COMMUNITY BANKSHARES INC /SC/
Form 10-Q
November 13, 2006

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2006 Commission File No. 000-22054

COMMUNITY BANKSHARES, INC.
(Exact name of registrant as specified in its charter)

South Carolina	57-0966962
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

102 Founders Court
Orangeburg, South Carolina 29118
(Address of principal executive offices, zip code)

(803) 535-1060
(Registrant's telephone number, including area code)

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 [X] No [ ]

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):

Large accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer [X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [X]

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: Common Stock, no par or stated value, 4,442,220 shares outstanding on October 27, 2006.

COMMUNITY BANKSHARES, INC.

FORM 10-Q

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PART I - FINANCIAL INFORMATION

Item 1. - Financial Statements

COMMUNITY BANKSHARES, INC.
Consolidated Balance Sheets

Assets

Cash and due from banks ....

Federal funds sold ....

Total cash and cash equivalents ....
Interest bearing deposits with other banks ....
Securities available-for-sale ....
Securities held-to-maturity (estimated fair value $1,802 for 2006
and $1,820 for 2005) ....
Other investments ....
Loans held for sale ....
Loans receivable ....
Less, allowance for loan losses ....

Net loans ....
Premises and equipment - net ....
Accrued interest receivable ....
Net deferred income tax assets ....
Goodwill ....
Core deposit intangible assets ....
Prepaid expenses and other assets ....

Total assets ....

Liabilities
Deposits
Noninterest bearing ....
Interest bearing ....

Total deposits ....
Short-term borrowings ....
Long-term debt ....
Accrued interest payable ....
Accrued expenses and other liabilities ....

Total liabilities ....

Shareholders' equity
Common stock - no par value; 12,000,000 shares authorized; issued and
outstanding - 4,442,220 for 2006 and
4,404,303 for 2005 ....
Retained earnings ....
Accumulated other comprehensive income (loss) ....

Total shareholders' equity ....

Total liabilities and shareholders' equity ....

See accompanying notes to unaudited consolidated financial statements.

COMMUNITY BANKSHARES, INC.
Consolidated Statements of Income

	(Un	
	Period E	
	Three Months	
	2006	2005
	(Dollars in thous	
Interest and dividend income		
Loans, including fees	$ 8,587	$ 7,702
Interest bearing deposits with other banks	33	11
Debt securities	607	464
Dividends	39	35
Federal funds sold	350	192
Total interest and dividend income	9,616	8,404
Interest expense		
Deposits		
Time deposits $100M and over	1,066	818
Other deposits	2,460	1,577
Total interest expense on deposits	3,526	2,395
Short-term borrowings	88	53
Long-term debt	458	481
Total interest expense	4,072	2,929
Net interest income	5,544	5,475
Provision for loan losses	665	2,300
Net interest income after provision	4,879	3,175
Noninterest income		
Service charges on deposit accounts	852	948
Mortgage loan brokerage income	963	1,041
Net securities gains or (losses)	-	-
Other	143	197
Total noninterest income	1,958	2,186
Noninterest expenses		
Salaries and employee benefits	2,798	2,550
Premises and equipment	648	552
Other	1,460	1,347
Total noninterest expenses	4,906	4,449
Income before income taxes	1,931	912
Income tax expense	730	330
Net income	$ 1,201	$ 582
Per share		
Net income	$ 0.27	$ 0.13
Net income - diluted	0.27	0.13
Cash dividends declared	0.11	0.10

See accompanying notes to unaudited consolidated financial statements.

COMMUNITY BANKSHARES, INC.
Consolidated Statements of Changes in Shareholders' Equity

(Unaudited)

	Common Stock Number of Shares	Common Stock Amount	Reta Earn
		(Dollars in thou	
Balance, January 1, 2005	4,390,784	$ 30,042	$
Comprehensive income:			
Net income	-	-	
Unrealized holding gains and losses on available-for-sale securities arising during the period, net of income taxes of $136	-	-	
Reclassification adjustment for losses (gains) realized in income, net of income taxes of $3	-	-	
Total other comprehensive income	-	-	
Total comprehensive income	-	-	
Proceeds of sale of common stock	775	14	
Exercise of employee stock options	12,744	146	
Cash dividends declared, $.30 per share	-	-	
Balance, September 30, 2005	4,404,303	$ 30,202	$
Balance, January 1, 2006	4,404,303	$ 30,202	$
Comprehensive income:			
Net income	-	-	
Unrealized holding gains and losses on available-for-sale securities arising during the period, net of income taxes of $76	-	-	
Reclassification adjustment for losses (gains) realized in income, net of income taxes of $0	-	-	
Total other comprehensive income (loss)	-	-	
Total comprehensive income	-	-	
Proceeds of sale of common stock	1,000	16	

Exercise of employee stock options	36,917	396	
Cash dividends declared, $.33 per share	-	-	
Balance, September 30, 2006	4,442,220	$ 30,614	$

See accompanying notes to unaudited consolidated financial statements.

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COMMUNITY BANKSHARES, INC.
Consolidated Statements of Cash Flows

Operating activities

Net income ....
Adjustments to reconcile net income to net
cash provided by operating activities
Provision for loan losses ....
Depreciation and amortization ....
Amortization of intangibles ....
Net amortization of securities ....
Net securities (gains) or losses ....
Proceeds of sales of loans held for sale ....
Originations of loans held for sale ....
Increase in accrued interest receivable ....
Decrease (increase) in other assets ....
Losses (gains) on sale of other real estate ....
Increase in accrued interest payable ....
Increase in other liabilities ....

Net cash provided by operating activities ....

