial condition and other objective evidence. The following table summarizes temporarily impaired securities and their approximate fair values at December 31, 2011.

Dollars in thousands	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Government-sponsored agencies	\$-	\$-	\$-	\$-	\$-	\$-
Mortgage-backed securities	12,489	(25)	6,780	(156)	19,269	(181)
State and political subdivisions	1,984	(17)	1,667	(172)	3,651	(189)
Corporate securities	-	-	811	(287)	811	(287)
Other equity securities	154	(120)	34	(19)	188	(139)
	\$14,627	\$(162)	\$9,292	\$(634)	\$23,919	\$(796)

For securities with unrealized losses, the following information was considered in determining that the securities were not other-than-temporarily impaired:

Securities issued by U.S. Government-sponsored agencies. As of December 31, 2011 and 2010 there were no unrealized losses on these securities.

Mortgage-backed securities issued by U.S. Government agencies and U.S. Government-sponsored enterprises. As of December 31, 2011, the total unrealized losses on these securities amounted to \$181,000, compared with \$2.9 million at December 31, 2010. All of these securities were credit rated "AAA" by the major credit rating agencies. Management

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believes that securities issued by U.S. Government agencies bear no credit risk because they are backed by the full faith and credit of the United States and that securities issued by U.S. Government-sponsored enterprises have minimal credit risk, as these agencies enterprises play a vital role in the nation's financial markets. Management believes that the unrealized losses at December 31, 2011 were attributable to changes in current market yields and spreads since the date the underlying securities were purchased, and does not consider these securities to be other-than-temporarily impaired at December 31, 2011. The Company also has the ability and intent to hold these securities until a recovery of their amortized cost, which may be at maturity.

Obligations of state and political subdivisions. As of December 31, 2011, the total unrealized losses on municipal securities amounted to \$189,000, compared with \$2.7 million at December 31, 2010. Municipal securities are supported by the general taxing authority of the municipality and, in the cases of school districts, are supported by state aid. At December 31, 2011, all municipal bond issuers were current on contractually obligated interest and principal payments. The Company attributes the unrealized losses at December 31, 2011 to changes in prevailing market yields and pricing spreads since the dates the underlying securities were purchased, combined with current market liquidity conditions and the disruption in the financial markets in general. Accordingly, the Company does not consider these municipal securities to be other-than-temporarily impaired at December 31, 2011. The Company also has the ability and intent to hold these securities until a recovery of their amortized cost, which may be at maturity.

Corporate securities. As of December 31, 2011, the total unrealized losses on corporate securities amounted to \$287,000, compared with \$247,000 at December 31, 2010. Corporate securities are dependent on the operating performance of the issuers. At December 31, 2011, all corporate bond issuers were current on contractually obligated interest and principal payments. The Company attributes the unrealized losses at December 31, 2011 to changes in prevailing market yields and pricing spreads since the dates the underlying securities were purchased, combined with current market liquidity conditions and the disruption in the financial markets in general. Accordingly, the Company does not consider these corporate securities to be other-than-temporarily impaired at December 31, 2011. The Company also has the ability and intent to hold these securities until a recovery of their amortized cost, which may be at maturity.

Federal Home Loan Bank Stock

Federal Home Loan Bank stock and Federal Reserve Bank stock have also been evaluated for impairment. The Bank is a member of the Federal Home Loan Bank ("FHLB") of Boston. The FHLB is a cooperatively owned wholesale bank for housing and finance in the six New England States. Its mission is to support the residential mortgage and community-development lending activities of its members, which include over 450 financial institutions across New England. As a requirement of membership in the FHLB, the Bank must own a minimum required amount of FHLB stock, calculated periodically based primarily on the Bank's level of borrowings from the FHLB. The Company uses the FHLB for much of its wholesale funding needs. As of December 31, 2011 and 2010, the Company's investment in FHLB stock totaled \$14.0 million.

FHLB stock is a non-marketable equity security and therefore is reported at cost, which equals par value. Shares held in excess of the minimum required amount are generally redeemable at par value. However, in the first quarter of 2009 the FHLB announced a moratorium on such redemptions in order to preserve its capital in response to current market conditions and declining retained earnings, which moratorium remains in effect. The minimum required shares are redeemable, subject to certain limitations, five years following termination of FHLB membership. The Bank has no intention of terminating its FHLB membership.

