

Board of Governors of the Federal Reserve System
Washington, D.C. 20551

FORM 10-Q

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

For the quarterly period ended June 30, 2008

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

For the transition period from _____ to _____

BANK OF MCKENNEY

(Exact name of registrant as specified in its charter)

Virginia

54-0132540

(State or other jurisdiction of incorporation or organization)

(IRS employer identification no.)

20718 First Street

McKenney, Virginia

23872

(Address of principal executive offices)

(Zip Code)

(804) 478-4434

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

Large accelerated filer

Accelerated Filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

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

Yes No

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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by the court.

Yes No

SEC 1296 (02-08) **Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB control number.**

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the last practical date.

1,926,656 shares of Common Stock, par value \$2.00 per share (August 8, 2008)

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

BANK OF MCKENNEY AND SUBSIDIARY Consolidated Balance Sheets

June 30, 2008 (unaudited) and December 31, 2007

	June 30, 2008	December 31, 2007
ASSETS		
Cash and due from banks	\$ 5,220,281	\$ 3,666,898
Federal funds sold	791,000	7,557,000
Interest-bearing time balances in other banks	3,013,819	--
Securities available for sale, at fair market value	32,023,011	28,807,961
Restricted investments	974,525	1,274,025
Loans:		
Commercial	7,532,668	7,607,912
Commercial real estate	46,716,979	45,470,030
Real estate construction	11,343,870	12,287,132
Residential real estate	41,225,931	39,050,277
Consumer	2,485,438	2,612,284
Loans, gross	\$ 109,304,886	\$ 107,027,635
Less allowance for loan losses	(956,525)	(925,000)
Loans, net	\$ 108,348,361	\$ 106,102,635
Land, premises and equipment, net	8,360,425	8,361,377
Other real estate owned	199,063	--
Accrued interest receivable	874,066	752,668
Bank owned life insurance	3,062,282	2,999,852
Other assets	1,896,253	1,669,037
Total Assets	\$ 164,763,086	\$ 161,191,453
LIABILITIES		
Deposits:		
Noninterest-bearing deposits	\$ 24,907,956	\$ 24,279,539
Savings and interest bearing demand deposits	35,384,778	28,556,694
Time deposits	77,326,301	74,682,839
Total deposits	\$ 137,619,035	\$ 127,519,072
Federal Home Loan Bank advances	7,500,000	13,666,667
Accrued interest payable	382,528	416,040
Accrued expenses and other liabilities	1,004,852	1,520,973
Total Liabilities	\$ 146,506,415	\$ 143,122,752
Commitments and contingencies	\$ --	\$ --
SHAREHOLDERS' EQUITY		
Common stock, \$2 par value, authorized 2,250,000 shares issued and outstanding 1,926,656 shares	\$ 3,853,312	\$ 3,853,312
Surplus	5,893,958	5,893,958
Retained earnings	8,854,019	8,240,118
Accumulated other comprehensive income/(loss)	(3,446,218)	81,313
Total shareholders' equity	\$ 15,155,071	\$ 18,068,701
Total Liabilities and Shareholders' Equity	\$ 161,661,486	\$ 161,191,453

See Notes to Unaudited Consolidated Financial Statements

BANK OF MCKENNEY AND SUBSIDIARY

Consolidated Statements of Income

(unaudited)