Investing activities
Net (increase) decrease in interest bearing deposits with other banks ....
Purchases of available-for-sale securities ....
Maturities, calls and paydowns of available-for-sale securities ....
Proceeds of sales of available-for-sale securities ....
Net decrease (increase) in other investments ....
Net increase in loans made to customers ....
Purchases of premises and equipment ....
Proceeds from sales of other real estate ....

Net cash used by investing activities	
Financing activities	
Net increase in deposits	
Net (decrease) increase in short-term borrowings	
Proceeds from issuing long-term debt	
Repayment of long-term debt	
Exercise of employee stock options	
Sale of common stock	
Cash dividends paid	
Net cash (used) provided by financing activities	
Increase in cash and cash equivalents	
Cash and cash equivalents, beginning of period	
Cash and cash equivalents, end of period	
Supplemental Disclosures of Cash Flow Information	
Cash payments for interest, including $5 capitalized	
during construction in 2005	
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Transfer to net deferred income tax assets from prepaid current income taxes	

See accompanying notes to unaudited consolidated financial statements.

COMMUNITY BANKSHARES, INC.

Notes to Unaudited Consolidated Financial Statements

Organization - Pursuant to a plan approved by CBI's Board of Directors in the first quarter of 2006 and subsequently approved by regulatory authorities, CBI's subsidiary Orangeburg National Bank was renamed Community Resource Bank N.A. in the third quarter of 2006. After the close of business of September 29, 2006, also pursuant to those plans and approvals, the remaining three subsidiary banks (Sumter National Bank, Florence National Bank and Bank of Ridgeway) were merged into Community Resource Bank, N.A. Community Resource Bank, N.A. (the "Bank") and Community Resource Mortgage, Inc. now comprise CBI's operating subsidiaries.

Accounting Principles - A summary of significant accounting policies and the audited financial statements for 2005 are included in Community Bankshares, Inc.'s (the "Company" or "CBI") Annual Report on Form 10-K for the year ended December 31, 2005 filed with the Securities and Exchange Commission. Certain amounts in the 2005 financial statements have been reclassified to conform to the current presentation. Such reclassifications had no effect on net income or retained earnings for any period.

Management Opinion - The interim financial statements in this report are unaudited. In the opinion of management, all the adjustments necessary to present a fair statement of the results for the interim period have been made. Such adjustments are of a normal and recurring nature. The results of operations for any interim period are not necessarily indicative of the results to be expected for an entire year. These interim financial statements should be read in conjunction with the annual financial statements and notes thereto contained in the 2005 Annual Report on Form 10-K.

Nonperforming Loans - As of September 30, 2006, there were $8,668,000 in nonaccrual loans and $377,000 of loans 90 or more days past due and still accruing interest.

Earnings Per Share - Basic earnings per share is computed by dividing net income applicable to common shares by the weighted average number of common shares outstanding. Diluted earnings per share is computed by dividing applicable net income by the weighted average number of shares outstanding and any dilutive potential common shares and dilutive stock options. It is assumed that all dilutive stock options are exercised at the beginning of each period and that the proceeds are used to purchase shares of the Company's common stock at the average market price during the period. Net income per share and net income per share, assuming dilution, were computed as follows:

	(Una	
	Period Ende	
	Three Months	
	2006	2005
	(Dollars in thousand	
Net income per share, basic		
Numerator - net income	$ 1,201	$ 582
Denominator		
Weighted average common shares		
issued and outstanding	4,439,245	4,404,303
Net income per share, basic	$ .27	$ .13
Net income per share, assuming dilution		
Numerator - net income	$ 1,201	$ 582
Denominator		
Weighted average common shares		
issued and outstanding	4,439,245	4,404,303
Effect of dilutive stock options	78,967	97,744
Total shares	4,518,212	4,502,047

Net income per share, assuming dilution	$ .27	$ .13
	==========	==========

Share-Based Compensation - Effective January 1, 2006, the Company began accounting for compensation expenses related to stock options granted to employees and directors under the recognition and measurement principles of Statement of Accounting Standards No. 123(R) "Share-Based Payment" ("SFAS 123(R)) using the modified prospective application method. The Company had previously elected to continue using the methodology of Accounting Principles Board Opinion No. 25 ("APB No. 25"), "Accounting for Stock Issued to Employees," to account for compensation expenses related to share-based compensation until the mandatory effective date for SFAS 123(R).

Options previously issued under the Company's plans had no intrinsic value at the grant date and no compensation cost was recognized in accordance with APB No. 25. Statement of Financial Accounting Standards No. 123 ("SFAS No. 123"), "Accounting for Stock-Based Compensation," required entities to provide pro forma disclosures of net income, and earnings per share, as if the fair value based method of accounting promulgated by that standard had been applied. Under the modified prospective application method of SFAS 123(R), the Company is required to apply SFAS 123(R) only to new awards and to awards modified, repurchased or cancelled after the required effective date. Also, compensation cost would be recognized for the portions of previously granted awards outstanding which had not vested on the effective date. The Company had no such awards outstanding as of January 1, 2006.

Variable Interest Entity - On March 8, 2004, CBI sponsored the creation of a Variable Interest Entity ("VIE"), SCB Capital Trust I (the "Trust"), and is the sole owner of the common securities issued by the Trust. On March 10, 2004, the Trust issued $10,000,000 in floating rate capital securities. The proceeds of this issuance, and the amount of CBI's investment in the common securities, were used to acquire $10,310,000 principal amount of CBI's floating rate junior subordinated deferrable interest debt securities ("Debentures") due April 7, 2034, which securities, and the accrued interest thereon, now constitute the Trust's sole assets. The interest rate associated with the Debentures and the

capital securities, and the distribution rate on the common securities of the Trust, was established initially at 3.91% and is adjustable quarterly at 3 month LIBOR plus 280 basis points. The index rate (LIBOR) may not be lower than 1.11%. CBI may defer interest payments on the Debentures for up to twenty consecutive quarters, but not beyond the stated maturity date of the Debentures. In the event that such interest payments are deferred by CBI, the Trust may defer distributions on the common securities. In such an event, CBI would be restricted in its ability to pay dividends on its common stock and to perform under other obligations that are not senior to the junior subordinated Debentures.