Although the Company had no dividend income on its FHLB stock in 2010, in each of the four quarters of 2011, FHLB's board of directors declared a dividend equal to an annual yield of 0.30%. FHLB's board of directors anticipates that it will continue to declare modest cash dividends through 2012, but cautioned that adverse events such as a negative trend in credit losses on the FHLB's private-label mortgage-backed securities or mortgage portfolio, a

meaningful decline in income, or regulatory disapproval could lead to reconsideration of this plan.

The Company periodically evaluates its investment in FHLB stock for impairment based on, among other factors, the capital adequacy of the FHLB and its overall financial condition. No impairment losses have been recorded through December 31, 2011. The Bank will continue to monitor its investment in FHLB stock.

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Lending Activities

The loan portfolio declined \$22.6 million or 2.5% in 2011, with total loans at \$865.0 million at December 31, 2011, compared to \$887.6 million at December 31, 2010. Commercial loans decreased \$13.9 million or 3.6% between December 31, 2010 and December 31, 2011, residential term loans increased by \$3.4 million or 1.0% during the same period. At the same time, municipal loans decreased by \$5.6 million or 25.7%. Loan demand in the Bank's market area has been limited in the past three years as a result of continued weak economic conditions. In addition, in order to reduce the Bank's exposure to interest rate risk, the Bank has sold residential mortgages to the secondary market that have been refinanced by borrowers seeking to take advantage of lower interest rates.

Commercial loans are comprised of three categories: commercial real estate loans, commercial construction loans and other commercial loans. Commercial real estate is primarily comprised of loans to small businesses collateralized by owner-occupied real estate, while other commercial is primarily comprised of loans to small businesses collateralized by plant and equipment, commercial fishing vessels and gear, and limited inventory-based lending. Commercial real estate loans typically have a maximum loan-to-value ratio of 75% based upon current appraisal information at the time the loan is made. Commercial construction loans comprise a very small portion of the portfolio, and at 26.0% of capital are well under the regulatory guidance of 100.0% of total risk-based capital. Construction and non-owner-occupied commercial real estate loans are at 98.0% of total capital, well under regulatory guidance of 300.0% of capital. Municipal loans are comprised of loans to municipalities in the State of Maine for capitalized expenditures, construction projects or tax-anticipation notes. All municipal loans are considered general obligations of the municipality and as such are collateralized by the taxing ability of the municipality for repayment of debt. Residential loans are also comprised of two categories, term loans, which include traditional amortizing home mortgages, and construction loans, which include loans for owner-occupied residential construction. Residential loans typically have a 75% to 80% loan to value based upon current appraisal information at the time the loan is made. Home equity loans and lines of credit are generally underwritten to the same standards. Consumer loans are primarily short-term amortizing loans to individuals collateralized by automobiles, pleasure craft and recreation vehicles, with a maximum loan to value ratio of 80%-90% of the purchase price of the collateral. Consumer loans also include a small amount of unsecured short-term time notes to individuals.

The following table summarizes the loan portfolio as of December 31, 2011, 2010, 2009, 2008 and 2007.

		As of December 31,											
Dollars		2011		2010		2009		2008		2007			
in thousands													
Commercial													
Real estate	\$255,424	29.5 %	\$245,540	27.7 %	\$240,178	25.2 %	\$219,057	22.3 %	\$202,301	22.0 %			
Construction	32,574	3.8 %	41,869	4.7 %	48,714	5.1 %	48,182	4.9 %	-	0.0 %			
Other	86,982	10.1 %	101,462	11.4 %	114,486	12.0 %	118,109	12.1 %	109,954	11.9 %			
Municipal	16,221	1.9 %	21,833	2.5 %	45,952	4.8 %	34,832	3.6 %	34,425	3.7 %			
Residential													
Term	341,286	39.5 %	337,927	38.1 %	367,267	38.7 %	431,520	44.0 %	431,237	46.9 %			
Construction	10,469	1.2 %	15,512	1.7 %	17,361	1.8 %	26,235	2.7 %	45,942	5.0 %			
Home equity													
line of credit	105,244	12.1 %	105,297	11.9 %	94,324	9.9 %	77,206	7.9 %	74,199	8.1 %			
Consumer	16,788	1.9 %	18,156	2.0 %	24,210	2.5 %	24,132	2.5 %	22,106	2.4 %			
Total loans	\$864,988	100.0 %	\$887,596	100.0 %	\$952,492	100.0 %	\$979,273	100.0 %	\$920,164	100.0 %			

The following table sets forth certain information regarding the contractual maturities of the Bank's loan portfolio as of December 31, 2011:

Dollars in thousands	< 1 Year	1 - 5 Years	5 - 10 Years	> 10 Years	Total
Commercial					
Real estate	\$7,548	\$17,609	\$21,635	\$208,632	\$255,424
Construction	12,289	1,864	324	18,097	32,574
Other	11,154	23,635	20,371	31,822	86,982
Municipal	406	3,597	6,082	6,136	16,221
Residential					
Term	1,874	12,909	22,189	304,314	341,286
Construction	4,296	644	8	5,521	10,469
Home equity line of credit	958	1,806	547	101,933	105,244
Consumer	7,116	6,200	1,036	2,436	16,788
Total loans	\$45,641	\$68,264	\$72,192	\$678,891	\$864,988

The following table provides a listing of loans by category, excluding loans held for sale, between variable and fixed rates as of December 31, 2011.

Dollars in thousands	Fixed-Rate		Adjustable-Rate		Total	
	Amount	% of total	Amount	% of total	Amount	% of total
Commercial						
Real estate	\$47,799	5.5 %	\$207,625	24.1 %	\$255,424	29.5 %
Construction	624	0.1 %	31,950	3.8 %	32,574	3.8 %
Other	40,423	4.7 %	46,559	5.4 %	86,982	10.1 %
Municipal	16,144	1.9 %	77	0.0 %	16,221	1.9 %
Residential						
Term	137,263	15.9 %	204,023	23.6 %	341,286	39.5 %
Construction	4,360	0.5 %	6,109	0.7 %	10,469	1.2 %
Home equity line of credit	3,148	0.4 %	102,096	11.8 %	105,244	12.1 %
Consumer	13,496	1.6 %	3,292	0.4 %	16,788	1.9 %
Total loans	\$263,257	30.6 %	\$601,731	69.8 %	\$864,988	100.0 %

Loan Concentrations

As of December 31, 2011, the Bank did not have any concentration of loans in one particular industry that exceeded 10% of its total loan portfolio.

Loans Held for Sale

As of December 31, 2011, the Bank did not have any loans held for sale. This compares to \$2.8 million at December 31, 2010. Loans held for sale are carried at the lower of cost or market value. No recourse obligations have been incurred in connection with the sale of loans.

Credit Risk Management and Allowance for Loan Losses

Credit risk is the risk of loss arising from the inability of a borrower to meet its obligations. We manage credit risk by evaluating the risk profile of the borrower, repayment sources, the nature of the underlying collateral, and other support given current events, conditions, and expectations. We attempt to manage the risk characteristics of our loan portfolio through various control processes, such as credit evaluation of borrowers, establishment of lending limits, and application of lending procedures, including the holding of adequate collateral and the maintenance of compensating balances. However, we seek to rely primarily on the cash flow of our borrowers as the principal source of repayment. Although credit policies and evaluation processes are designed to minimize our risk, Management recognizes that loan losses will occur and the amount of these losses will fluctuate depending on the risk characteristics of our loan portfolio,

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as well as general and regional economic conditions.

We provide for loan losses through the establishment of an allowance for loan losses which represents an estimated reserve for existing losses in the loan portfolio. We deploy a systematic methodology for determining our allowance that includes a quarterly review process, and adjustment to our allowance. We classify our portfolios as either residential and consumer or commercial and monitor credit risk separately as discussed below. We evaluate the adequacy of our allowance continually based on a review of significant loans, with a particular emphasis on nonaccruing, past due, and other loans that we believe require special attention.

The allowance consists of four elements: (1) specific reserves for loans evaluated individually for impairment; (2) general reserves for types or portfolios of loans based on historical loan loss experience, (3) qualitative reserves judgmentally adjusted for local and national economic conditions, concentrations, portfolio composition, volume and severity of delinquencies and nonaccrual loans, trends of criticized and classified loans, changes in credit policies, and underwriting standards, credit administration practices, and other factors as applicable; and (4) unallocated reserves. All outstanding loans are considered in evaluating the adequacy of the allowance.

The appropriate level of the allowance for loan losses is determined using a consistent, systematic methodology, which analyzes the risk inherent in the loan portfolio. In addition to evaluating the collectability of specific loans when determining the appropriate level of the allowance for loan losses, Management also takes into consideration other factors such as changes in the mix and size of the loan portfolio, historical loss experience, the amount of delinquencies and loans adversely classified, economic trends, changes in credit policies, and experience, ability and depth of lending management. The allowance for loan losses is developed by an allocation process whereby specific loss allocations are made against certain adversely classified loans, and general loss allocations are made against segments of the loan portfolio which have similar attributes. The Company's historical loss experience, industry trends, and the impact of the local and regional economy on the Company's borrowers, are considered by Management in determining the appropriate level of the allowance for loan losses.