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
Interest and Dividend Income:	2008	2007	2008	2007
Interest and fees on loans	\$ 2,057,923	\$ 2,012,825	\$ 4,182,652	\$ 4,009,332
Interest and dividends on securities - taxable	351,220	263,500	649,691	546,097
Interest on securities - nontaxable	38,917	18,346	72,781	34,143
Interest on federal funds sold	36,747	110,133	85,901	207,482
Interest on deposits with other institutions	16,533	7,301	30,275	13,106
Total interest and dividend income	<u>\$ 2,501,340</u>	<u>\$ 2,412,105</u>	<u>\$ 5,021,300</u>	<u>\$ 4,810,160</u>
Interest Expense:				
Money market and NOW accounts	\$ 66,215	\$ 41,307	\$ 118,615	\$ 84,350
Savings	17,951	19,948	35,895	39,951
Time	813,055	767,948	1,655,488	1,483,580
Federal Home Loan Bank advances	154,489	163,536	314,605	326,255
Total interest expense	<u>\$ 1,051,710</u>	<u>\$ 992,739</u>	<u>\$ 2,124,603</u>	<u>\$ 1,934,136</u>
Net interest income	\$ 1,449,630	\$ 1,419,366	\$ 2,896,697	\$ 2,876,024
Provision for loan losses	130,000	20,000	160,000	20,000
Net interest income after provision for loan losses	<u>\$ 1,319,630</u>	<u>\$ 1,399,366</u>	<u>\$ 2,736,697</u>	<u>\$ 2,856,024</u>
Noninterest income:				
Service charges on deposit accounts	\$ 216,953	\$ 218,402	\$ 421,381	\$ 408,122
Secondary market origination fees	117,482	108,303	244,873	189,199
Net gain/(loss) on sale of securities	226,666	(372)	250,472	67,735
Bank-owned Life Insurance	31,023	29,982	62,430	59,456
Other operating income	40,368	42,715	88,244	92,242
Gain on sale of other real estate owned	--	--	9,579	--
Gain on sale of fixed assets	--	47,132	--	51,649
Total noninterest income	<u>\$ 632,492</u>	<u>\$ 446,162</u>	<u>\$ 1,076,979</u>	<u>\$ 868,403</u>
Noninterest expense:				
Salaries and employee benefits	\$ 913,551	\$ 868,209	\$ 1,815,949	\$ 1,712,037
Occupancy expense	88,826	80,214	183,864	160,865
Furniture and equipment expense	117,917	106,749	229,194	210,674
Data processing	59,846	52,868	104,120	101,780
Telecommunications	36,075	27,254	69,283	54,521
Stationery and supplies	22,498	25,342	46,102	53,505
Audit and accounting fees	46,682	35,900	91,740	81,537
Corporate franchise tax	30,875	28,571	61,750	57,122
Other operating expenses	193,740	161,433	358,742	336,336
Total noninterest expense	<u>\$ 1,510,010</u>	<u>\$ 1,386,540</u>	<u>\$ 2,960,744</u>	<u>\$ 2,768,377</u>
Net income before taxes	\$ 442,112	\$ 458,988	\$ 852,932	\$ 956,050
Income taxes	122,415	136,858	239,031	285,413
Net income	<u>\$ 319,697</u>	<u>\$ 322,130</u>	<u>\$ 613,901</u>	<u>\$ 670,637</u>
Net income per common share, basic and diluted	<u>\$ 0.17</u>	<u>\$ 0.17</u>	<u>\$ 0.32</u>	<u>\$ 0.35</u>

See Notes to Unaudited Consolidated Financial Statements

BANK OF MCKENNEY AND SUBSIDIARY

Consolidated Statements of Changes in Shareholders' Equity

For the Six Months Ended June 30, 2008 and 2007

(unaudited)

	<u>Common</u> <u>Stock</u>	<u>Surplus</u>	<u>Retained</u> <u>Earnings</u>	<u>Accumulated</u> <u>Other</u> <u>Comprehensive</u> <u>Income (Loss)</u>	<u>Comprehensive</u> <u>Income</u>	<u>Total</u>
Balance at December 31, 2006	\$ 3,853,312	\$ 5,893,958	\$ 7,467,215	\$ (296,832)		\$ 16,917,653
Comprehensive income:						
Net income	-	-	670,637	-	\$ 670,637	670,637
Other comprehensive loss:						
Unrealized holding losses on securities available for sale arising during the period, net of tax benefit of \$12,898	-	-	-	-	(25,037)	-
Less reclassification adjustment, net of tax of (\$23,030)	-	-	-	-	(44,705)	-
Other comprehensive loss, net of tax				(69,742)	\$ (69,742)	(69,742)
Total comprehensive income					<u>\$ 600,895</u>	
Balance at June 30, 2007	<u>\$ 3,853,312</u>	<u>\$ 5,893,958</u>	<u>\$ 8,137,852</u>	<u>\$ (366,574)</u>		<u>\$ 17,518,548</u>
Balance at December 31, 2007	\$ 3,853,312	\$ 5,893,958	\$ 8,240,118	\$ 81,313		\$ 18,068,701
Comprehensive income:						
Net income	-	-	613,901	-	\$ 613,901	613,901
Other comprehensive income:						
Unrealized holding losses on securities available for sale arising during the period, net of tax benefit of \$134,258	-	-	-	-	(260,619)	-
Less reclassification adjustment, net of tax of (\$85,160)	-	-	-	-	(165,312)	-
Other comprehensive loss, net of tax				(425,931)	\$ (425,931)	(425,931)
Total comprehensive income					<u>\$ 187,970</u>	
Balance at June 30, 2008	<u>\$ 3,853,312</u>	<u>\$ 5,893,958</u>	<u>\$ 8,854,019</u>	<u>\$ (344,618)</u>		<u>\$ 18,256,671</u>