The Debentures are redeemable at par at the option of CBI, in whole or in part, on any interest payment date on or after April 7, 2009. Prior to that date, the Debentures are redeemable at 105% of par upon the occurrence of certain events that would have a negative effect on the Trust or that would cause it to be required to be registered as an investment company under the Investment Company Act of 1940 or that would cause trust preferred securities not to be eligible to be treated as Tier 1 capital by the Federal Reserve Board.

Upon repayment or redemption of the Debentures, the Trust will use the proceeds of the transaction to redeem an equivalent amount of trust preferred securities and trust common securities. The Trust's obligations under the trust preferred securities are unconditionally guaranteed by CBI.

The Company's investment in the common securities of the Trust is carried at cost in other assets and the Debentures are included in long-term debt in the consolidated balance sheet.

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

Forward Looking Statements

Statements included in this report which are not historical in nature are intended to be, and are hereby identified as `forward-looking statements' for purposes of the safe harbor provided by Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements which are other than statements of historical facts. Such forward-looking statements may be identified, without limitation, by the use the of the words "anticipates," "believes," "estimates," "expects," "intends," "plans," "predicts," "projects," and similar expressions. The Company's expectations, beliefs, estimates, intentions, plans, predictions and projections are expressed in good faith and are believed by the Company to have a reasonable basis, including without limitation, management's examination of historical operating trends, data contained in the Company's records and other data available from third parties, but there can be no assurance that management's expectations, beliefs, estimates, intentions, plans, predictions or projections will result or be achieved or accomplished. The Company cautions readers that forward-looking statements, including without limitation, those relating to the Company's recent and continuing expansion, its future business prospects, revenues, working capital, liquidity, capital needs, interest costs, income, and adequacy of the allowance for loan losses, are subject to risks and uncertainties that could cause actual results to differ materially from those indicated in the forward-looking statements, due to several important factors herein identified, among others, and other risks and factors identified from time to time in the Company's reports filed with the Securities and Exchange Commission. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

References to our Website Address

References to our website address throughout this Quarterly Report on Form 10-Q and in any documents incorporated into this Form 10-Q by reference are for informational purposes only, or to fulfill specific disclosure requirements of the Securities and Exchange Commission's rules or the American Stock Exchange listing standards. These references are not intended to, and do not, incorporate the contents of our website by reference into this Form 10-Q or the accompanying materials.

Critical Accounting Policies

CBI has adopted various accounting policies, which govern the application of accounting principles generally accepted in the United States of America in the preparation of CBI's financial statements. The significant accounting policies of CBI are described in detail in the notes to CBI's audited consolidated financial statements included in CBI's 2005 Annual Report on Form 10-K filed with the Securities and Exchange Commission.

Certain accounting policies involve significant judgments and estimates by management, which have a material impact on the carrying value of certain assets and liabilities. Management considers such accounting policies to be critical accounting policies. The judgments and estimates used by management are based on historical experience and other factors, which are believed to be reasonable under the circumstances. Because of the nature of the judgments and assumptions made by management, actual results could differ from these judgments and estimates, which could have a material impact on the carrying values of assets and liabilities and the results of operations of CBI.

CBI is a bank holding company and, as a financial institution, believes the allowance for loan losses is a critical accounting policy that requires the most significant judgments and estimates used in preparation of its consolidated financial statements. Refer to the sections "Allowance for Loan Losses" and "Provision for Loan Losses" in the Annual Report on Form 10-K for 2005 for a detailed description of CBI's estimation process and methodology related to the allowance for loan losses.

Pursuant to a plan approved by CBI's Board of Directors in the first quarter of 2006 and subsequently approved by regulatory authorities, CBI's subsidiary Orangeburg National Bank was renamed Community Resource Bank N.A. in the third quarter of 2006. After the close of business on September 29, 2006, also pursuant to those plans and approvals, the remaining three subsidiary banks (Sumter National Bank, Florence National Bank and Bank of Ridgeway) were merged into Community Resource Bank, N.A. Community Resource Bank, N.A. and Community Resource Mortgage, Inc. now comprise CBI's operating subsidiaries. In accordance with generally accepted acconting principles, the accounting for the merger between these affiliated entities was treated in a manner similar to a pooling of interests.

CHANGES IN FINANCIAL CONDITION

During the nine months ended September 30, 2006, long-term debt, in the form of FHLB advances, decreased by $6,007,000, noninterest bearing deposits decreased by $7,218,000 and interest bearing deposits increased by $13,826,000.

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Also during the first nine months of 2006, loans held for sale increased by $1,972,000, gross loans receivable decreased by $1,878,000, federal funds sold increased by $7,646,000 and securities available-for-sale decreased by $3,043,000.

During the first nine months of 2006, net charge-offs of loans totaled $4,542,000, including $1,482,000 in the third quarter. Those net charge-offs decreased both loans and the allowance for loan losses.

During the third quarter of 2006, federal funds sold increased by $23,323,000, loans held for sale decreased by $6,373,000 and gross loans receivable decreased by $7,064,000. Interest bearing deposits increased by $11,830,000 during the 2006 three-month period and short-term borrowings decreased by $4,590,000. Because of high interest rates for federal funds and the the pending consolidation of the four banks' charters, planned for the fourth quarter, management made a deliberate decision to maintain relatively high liquidity.