The allowance for loan losses is increased by provisions charged against current earnings. Loan losses are charged against the allowance when Management believes that the collectability of the loan principal is unlikely. Recoveries on loans previously charged off are credited to the allowance. While Management uses available information to assess possible losses on loans, future additions to the allowance may be necessary based on increases in non-performing loans, changes in economic conditions, growth in loan portfolios, or for other reasons. Any future additions to the allowance would be recognized in the period in which they were determined to be necessary. In addition, various regulatory agencies periodically review the Company's allowance for loan losses as an integral part of their examination process. Such agencies may require the Company to record additions to the allowance based on judgments different from those of Management.

Commercial

Our commercial portfolio includes all secured and unsecured loans to borrowers for commercial purposes, including commercial lines of credit and commercial real estate. Our process for evaluating commercial loans includes performing updates on loans that we have rated for risk. Our non-performing commercial loans are generally reviewed individually to determine impairment, accrual status, and the need for specific reserves. Our methodology incorporates a variety of risk considerations, both qualitative and quantitative. Quantitative factors include our historical loss experience by loan type, collateral values, financial condition of borrowers, and other factors. Qualitative factors include judgments concerning general economic conditions that may affect credit quality, credit concentrations, the pace of portfolio growth, and delinquency levels. These qualitative factors are also considered in connection with our unallocated portion of our allowance for loan losses.

The process of establishing the allowance with respect to our commercial loan portfolio begins when a loan officer initially assigns each loan a risk rating, using established credit criteria. Approximately 50% of our outstanding loans and commitments are subject to review and validation annually by an independent consulting firm, as well as periodically by our internal credit review function. The methodology employs Management's judgment as to the level of losses on existing loans based on our internal review of the loan portfolio, including an analysis of a borrower's

current financial position, and the consideration of current and anticipated economic conditions and their potential effects on specific borrowers and lines of business. In determining our ability to collect certain loans, we also consider the fair value of underlying collateral. We also evaluate credit risk concentrations, including trends in large dollar exposures to related borrowers, industry and geographic concentrations, and economic and environmental factors.

Consumer and Residential

Consumer and residential mortgage loans are generally segregated into homogeneous pools with similar risk characteristics. Trends and current conditions in consumer and residential mortgage pools are analyzed and historical loss experience is adjusted accordingly. Quantitative and qualitative adjustment factors for the consumer and

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residential mortgage portfolios are consistent with those for the commercial portfolios. Certain loans in the consumer and residential portfolios identified as having the potential for further deterioration are analyzed individually to confirm the appropriate risk classification and accrual status, and to determine the need for a specific reserve. Consumer loans greater than 120 days past due are generally charged off. Residential loans 90 days or more past due are placed on non-accrual status unless the loans are both well secured and in the process of collection.

Unallocated

The unallocated portion of the allowance is intended to provide for losses that are not identified when establishing the specific and general portions of the allowance and is based upon Management's evaluation of various conditions that are not directly measured in the determination of the portfolio and loan specific allowances. Such conditions include general economic and business conditions affecting our lending area, credit quality trends (including trends in delinquencies and nonperforming loans expected to result from existing conditions), loan volumes and concentrations, specific industry conditions within portfolio categories, recent loss experience in particular loan categories, duration of the current business cycle, bank regulatory examination results, findings of external loan review examiners, and Management's judgment with respect to various other conditions including loan administration and management and the quality of risk identification systems. Management reviews these conditions quarterly. We have risk management practices designed to ensure timely identification of changes in loan risk profiles; however, undetected losses may exist inherently within the loan portfolio. The judgmental aspects involved in applying the risk grading criteria, analyzing the quality of individual loans, and assessing collateral values can also contribute to undetected, but probable, losses.

The allowance for loan losses includes reserve amounts to assigned individual loans on the basis of loan impairment. Certain loans are evaluated individually and are judged to be impaired when Management believes it is probable that the Company will not collect all of the contractual interest and principal payments as scheduled in the loan agreement. Under this method, loans are selected for evaluation based on internal risk ratings or non-accrual status. A specific reserve is allocated to an individual loan when that loan has been deemed impaired and when the amount of a probable loss is estimable on the basis of its collateral value, the present value of anticipated future cash flows, or its net realizable value. At December 31, 2011, impaired loans with specific reserves totaled \$14.2 million and the amount of such reserves was \$2.1 million. This compares to impaired loans with specific reserves of \$9.5 million at December 31, 2010 and the amount of such reserves was \$1.3 million.