See Notes to Unaudited Consolidated Financial Statements

BANK OF MCKENNEY AND SUBSIDIARY

Consolidated Statements of Cash Flows

For the Six Months Ended June 30, 2008 and 2007

(unaudited)

	2008	2007
Cash Flows from Operating Activities		
Net income	\$ 613,906	\$ 670,637
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	248,529	218,494
Provision for loan losses	160,000	20,000
Capitalized interest on interest-bearing deposits in banks	(13,819)	-
Increase in cash surrender value of life insurance	(62,430)	(59,456)
Net gain on sales of securities available for sale	(250,472)	(67,735)
Net gain on sales of fixed assets	-	(51,649)
Net gain on sales of other real estate owned	(9,579)	-
Net amortization of premium on securities	(45,133)	6,113
Changes in assets and liabilities:		
(Increase) Decrease in accrued interest receivable	(121,398)	120,092
Increase in other assets	(7,805)	(74,522)
(Decrease) Increase in accrued interest payable	(33,512)	43,837
Increase in accrued expenses and other liabilities	4,076	25,869
Net cash provided by operating activities	\$ 482,363	\$ 851,680
Cash flows from Investing Activities		
Net change in interest-bearing deposits in banks	\$ (3,000,000)	\$ -
Activity in available for sale securities:		
Sales	7,227,306	4,008,580
Maturities, prepayments and calls	13,847,389	404,947
Purchases	(24,639,487)	(4,084,238)
Redemption of restricted securities (FHLB stock)	299,500	11,100
Net increase in loans	(2,740,204)	(2,835,342)
Purchase of land, premises and equipment	(247,162)	(468,208)
Proceeds from sale of fixed assets	-	220,911
Proceeds from sale of other real estate owned	144,579	-
Net cash used in investing activities	\$ (9,108,079)	\$ (2,742,250)
Cash Flows from Financing Activities		
Net increase in deposits	\$ 10,099,963	\$ 2,201,182
Dividend distributions	(520,197)	(481,664)
Repayment of long-term debt	(6,166,667)	(166,667)
Net cash provided by financing activities	\$ 3,413,099	\$ 1,552,851
Net decrease in cash and cash equivalents	\$ (5,212,617)	\$ (337,719)
Cash and Cash Equivalents		
Beginning of year	11,223,898	9,444,157
End of Year	\$ 6,011,281	\$ 9,106,438
Supplemental Disclosures of Cash Flow Information		
Cash paid during the year for:		
Interest	\$ 2,158,113	\$ 1,890,299
Income Taxes	\$ 235,600	\$ 344,091
Supplemental Disclosures of Noncash Investing and Financing Activities		
Fair value adjustment for securities	\$ (645,347)	\$ (105,669)
Capitalized interest	\$ -	\$ 1,281

See Notes to Unaudited Consolidated Financial Statements

Notes to Unaudited Consolidated Financial Statements

1. General

Bank of McKenney (the “Bank”) offers a full range of banking and financial services to individuals, professionals, and small and medium sized businesses through six full service banking offices in the counties of Dinwiddie, southern Chesterfield and Prince George and the city of Colonial Heights. The Bank is subject to competition from other financial institutions. The Bank is also subject to the regulations of the Board of Governors of the Federal Reserve System and the State Corporation Commission of Virginia, and it undergoes periodic examinations by these regulatory authorities.

McKenney Group, L.L.C. (the “Subsidiary”) is a wholly-owned subsidiary of the Bank. McKenney Group, L.L.C. was formed in December of 2000 to provide networking solutions to Virginia community banks. The Subsidiary maintains the partial ownership interests previously acquired by McKenney Title, Inc.