During the third quarter, there were inconsistencies between the four markets in how effectively and efficiently loans and deposits were attracted. Generally, time and savings deposit growth was relatively easy to attract. Loan growth was challenging and was reduced by loan charge-offs.

Early in the fourth quarter, after merger of the banks, management began making its deposit products consistent between markets. The Bank has added an attractive, interest-bearing checking account and money market account in an effort to improve growth in core deposits, and anticipates less emphasis on time deposits. At the same time, the Bank has begun actively marketing certain select loan products, and is currently focusing on home equity lines of credit.

RESULTS OF OPERATIONS

Earnings Performance

Three Months Ended September 30, 2006 and 2005

For the quarter ended September 30, 2006, CBI recorded consolidated net income of $1,201,000, compared with $582,000 for the comparable period of 2005. This represents an increase of $619,000 or 106.4%. Basic and diluted earnings per share were $.27 in the 2006 period, compared with $.13 for the 2005 quarter.

Compared with the third quarter of 2005, operating results for the third quarter of 2006 were affected primarily by lower provisions for loan losses in the 2006 period, a reduction in service charges assessed against deposit accounts, and an increase in noninterest expenses. Generally, market interest rates, as well as the rates associated with the Company's interest earning assets and its interest-bearing liabilities were higher in the 2006 period as a result of Federal Reserve efforts to slow the nation's economy and control inflation. More recently, the Federal Reserve has not increased its federal funds rate target. The last such increase was made in June 2006.

The provision for loan losses for the third quarter of 2006 was lower than for the same period of 2005 due to continuing efforts to effect positive changes in the quality of the Company's loan portfolio. Significant progress has been, and continues to be, made in identifying problem loans, meeting with borrowers and obtaining liens on additional collateral to better secure such

loans, and establishing more realistic plans for repayment of loans. In an effort to further reduce the future level of risk in the loan portfolio, management has implemented more stringent underwriting controls intended to proactively mitigate risks in the loan portfolio before loans are funded or committed. Such controls include more vigorously monitoring established loan officer approval authorities, developing and utilizing more detailed analyses of positive and negative factors during underwriting, increased scrutiny of financial and other information pertaining to potential borrowers, and limiting the aggregate amounts of loans that can be approved for various purposes. Management has implemented different requirements for conforming and non-conforming loans in order to expedite the approval of credit requests that present minimal risk to the Bank. The provision and allowance for loan losses continue to be affected by high levels of non-performing and potential problem loans and charge-offs. During the third quarter of 2006, net charge-offs were $1,482,000 compared with $454,000 during the same period of 2005.

Noninterest expenses increased in part because of changes in the corporate management structure designed to enhance controls and risk management activities, particularly in the lending function. Also, in 2006, the Company increased its formula for matching employees' contributions to the 401(k) defined contribution retirement plan. This resulted in higher levels of employee participation in the plan. Expenses of premises and equipment increased in the 2006 quarter due to the Company's moving into its newly constructed headquarters and operations center building in the first quarter of 2006 and the leasing of other office space to provide for the needs of certain management and other personnel who are located away from the corporate headquarters. Also, in conjunction with renaming one of the banking subsidiaries and merging all the former four subsidiary banks into that renamed bank, the Company incurred higher expenses for advertising and stationery and supplies.

Summary Inc

(Dollars i

For the Three Months Ended September 30,	2006	2005
Interest income	$ 9,616	$ 8,404
Interest expense	4,072	2,929
Net interest income	5,544	5,475
Provision for loan losses	665	2,300
Noninterest income	1,958	2,186
Noninterest expenses	4,906	4,449
Income tax expense	730	330
Net income	$ 1,201	$ 582

Nine Months Ended September 30, 2006 and 2005

For the nine months ended September 30, 2006, CBI recorded consolidated net income of $3,775,000, compared with $3,493,000 for the comparable period of 2005. This represents an increase of $282,000 or 8.1%. Basic earnings per share were $.85 in the 2006 period, compared with $.79 for the 2005 quarter. Diluted earnings per share for the 2006 nine months period were $.84 compared with $.78 for the same period of 2005.

CBI's consolidated net income for the nine months ended September 30, 2006 was positively affected by a reduced amount of provision for loan losses, and increased levels of net interest income, primarily related to increased loan volumes and yields. A significant proportion of the Bank's loan portfolio is made up of variable rate loans. Those loans have been repriced favorably several times during 2006. The prime rate, which is the index to which most of those variable rate loans are related, increased four times totaling 100 basis points during 2006, and eight times totaling 200 basis points since September 30, 2005.

Noninterest income for the 2006 nine-months period increased slightly from the amount for the same period of 2005. However, slight reductions were noted in the 2006 amounts of service charges on deposit accounts and credit insurance sales. Noninterest expenses negatively affected results for the 2006 year-to-date period because of the same factors discussed above for the third quarter.

Summary Income S

(Dollars in thou

For the Nine Months Ended September 30,	2006	2005
Interest income	$27,332	$23,431
Interest expense	11,194	7,648
Net interest income	16,138	15,783
Provision for loan losses	1,955	3,335
Noninterest income	5,952	5,817
Noninterest expenses	14,165	12,793
Income tax expense	2,195	1,979
Net income	$ 3,775	$ 3,493

Net Interest Income

Net interest income is the amount of interest income earned on interest earning assets (primarily loans, securities, interest bearing deposits with other banks, and federal funds sold), less the interest expense incurred on interest bearing liabilities (interest bearing deposits and other borrowings), and is the principal source of the Company's earnings. Net interest income is affected by the level of interest rates, volume and mix of interest earning assets and interest bearing liabilities and the relative funding of those assets.