All of these analyses are reviewed and discussed by the Directors' Loan Committee, and recommendations from these processes provide Management and the Board of Directors with independent information on loan portfolio condition. Our total allowance at December 31, 2011 is considered by Management to be appropriate to address the credit losses inherent in the loan portfolio at that date. Management views the level of the allowance for loan losses as appropriate. However, our determination of the appropriate allowance level is based upon a number of assumptions we make about future events, which we believe are reasonable, but which may or may not prove valid. Thus, there can be no assurance that our charge offs in future periods will not exceed our allowance for loan losses or that we will not need to make additional increases in our allowance for loan losses.

The following table summarizes our allocation of allowance by loan type as of December 31, 2011, 2010, 2009, 2008 and 2007. The percentages are the portion of each loan type to total loans.

Dollars in thousands	As of December 31,											
	2011		2010		2009		2008		2007			
Commercial												
Real estate	\$5,659	29.5 %	\$5,260	27.7 %	\$4,986	25.2 %	\$2,958	22.3 %	\$3,020	22.0 %		
Construction	658	3.8 %	1,012	4.7 %	807	5.1 %	650	4.9 %	-	0.0 %		
Other	2,063	10.1 %	2,377	11.4 %	3,363	12.0 %	2,595	12.1 %	1,633	11.9 %		
Municipal	19	1.9 %	19	2.5 %	23	4.8 %	20	3.6 %	25	3.7 %		

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Residential											
Term	1,159	39.5 %	1,408	38.1 %	1,198	38.7 %	713	44.0 %	706	46.9 %	
Construction	255	1.2 %	44	1.7 %	174	1.8 %	44	2.7 %	75	5.0 %	
Home equity											
line of credit	595	12.1 %	670	11.9 %	515	9.9 %	482	7.9 %	491	8.1 %	
Consumer	584	1.9 %	646	2.0 %	717	2.5 %	662	2.5 %	606	2.4 %	
Unallocated	2,008	0.0 %	1,880	0.0 %	1,854	0.0 %	676	0.0 %	244	0.0 %	
Total	\$13,000	100.0%	\$13,316	100.0%	\$13,637	100.0%	\$8,800	100.0%	\$6,800	100.0%	

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The allowance for loan losses totaled \$13.0 million at December 31, 2011, compared to \$13.3 million at December 31, 2010. Management's ongoing application of methodologies to establish the allowance include an evaluation of non-accrual loans and troubled debt restructured for specific reserves. These specific reserves increased \$0.8 million in 2011 from \$1.3 million at December 31, 2010 to \$2.1 million at December 31, 2011. The specific loans that make up those categories change from period to period. The portion of the reserve based upon homogeneous pools of loans increased by \$234,000 in 2011. The portion of the reserve based on qualitative factors decreased by \$1.5 million during 2011 due to less uncertainty with real estate appraisal values. Despite the shifts in specific, pooled and qualitative reserves, Management feels that market trends and other internal factors justified the minimal increase in unallocated reserves during 2011.

A breakdown of the allowance for loan losses as of December 31, 2011, by loan segment and allowance element, is presented in the following table:

In thousands of dollars	Specific Reserves Evaluated Individually for Impairment	General Reserves Based on Historical Loss Experience	Reserves for Qualitative Factors	Unallocated Reserves	Total Reserves
Commercial					
Real estate	\$ 808	\$2,578	\$2,273	\$-	\$5,659
Construction	33	332	293	-	658
Other	402	883	778	-	2,063
Municipal	-	-	19	-	19
Residential					
Term	478	222	459	-	1,159
Construction	235	6	14	-	255
Home equity line of credit	91	149	355	-	595
Consumer	11	331	242	-	584
Unallocated	-	-	-	2,008	2,008
	\$ 2,058	\$4,501	\$4,433	\$2,008	\$13,000

Based upon Management's evaluation, provisions are made to maintain the allowance as a best estimate of inherent losses within the portfolio. The provision for loan losses to maintain the allowance was \$10.6 million in 2011 compared to \$8.4 million in 2010. Net charge offs were \$10.9 million in 2011 compared to net charge offs of \$8.7 million in 2010. Year-over-year the allowance as a percentage of loans outstanding was unchanged at 1.50%.