The accompanying consolidated financial statements of Bank of McKenney and its subsidiary collectively have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information. They do not include all of the information and notes required by accounting principles generally accepted in the United States of America for complete financial statements. Therefore, these consolidated statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Bank of McKenney Annual Report on Form 10-KSB for the year ended December 31, 2007. All significant intercompany balances and transactions have been eliminated. In the opinion of management, the accompanying consolidated financial statements contain all adjustments and reclassifications consistent of a normal and recurring nature considered necessary to present fairly the financial position as of June 30, 2008 and December 31, 2007 and the results of operations for the three and six month periods ended June 30, 2008 and 2007 and changes in shareholders’ equity and cash flows for the six months ended June 30, 2008 and 2007. Operating results for the three and six-month periods ended June 30, 2008 and 2007 are not necessarily indicative of full year financial results.

Certain prior year amounts have been reclassified to conform to the current year’s method of presentation.

2. Investment Securities

The following table sets forth a summary of the amortized cost and fair market value of investment securities available for sale at June 30, 2008 and December 31, 2007:

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized (Losses)</u>	<u>Fair Market Value</u>
June 30, 2008				
U.S. government agencies	\$ 14,134,905	\$ 38,100	\$ (176,396)	\$ 13,996,609
Mortgage-backed securities	1,302,842	-	(10,707)	1,292,135
Obligations of state and political subdivisions	4,238,263	19,647	(26,864)	4,231,046
Corporate debt securities	12,869,157	-	(365,936)	12,503,221
	<u>\$ 32,545,167</u>	<u>\$ 57,747</u>	<u>\$ (579,903)</u>	<u>\$ 32,023,011</u>
December 31, 2007				
U.S. government agencies	\$ 22,152,627	\$ 196,797	\$ (73,853)	\$ 22,275,571
Mortgage-backed securities	1,827,579	39	(2,100)	1,825,518
Obligations of state and political subdivisions	3,700,426	34,075	(2,629)	3,731,872
Corporate debt securities	1,004,127	-	(29,127)	975,000
	<u>\$ 28,684,759</u>	<u>\$ 230,911</u>	<u>\$ (107,709)</u>	<u>\$ 28,807,961</u>

The contractual maturities of investment securities classified as available for sale on June 30, 2008 are shown below. Expected maturities may differ from contractual maturities because mortgages underlying the mortgage-backed securities may be called or prepaid without any penalties.

	<u>Amortized Cost</u>	<u>Fair Market Value</u>
Available for Sale		
Maturing within one year	\$ 2,936,094	\$ 2,930,970
Maturing after one year, but within five years	16,643,671	16,531,204
Maturing after five years, but within ten years	11,662,560	11,268,702
Maturing after ten years	1,302,842	1,292,135
	<u>\$ 32,545,167</u>	<u>\$ 32,023,011</u>

There were no securities pledged to secure public deposits or for other purposes required by law at June 30, 2008. The Bank utilizes letters of credit through the Federal Home Loan Bank for meeting the collateral requirements of such deposits.

Due to certain banking relationships with the Federal Reserve Bank, the Federal Home Loan Bank and Community Bankers' Bank, the Bank has invested \$974,525 in restricted investments required by these entities. These investments are carried at cost, which approximates redemption value.

The Bank had securities in its portfolio at June 30, 2008 and December 31, 2007 that reflected an unrealized loss in value. These unrealized losses have been evaluated and are considered to be temporary impairments of the value of the issues. A summary of these securities as of June 30, 2008 and December 31, 2007 is as follows:

Description	June 30, 2008					
	Total		Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Agencies	\$ 8,895,270	\$ (176,396)	\$ 6,582,932	\$ (167,068)	\$ 2,312,338	\$ (9,328)
Mortgage backs	1,292,135	(10,707)	1,292,135	(10,707)	-	-
Corporate	12,503,221	(365,936)	11,510,721	(357,060)	992,500	(8,876)
Tax exempt municipals	<u>1,564,522</u>	<u>(26,864)</u>	<u>1,564,522</u>	<u>(26,864)</u>	-	-
Total Unrealized Loss Positions	<u>\$ 24,255,148</u>	<u>\$ (579,903)</u>	<u>\$ 20,950,310</u>	<u>\$ (561,699)</u>	<u>\$ 3,304,838</u>	<u>\$ (18,204)</u>