Three Months Ended September 30, 2006 and 2005

Net interest income for the three months ended September 30, 2006 was $5,544,000, an increase of $69,000, or 1.3%, over the amount reported for the third quarter of 2005. Interest income and interest expense for the 2006 quarter were both significantly higher than during the same period of 2005, primarily due to increases in the interest rates earned on, or paid for, those items.

The average rate earned on loans, including loans held for sale, was 7.95% and 7.03% for the third quarters of 2006 and 2005, respectively. The average yield on earning assets was 7.35% for the third quarter of 2006, compared with 6.46% for the third quarter of 2005. The average cost of time deposits increased to 4.31% for the third quarter of 2006, compared with 3.20%

for the same period of 2005. The average cost of all interest-bearing liabilities was 3.69% for the 2006 quarter and 2.72% for the same period of 2005. Accordingly, the interest rate spread (interest earning assets yield minus the rate paid for interest-bearing liabilities) for the 2006 third quarter narrowed to 3.66%, or 8 basis points lower than for the same period of 2005. Net yield on earning assets (net interest income divided by average interest earning assets) for the 2006 quarter was 4.24%, or 3 basis points higher than for the same period of 2005.

Average amounts of interest earning assets were approximately $2,584,000 higher in the 2006 period than in the 2005 period. However, more robust growth in the average amounts of interest-bearing liabilities was noted as the 2006 average amount was approximately $11,454,000 more than the 2005 amount. During the third quarter of 2006, the Company was more reliant on interest-bearing liabilities to fund earning assets than it was during the 2005 second quarter.

Average Balances,
Quarter Ended S

	2006 Average Balances	2006 Interest Income / Expense	2006 Yields / Rates (1)	
			(Dollars in	
Assets				
Interest bearing deposits with other banks	$ 1,772	$ 33	7.39%	$
Investment securities - taxable	55,848	601	4.27%	
Investment securities - tax exempt (2)	4,917	45	3.63%	
Federal funds sold	27,830	350	4.99%	
Loans, including loans held for sale (2)(3)	428,544	8,587	7.95%	
Total interest earning assets	518,911	9,616	7.35%	
Cash and due from banks	15,839			
Allowance for loan losses	(9,382)			
Premises and equipment, net	9,699			
Intangible assets	7,004			
Other assets	8,736			
Total assets	$ 550,807			$
Liabilities and shareholders' equity				
Interest bearing deposits				
Savings	$ 90,231	$ 674	2.96%	$
Interest bearing transaction accounts	66,453	182	1.09%	
Time deposits	245,619	2,670	4.31%	
Total interest bearing deposits	402,303	3,526	3.48%	
Short-term borrowings	11,536	88	3.03%	
Long-term debt	24,501	458	7.42%	
Total interest bearing liabilities	438,340	4,072	3.69%	

Noninterest bearing demand deposits	54,758			
Other liabilities	3,360			
Shareholders' equity	54,349			
	---------			-
Total liabilities and shareholders' equity ..	$ 550,807			$
	=========			=
Interest rate spread			3.66%	
Net interest income and net yield on earning assets		$ 5,544	4.24%	

(1) Yields and rates are annualized.
(2) Yields on tax-exempt securities and loans have not been stated on a tax-equivalent basis.
(3) Nonaccruing loans are included in the average balances and income from such loans is recognized on a cash basis.

Nine Months Ended September 30, 2006 and 2005

Net interest income for the nine months ended September 30, 2006 increased by $355,000, or 2.2% over the amount for the same period of 2005. Both interest income and interest expense increased significantly in the 2006 period due to continued increases in market interest rates and higher levels of interest earning assets and interest-bearing liabilities.

For the 2006 year-to-date period, the interest rate spread and net yield on earning assets both decreased as compared with the same period of 2005. Interest rate spread decreased by 20 basis points and net yield on earning assets decreased by 9 basis points. These decreases resulted primarily from higher rates paid on interest-bearing liabilities, which increased slightly more than rates earned on earning assets. Average amounts of interest earning assets, especially loans and federal funds sold, were higher in the 2006 period, and net interest income increased despite the narrowing of interest margins.

	Average Balance		
	Nine Months E		
	2006		
	Average Balances	Interest Income / Expense	Yield Rates
			(Dollar
Assets			

Interest bearing deposits with other banks	$ 1,701	$ 88	6.92
Investment securities - taxable	56,798	1,694	3.99
Investment securities - tax exempt (2)	5,100	136	3.57
Federal funds sold	27,541	988	4.80
Loans, including loans held for sale (2) (3)	430,801	24,426	7.58
Total interest earning assets	521,941	27,332	7.00
Cash and due from banks	15,503		
Allowance for loan losses	(10,456)		
Premises and equipment, net	9,988		
Intangible assets	7,065		
Other assets	8,482		
Total assets	$ 552,523		
Liabilities and shareholders' equity			
Interest bearing deposits			
Savings	$ 88,268	$ 1,701	2.58
Interest bearing transaction accounts	71,163	580	1.09
Time deposits	240,811	7,220	4.01
Total interest bearing deposits	400,242	9,501	3.17
Short-term borrowings	9,848	278	3.77
Long-term debt	29,089	1,415	6.50
Total interest bearing liabilities	439,179	11,194	3.41
Noninterest bearing demand deposits	58,301		
Other liabilities	2,943		
Shareholders' equity	52,100		
Total liabilities and shareholders' equity	$ 552,523		
Interest rate spread			3.59
Net interest income and net yield on earning assets		$ 16,138	4.13

(1) Yields andrates are annualized.
(2) Yields on tax-exempt securities and loans have not been stated on a tax-equivalent basis.
(3) Nonaccruing loans are included in the average balances and income from such loans is recognized on a cash basis.