The following table summarizes the activities in our allowance for loan losses as of December 31, 2011, 2010, 2009, 2008 and 2007:

Dollars in thousands	As of December 31,					
	2011	2010	2009	2008	2007	
Balance at beginning of year	\$13,316	\$13,637	\$8,800	\$6,800	\$6,364	
Loans charged off:						
Commercial						
Real estate	1,619	4,005	2,430	3	27	
Construction	346	175	-	-	-	
Other	6,473	1,125	2,329	1,997	477	
Municipal	19	-	-	-	-	
Residential						
Term	1,421	392	1,767	113	13	
Construction	505	2,361	47	-	-	
Home equity line of credit	415	8	177	83	50	
Consumer	381	951	826	745	770	
Total	11,179	9,017	7,576	2,941	1,337	
Recoveries on loans previously charged off						
Commercial						
Real estate	23	4	-	-	-	
Construction	-	-	-	-	-	
Other	42	69	79	32	142	
Municipal	18	-	-	-	-	
Residential						
Term	7	4	59	5	4	
Construction	-	-	-	-	-	
Home equity line of credit	1	-	1	-	21	
Consumer	222	219	114	204	174	
Total	313	296	253	241	341	
Net loans charged off	10,866	8,721	7,323	2,700	996	
Provision for loan losses	10,550	8,400	12,160	4,700	1,432	
Balance at end of period	\$13,000	\$13,316	\$13,637	\$8,800	\$6,800	
Ratio of net loans charged off to average loans outstanding	1.23	% 0.94	% 0.75	% 0.28	% 0.11	%
Ratio of allowance for loan losses to total loans outstanding	1.50	% 1.50	% 1.43	% 0.90	% 0.74	%

Management believes the allowance for loan losses is appropriate as of December 31, 2011. In Management's opinion, the level of provision for loan losses and the corresponding decrease in the allowance for loan losses from December 31, 2010, is directionally consistent with the decline in the size of our loan portfolio and corresponding levels of specific reserves and unallocated reserves.

Nonperforming Loans

Nonperforming loans are comprised of loans, for which based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement or when principal and interest is 90 days or more past due unless the loan is both well secured and in the process of collection (in which case the loan may continue to accrue interest in spite of its past due status). A loan is “well secured” if it is secured (1) by collateral in the form of liens on or pledges of real or personal property, including securities, that have a realizable value sufficient to discharge the debt (including accrued interest) in full, or (2) by the guarantee of a financially responsible party. A loan is “in the process of collection” if collection of the loan is proceeding in due course either (1) through legal action, including judgment enforcement procedures, or, (2) in appropriate circumstances, through collection efforts not involving legal action which are reasonably expected to result in repayment of the debt or in its restoration to a current status in the near future.

When a loan becomes nonperforming (generally 90 days past due), it is evaluated for collateral dependency based upon the most recent appraisal or other evaluation method. If the collateral value is lower than the outstanding loan balance plus accrued interest and estimated selling costs, the loan is placed on non-accrual status, all accrued interest is reversed from interest income, and a specific reserve is established for the difference between the loan balance and the collateral value less selling costs. At the same time, and if secured by real estate, a new independent, third-party appraisal may be ordered, based on the currency of the most recent appraisal and the size of the loan, and upon receipt of the new appraisal the loan may have an additional specific reserve or write down based upon the new appraisal information.

On an ongoing basis, if a non-performing loan is collateral dependent as its source of repayment, we may have an independent appraisal done periodically, based on the currency of the most recent appraisal and the size of the loan, and an additional specific reserve or write down based upon the new appraisal information will be made if appropriate. Once a loan is placed on nonaccrual, it remains in nonaccrual status until the loan is current as to payment of both principal and interest and the borrower demonstrates the ability to pay and remain current. All payments made on nonaccrual loans are applied to the principal balance of the loan.