Provision and Allowance for Loan Losses

The provision for loan losses for the 2006 three month period was $665,000, a decrease of $1,635,000, or 71.1%, from $2,300,000 for the same period of 2005. The provision for loan losses decreased to $1,955,000 for the 2006 nine month period from $3,335,000 for the 2005 nine month period, a

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decrease of $1,380,000 or 41.4%. Although the provisions for loan losses were lower in 2006 for each of the periods, high levels of charge-offs and nonperforming and potential problem loans continue to affect the Company's allowance and provision for loan losses negatively. Management continues to use new information about these loans to refine its estimates of the loans' ultimate collectibility and the adequacy of its loan loss allowance.

Net charge-offs during the nine months ended September 30, 2006 were $4,542,000, compared with $1,024,000 for the same period of 2005. The coverage ratio (allowance for loan losses divided by nonperforming loans) was 1.00x as of September 30, 2006 and .94x as of December 31, 2005.

The activity in the allowance for loan losses is summarized in the following table:

	Nine Months Ended September 30, 2006
	(Dol
Allowance at beginning of period	$ 11,641
Transfer of allowance for off-balance-sheet contingencies to other liabilities	-
Provision for loan losses	1,955
Net charge-offs	(4,542)
Allowance at end of period	$ 9,054
Allowance as a percentage of loans outstanding	2.20%
Loans at end of period	$ 412,106

Following is a summary of nonperforming loans as of September 30, 2006 and December 31, 2005:

	September 30, 2006	December 31, 2005
	(Dollars in thousands)	
Nonperforming loans		
Nonaccrual loans	$ 8,668	$11,651
Past due 90 days or more and still accruing	377	729
Total	$ 9,045	$12,380
Nonperforming loans as a percentage of:		
Loans outstanding	2.19%	2.99%
Allowance for loan losses	99.90%	106.35%

The following table shows quarterly changes in nonperforming and potential problem loans since December 31, 2004.

	Nonaccrual Loans	90 Days or More Past Due and Still Accruing	Total Nonperforming Loans	Percen of To Loa
			(Dollars in thousands	
December 31, 2004	$ 4,941	$ 137	$ 5,078	1.
Net change	118	215	333	
March 31, 2005	5,059	352	5,411	1.
Net change	200	(9)	191	
June 30, 2005	5,259	343	5,602	1.
Net change	4,954	74	5,028	
September 30, 2005	10,213	417	10,630	2.
Net change	1,438	312	1,750	
December 31, 2005	11,651	729	12,380	2.
Net change	3,128	949	4,077	
March 31, 2006	14,779	1,678	16,457	3.
Net change	(3,628)	(1,476)	(5,104)	
June 30, 2006	11,151	202	11,353	2.
Net change	(2,483)	175	(2,308)	
September 30, 2006	$ 8,668	$ 377	$ 9,045	2.

During the second quarter of 2006, management settled a loan relationship of $1,450,000 that was included in nonaccrual loans as of March 31, 2006, realizing a recovery of approximately $350,000. During the first nine months of 2006, management focused on reviewing and establishing workout or collection plans or providing other credit enhancements for all significant nonperforming and potential problem loans.

During the 2006 third quarter, approximately $829,000 of loans were first recognized as nonaccrual loans. Of the $2,483,000 net decrease in nonaccrual loans during the third quarter of 2006, approximately $1,357,000 was attributable to writedowns or charge-offs. The remainder of the net decrease represents payments received, amounts refinanced with significant credit enhancements and returned to accruing status, and loans paid in full during the period.

Management will continue to monitor the levels of nonperforming loans and address the weaknesses in these credits to enhance the ultimate collection or recovery of these assets. Management considers the levels and trends in nonperforming assets and potential problem loans in determining how the provision and allowance for loan losses is estimated and adjusted. In the opinion of management, the Company's allowance for loan losses at September 30, 2006 is adequate to provide for losses that may be inherent in the loan portfolio.

Noninterest Income

Noninterest income for the 2006 third quarter decreased $228,000, or

10.4%, from the $2,186,000 reported for the same 2005 period. Mortgage loan brokerage income for the 2006 quarter decreased by $78,000, or 7.5%, from the

$1,041,000 recorded in the 2005 period as a result of declining market demand. Service charges on deposit accounts were $96,000, or 10.1%, less than for the 2005 three-month period, primarily as a result of increases in earnings credits applied to commercial accounts.

For the nine months ended September 30, 2006, noninterest income was $135,000, or 2.3% more than for the first nine months of 2005. Mortgage loan brokerage income increased $195,000.

Noninterest Expenses

Noninterest expenses for the third quarter of 2006 were $457,000, or 10.3%, higher than the amounts reported for the same period of 2005. Salaries and employee benefits expenses were $248,000, or 9.7%, higher in the 2006 period, due to additions made to the Company's executive management. Expenses related to premises and equipment increased by $96,000 in the 2006 period, primarily due to the Company's occupancy of its new headquarters and operations center building during the first quarter of 2006.

Noninterest expenses for the first nine months of 2006 were $1,372,000, or 10.7%, more than for the same period of 2005. Salaries and employee benefits for the 2006 nine month period were $968,000, or 13.5%, more than for the same period of 2005. This expense increased due to higher levels of mortgage loan brokerage commission-based compensation incurred in the 2006 period, additions made to the Company's executive management, increased employee participation in the Company's 401(k) plan, and normal periodic wage and salary adjustments. Expenses associated with premises and equipment were $248,000, or 15.1%, higher in the 2006 period, primarily due to the Company's occupancy of its new headquarters and operations center building during the first quarter of 2006.

Income Taxes

Income tax expense was $400,000 more in the 2006 third quarter than for the 2005 period. Income tax expense for the 2006 nine month period was $216,000 more than for the same period of 2005.

LIQUIDITY

Liquidity is the ability to meet current and future obligations through liquidation or maturity of existing assets or the acquisition of additional liabilities. Adequate liquidity is necessary to meet the requirements of customers for loans and deposit withdrawals in a timely and economical manner. The most manageable sources of liquidity are composed of liabilities, with the primary focus of liquidity management being the ability to attract deposits within CBI's market areas. Individual and commercial deposits are the primary source of funds for lending activities, along with long-term borrowings from the Federal Home Loan Bank of Atlanta and the proceeds of issuing $10,000,000 of subordinated debentures. Cash and amounts due from banks and federal funds sold are CBI's primary sources of asset liquidity. These funds provide a cushion against short-term fluctuation in cash flow from both loans and deposits. Securities available-for-sale are CBI's principal source of secondary asset liquidity. However, the availability of this source is limited by pledging commitments for public deposits and securities sold under agreements to repurchase, and is influenced by market conditions.

CBI and the Bank also maintain various federal funds lines of credit with correspondent banks and are able to borrow from the Federal Home Loan Bank of Atlanta ("FHLB") and the Federal Reserve Bank's discount window.

Total deposits as of September 30, 2006 were $470,817,000, an increase of $6,608,000, or 1.4%, from the amount as of December 31, 2005. During the nine months ended September 30, 2006, there was a notable movement of funds from noninterest bearing demand deposit accounts and interest-bearing transaction accounts into savings and certificate of deposit accounts. Such transfers of funds are the expected result of the higher rates of interest currently being paid for longer-term fixed-rate deposits, and the larger difference between the rates currently being paid for such fixed rate deposits and the rates currently being paid for more highly liquid interest bearing deposits. As of September 30, 2006 the loan to deposit ratio, excluding loans held for sale, was 87.5%, compared with 89.2% at December 31, 2005 and 91.0% at September 30, 2005.

Management believes CBI and its subsidiaries' liquidity sources are adequate to meet their current and projected operating needs.

CAPITAL RESOURCES

CBI and the Bank are subject to regulatory risk-based capital adequacy standards. Under these standards, bank holding companies and banks are required to maintain certain minimum ratios of capital to risk-weighted assets and average total assets. Under the provisions of the Federal Deposit Insurance Corporation Improvement Act of 1991, federal bank regulatory authorities are required to implement prescribed "prompt corrective actions" upon the deterioration of the capital position of a bank. If the capital position of an affected institution were to fall below a certain level, increasingly stringent regulatory corrective actions would be mandated.

During the first quarter of 2004, CBI sponsored the creation of a Trust that issued $10,000,000 in trust preferred securities. The Trust invested the proceeds of this issuance and $310,000 of capital provided by CBI into $10,310,000 of junior subordinated debentures due in 2034 ("Debentures") issued by CBI. Interest payments on the Debentures are due quarterly at a variable interest rate. CBI used the proceeds of the Debentures to repay certain pre-existing debt obligations, to enhance the capital position of two of its former subsidiary banks, to provide an additional funding mechanism for its mortgage loan brokerage activities, and for other general corporate purposes. Under current regulatory guidelines, the trust preferred securities issued by the Trust are includible in the Company's Tier 1 capital for risk-based capital purposes.

Immediately prior to the consolidation of the banking subsidiaries, each bank was "well capitalized" under applicable regulatory definitions and guidelines. The September 30, 2006 risk-based capital ratios for CBI and its banking subsidiaries, prior to the merger, are presented in the following table, compared with the "well capitalized" and minimum ratios under the regulatory definitions and guidelines:

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	Tier 1
Community Bankshares, Inc.	13.64%
Community Resource Bank, N.A. - pre-merger	11.73%
Sumter National Bank	11.42%
Florence National Bank	10.33%
Bank of Ridgeway	10.65%
Minimum "well capitalized" requirement	6.00%
Minimum requirement	4.00%

The following table shows the pro forma capital positions of the Company and the Bank immediately after the merger of the former banking subsidiaries.

	October 1, 2006		
	Tier 1	Total Capital	Leverage
Community Bankshares, Inc.	13.64%	14.87%	10.32%
Community Resource Bank, N.A. - pro forma post-merger	11.73%	12.84%	8.57%

OFF-BALANCE-SHEET ARRANGEMENTS

In the normal course of business, CBI engages in transactions that, in accordance with generally accepted accounting principles, are not recorded in the financial statements (generally commitments to extend credit) or are recorded in amounts that differ from their notional amounts (generally derivatives). These transactions involve elements of credit, interest rate and liquidity risk of varying degrees. Such transactions are used by CBI for general corporate purposes.

Variable Interest Entity

As discussed under "Capital Resources" and in the notes to unaudited consolidated financial statements under "Variable Interest Entity," as of September 30, 2006, CBI held an equity interest in, and guarantees the liabilities of, a non-consolidated variable interest entity.

Commitments

CBI's banking and mortgage brokerage subsidiaries are parties to credit related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of their customers. These financial instruments include commitments to extend credit and standby letters of credit. Such commitments involve varying degrees of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. Exposure to credit loss is represented by the contractual, or notional, amounts of these commitments. The same credit policies are used in making commitments as for on-balance-sheet instruments.

The following table sets forth the contractual amounts of commitments which represent credit risk:

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	September 30, 2006 (Dollars in thousands)
Loan commitments	$ 66,478
Standby letters of credit	2,693

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being fully drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if deemed necessary by management upon extension of credit, is based on management's credit evaluation of the counter-party. Collateral held varies but may include personal residences, accounts receivable, inventory, property, plant and equipment, and income-producing commercial properties.

Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. Those letters of credit are primarily issued to support private borrowing arrangements. All letters of credit are short-term guarantees. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Generally, collateral supporting those commitments is held if deemed necessary. Since many of the standby letters of credit are expected to expire without being drawn upon, the total letter of credit amounts do not necessarily represent future cash requirements.

In mid-2005, CBI reached an agreement with Jack Henry & Associates, Inc. to obtain licensing rights for a new core management information software system, known as Silverlake. The cost of this core system conversion is approximately $1,000,000, substantially all of which had been expended through September 30, 2006. The agreement also requires CBI to pay various support and maintenance costs throughout the licensing period. CBI estimates that during the next five years these costs will range from approximately $200,000 to $300,000 per year. However, the exact amounts will be determined by future events, such as asset growth, and cannot be exactly determined at this time. The Company completed the process of converting to the new system early in the fourth quarter of 2006.

Derivative Financial Instruments

In April, 2003, the Financial Accounting Standards Board issued Statement No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." Among other requirements, this Statement provides that loan commitment contracts entered into or modified after June 30, 2003 that relate to the origination of mortgage loans that will be held for sale shall be accounted for as derivative instruments by the issuer of the loan commitment. In March, 2004, the SEC issued its Staff Accounting Bulletin No 105 "Application of Accounting Principles to Loan Commitments," which resulted in no changes in CBI's accounting for such commitments. CBI issues mortgage loan rate lock commitments to potential borrowers to facilitate its origination of home mortgage loans that are intended to be sold. Between the time that CBI issues its commitments and the time that the loans close and are sold, CBI is subject to variability in the selling prices related to those commitments due to changes in market rates of interest. However, CBI offsets this variability through the use of so-called "forward sales contracts" to investors in the secondary market. Under these arrangements, an investor agrees to purchase the closed loans at a predetermined price. CBI generally enters into such forward sales contracts at the same time that rate lock commitments are issued. These arrangements effectively insulate CBI from the effects of changes in interest rates during the time the commitments are outstanding, but the arrangements do not qualify as

fair value hedges. These derivative financial instruments are carried in the balance sheet at estimated fair value and changes in the estimated fair values of these derivatives are recorded in the statement of income in net gains or losses on loans held for sale.

Derivative financial instruments are written in amounts referred to as notional amounts. Notional amounts only provide the basis for calculating payments between counterparties and do not represent amounts to be exchanged between parties or a measure of financial risk. The following table includes the notional principal amounts of rate lock commitments and forward sales contracts as of September 30, 2006, and the estimated fair values of those financial instruments included in other assets and liabilities in the balance sheet as of that date.

	September 30, 2006	
	Notional Amount	Estimated Fair Value Asset (Liability)
	(Dollars in thousands)	
Rate lock commitments to potential borrowers to originate mortgage loans to be held for sale	$ 46,407	$ 168
Forward sales contracts with investors of mortgage loans to be held for sale	46,407	(168)

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market risk is the risk of loss from adverse changes in market prices and rates. CBI's market risk arises principally from interest rate risk inherent in its lending, deposit and borrowing activities. Management actively monitors and manages its interest rate risk exposure. Although CBI manages other risks, such as credit quality and liquidity risk in the normal course of business, management considers interest rate risk to be its most significant market risk and this risk could potentially have the largest material effect on CBI's financial condition and results of operations. Other types of market risks such as foreign currency exchange risk and commodity price risk do not arise in the normal course of community banking activities.

CBI's Asset/Liability Committee uses a simulation model to assist in achieving consistent growth in net interest income while managing interest rate risk. According to the model, as of September 30, 2006, CBI is positioned so that net interest income would increase $178,000 and net income would increase $107,000 in the next twelve months if interest rates rose 100 basis points. Conversely, net interest income would decline $178,000 and net income would decline $107,000 in the next twelve months if interest rates declined 100 basis points. Computation of prospective effects of hypothetical interest rate changes are based on numerous assumptions, including relative levels of market interest rates and loan prepayment, and should not be relied upon as indicative of actual results. Further, the computations do not contemplate any actions CBI and its customers could undertake in response to changes in interest rates.

As of September 30, 2006 there was no significant change from the interest rate sensitivity analysis for the various changes in interest rates

calculated as of December 31, 2005. The foregoing disclosures related to the market risk of CBI should be read in connection with Management's Discussion and Analysis of Financial Position and Results of Operations included in the 2005 Annual Report on Form 10-K.

Item 4. Controls and Procedures

Based on the evaluation required by 17 C.F.R. Section 240.13a-15(b) or 240.15d-15(b) of the Company's disclosure controls and procedures (as defined in 17 C.F.R. Sections 240.13a-15(e) or 240.15d-15(e)), the Company's chief executive officer and chief financial officer concluded that such controls and procedures, as of the end of the period covered by this quarterly report, were effective.

There has been no change in the Company's internal control over financial reporting during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II--OTHER INFORMATION

Item 6. Exhibits

Exhibits 31-1	Rule 13a-14(a)/15d-14(a) Certification of principal executive officer
31-2	Rule 13a-14(a)/15d-14(a) Certification of principal financial officer
32	Certifications Pursuant to 18 U.S.C. Section 1350

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

DATED: November 13, 2006

COMMUNITY BANKSHARES, INC.

By: s/ Samuel L. Erwin

Samuel L. Erwin
Chief Executive Officer

By: s/ William W. Traynham

William W. Traynham
President and Chief Financial Officer
(Principal Accounting Officer)

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EXHIBIT INDEX

31-1	Rule 13a-14(a)/15d-14(a) Certification of principal executive officer
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