Nonperforming loans, expressed as a percentage of total loans, totaled 3.21% at December 31, 2011 compared to 2.39% at December 31, 2010. The following table shows the distribution of nonperforming loans and loans greater than 90 days past due as of December 31, 2011, 2010, 2009, 2008 and 2007:

Dollars in thousands	As of December 31,				
	2011	2010	2009	2008	2007
Commercial					
Real estate	\$7,064	\$5,946	\$6,589	\$7,477	\$734
Construction	2,350	937	458	-	-
Other	5,836	2,277	2,735	2,908	2,011
Municipal	-	-	-	-	-
Residential					
Term	11,312	8,932	6,322	6,594	2,109
Construction	1,198	3,567	3,182	-	-
Home equity line of credit	1,163	519	143	313	299
Consumer	53	113	309	137	1
Total loans 90 or more days past due	\$28,976	\$22,291	\$19,738	\$17,429	\$5,154
Non-accrual loans included in above total	\$27,806	\$21,175	\$18,562	\$12,449	\$2,867

Total nonperforming loans does not include loans 90 or more days past due and still accruing interest. These are loans in which we expect to collect all amounts due, including past-due interest. As of December 31, 2011, loans 90 or more days past due and still accruing interest totaled \$1.2 million, compared to \$1.1 million at December 31, 2010.

Troubled Debt Restructured

A restructuring of debt constitutes a troubled debt restructuring (“TDR”) if the Bank, for economic or legal reasons related to the borrower’s financial difficulties, grants a concession to the borrower that it would not otherwise consider. To determine whether or not a loan should be classified as a TDR, Management evaluates a loan based upon the following criteria:

- The borrower demonstrates financial difficulty; common indicators include past due status with bank obligations, substandard credit bureau reports, or an inability to refinance with another lender, and
- The Bank has granted a concession; common concession types include maturity date extension, interest rate adjustments to below market pricing, and deferment of payments.

As of December 31, 2011 we had 59 loans with a value of \$22.9 million that have been restructured. This compares to 32 loans with a value of \$5.5 million as of December 31, 2010. As of December 31, 2011, Management is aware of six loans classified as TDRs that are involved in bankruptcy with an outstanding balance of \$1.0 million as well as two loans in the process of foreclosure totaling \$240,000. There were 19 loans with an outstanding balance of \$3.4 million that were classified as TDRs and were on non-accrual status.

Impaired Loans

Impaired loans include restructured loans and loans placed on non-accrual status when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. These loans are measured at the present value of expected future cash flows discounted at the loan’s effective interest rate or at the fair value of the collateral if the loan is collateral dependent. If the measure of an impaired loan is lower than the recorded investment in the loan and estimated selling costs, a specific reserve is established for the difference. Impaired loans totaled \$42.1 million at December 31, 2011, and have increased \$16.8 million from December 31, 2010. The number of impaired loans increased by 36 loans from 175 to 211 during the same period. Impaired commercial loans increased \$14.2 million from December 31, 2010 to December 31, 2011. The specific allowance for impaired commercial loans increased from \$635,000 at December 31, 2010 to \$1.2 million as of December 31, 2011, which represented the fair value deficiencies for those loans for which the net fair value of the collateral was estimated at less than our carrying amount of the loan. From December 31, 2010 to December 31, 2011, impaired residential loans increased \$2.0 million, impaired home equity lines of credit increased \$644,000, and impaired consumer loans decreased \$53,000.

The following table sets forth impaired loans as of December 31, 2011, 2010, 2009, 2008 and 2007:

Dollars in thousands	As of December 31,				
	2011	2010	2009	2008	2007
Commercial					
Real estate	\$10,141	\$5,946	\$6,198	\$7,477	\$1,105
Construction	5,702	937	458	-	-
Other	7,042	1,753	2,638	2,742	2,281
Municipal	-	-	-	-	-
Residential					
Term	16,821	12,455	13,149	2,163	86
Construction	1,198	3,567	3,182	-	-
Home equity line of credit	1,163	519	143	67	-
Consumer	53	106	75	-	13
Total	\$42,120	\$25,283	\$25,843	\$12,449	\$3,485

Past Due Loans

The Bank's overall loan delinquency ratio was 3.07% at December 31, 2011, versus 3.15% at December 31, 2010. Loans 90 days delinquent and accruing increased slightly from \$1.1 million at December 31, 2010 to \$1.2 million as of December 31, 2011. This total is made up of 6 loans, with the largest loan totaling \$942,000. We expect to collect all amounts due on these loans, including interest.

The following table sets forth loan delinquencies as of December 31, 2011, 2010, 2009, 2008 and 2007:

Dollars in thousands	As of December 31,				
	2011	2010	2009	2008	2007
Commercial					
Real estate	\$6,864	\$6,055	\$9,443	\$10,446	\$2,607
Construction	1,777	1,057	458	584	325
Other	2,623	4,440	3,607	4,713	8,393
Municipal	-	-	-	-	-
Residential					
Term	12,174	12,231	11,747	11,526	8,803
Construction	1,198	1,828	3,182	-	-
Home equity line of credit	1,614	2,038	682	1,423	872
Consumer	347	266	775	609	496
Total	\$26,597	\$27,915	\$29,894	\$29,301	\$21,496
Loans 30-89 days past due to total loans	1.00	% 1.32	% 1.26	% 1.21	% 1.78
Loans 90+ days past due and accruing to total loans	0.14	% 0.13	% 0.12	% 0.51	% 0.25
Loans 90+ days past due on non-accrual to total loans	1.93	% 1.70	% 1.76	% 1.27	% 0.31
Total past due loans to total loans	3.07	% 3.15	% 3.14	% 2.99	% 2.34

As of December 31, 2011, the UBPR peer group had loans 30-89 days past due of 0.88% and loans 90+ days past due on non-accrual of 2.57%.

Potential Problem Loans and Loans in Process of Foreclosure

Potential problem loans consist of classified accruing commercial and commercial real estate loans that were between 30 and 89 days past due. Such loans are characterized by weaknesses in the financial condition of borrowers or collateral deficiencies. Based on historical experience, the credit quality of some of these loans may improve due to changes in collateral values or the financial condition of the borrowers, while the credit quality of other loans may deteriorate, resulting in some amount of loss. These loans are not included in the analysis of non-accrual loans. At December 31, 2011, there were 28 potential problem loans with a balance of \$4.7 million or 0.5% of total loans. This compares to 32 loans with a balance of \$3.9 million or 0.4% of total loans at December 31, 2010.

As of December 31, 2011, there were 45 loans in the process of foreclosure with a total balance of \$8.2 million. The Bank's foreclosure process begins when a loan becomes 45 days past due at which time a preliminary foreclosure letter is sent to the borrower. If the loan becomes 80 days past due, copies of the promissory note and mortgage deed are forwarded to the Bank's attorney for review and an affidavit for a Motion for Summary Judgment is then prepared. An authorized Bank officer signs the affidavit certifying the validity of the documents and verification of the past due amount which is then forwarded to the court. Once a Motion for Summary Judgment is granted, a Period of Redemption (POR) begins which gives the customer 90 days to cure the default. A foreclosure auction date is then set 30 days from the POR expiration date if the default is not cured.

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In March and October 2011, the Bank conducted self-audits of its loans in foreclosure and its foreclosure process and found there were no deficiencies or areas to improve. For loans sold to the secondary market on which servicing is retained, the Bank follows Freddie Mac's and Fannie Mae's published guidelines and regularly reviews these guidelines for updates and changes to process. All secondary market loans have been sold without recourse in a non-securitized, one-on-one basis. As a result, the Bank has no liability for these loans in the event of a foreclosure.

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Other Real Estate Owned

Other real estate owned and repossessed assets (“OREO”) are comprised of properties or other assets acquired through a foreclosure proceeding, or acceptance of a deed or title in lieu of foreclosure. Real estate acquired through foreclosure is carried at the lower of cost or fair value less estimated cost to sell. At December 31, 2011, there were 16 properties owned with a net OREO balance of \$4.1 million, net of an allowance for losses of \$0.4 million, compared to December 31, 2010 when there were 18 properties owned with a net OREO balance of \$4.9 million, net of an allowance for losses of \$0.1 million. The following table presents the composition of other real estate owned as of December 31, 2011, 2010, 2009, 2008 and 2007:

Dollars in thousands	As of December 31,				
	2011	2010	2009	2008	2007
Carrying Value					
Commercial					
Real estate	\$-	\$-	\$-	\$-	\$-
Construction	59	424	1,182	1,172	1,152
Other	1,504	1,795	1,920	731	-
Municipal	-	-	-	-	-
Residential					
Term	2,967	2,842	2,826	849	-
Construction	-	-	-	-	-
Home equity line of credit	-	-	-	-	-
Consumer	-	-	-	-	-
Total	\$4,530	\$5,061	\$5,928	\$2,752	\$1,152
Related Allowance					
Commercial					
Real estate	\$-	\$-	\$-	\$-	\$-
Construction	-	-	476	325	325
Other	127	66	-	-	-
Municipal	-	-	-	-	-
Residential					
Term	309	66	107	-	-
Construction	-	-	-	-	-
Home equity line of credit	-	-	-	-	-
Consumer	-	-	-	-	-
Total	\$436	\$132	\$		