Description	December 31, 2007					
	Total		Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Agencies	\$ 11,476,141	\$ (73,853)	\$ -	\$ -	\$ 11,476,141	\$ (73,853)
Mortgage backs	331,578	(2,100)	-	-	331,578	(2,100)
Corporate	975,000	(29,127)	-	-	975,000	(29,127)
Tax exempt municipals	<u>701,943</u>	<u>(2,629)</u>	<u>295,743</u>	<u>(894)</u>	<u>406,200</u>	<u>(1,735)</u>
Total Unrealized Loss Positions	<u>\$ 13,484,662</u>	<u>\$ (107,709)</u>	<u>\$ 295,743</u>	<u>\$ (894)</u>	<u>\$ 13,188,919</u>	<u>\$ (106,815)</u>

Management evaluates securities for other-than-temporary impairments at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

The securities identified above for June 30, 2008 with unrealized losses consist of one governmental mortgage pool issue, ten corporate issues, six government agency issues, and six issues of a municipality. One of the corporate credits, Ford Motor Credits, was previously downgraded to sub-investment grade; however, with the issuance being through the corporation's financing arm and the maturity being less than one year, no loss is expected at this time. The other unrealized losses reflect changes in the current interest rate environment as well as the issues' maturities. No principal is expected to be lost, and the unrealized losses, primarily due to interest rates, are considered temporary in nature.

3. Allowance for Loan Losses

The following represents an analysis of changes in the allowance for loan losses for the six months ended June 30, 2008 and 2007:

	June 30,	
	2008	2007
Balance, beginning of period	\$ 925,000	\$ 1,070,000
Provision for loan losses	160,000	20,000
Charge-offs	(152,570)	(221,072)
Recoveries of loans previously charged off	24,095	10,500
Balance, end of period	<u>\$ 956,525</u>	<u>\$ 879,428</u>
Allowance for loan losses to total loans	<u>0.88%</u>	<u>0.84%</u>

4. Earnings Per Share

As the Bank does not currently offer stock options, there was no effect on income available to common shareholders. The following shows the weighted average number of shares used in computing earnings per share.

	Six Months Ended June 30,			
	2008		2007	
	Shares	Per Share	Shares	Per Share
Basic & Diluted earnings per share	<u>1,926,656</u>	<u>\$ 0.32</u>	<u>1,926,656</u>	<u>\$ 0.35</u>

5. Fair Value Measurements

SFAS No. 157, *Fair Value Measurements*, defines fair value, establishes a framework for measuring fair value, establishes a three-level valuation hierarchy for disclosure of fair value measurement and enhances disclosure requirements for fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follow:

- ❖ *Level 1* - inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- ❖ *Level 2* - inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- ❖ *Level 3* - inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Following is a description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy:

Securities: Where quoted prices are available in an active market, securities are classified within level 1 of the valuation hierarchy. Level 1 securities would include highly liquid government bonds, mortgage products and exchange traded equities. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics, or discounted cash flow. Level 2 securities would include U.S. agency securities, mortgage-backed agency securities, obligations of states and political subdivisions and certain corporate, asset backed and other securities. In certain cases where there is limited activity or less transparency around inputs to the valuation, securities are classified within level 3 of the valuation hierarchy. Currently, all of the Company's securities are considered to be Level 2 securities.

Loans held for sale: At June 30, 2008, there were no loans held for sale.

Impaired loans: SFAS No. 157 applies to loans measured for impairment using the practical expedients permitted by SFAS No. 114, *Accounting by Creditors for Impairment of a Loan*, including impaired loans measured at an observable market price (if available), or at the fair value of the loan's collateral (if the loan is collateral dependent). Fair value of the loan's collateral, when the loan is dependent on collateral, is determined by appraisals or independent valuation which is then adjusted for the cost related to liquidation of the collateral.

Other Real Estate Owned: Certain assets such as other real estate owned (OREO) are measured at fair value less cost to sell. We believe that the fair value component in its valuation follows the provisions of SFAS No. 157.

Item 2. Management's Discussion and Analysis or Plan of Operation

The following discussion is intended to assist readers in understanding and evaluating the Bank's financial condition and results of operations. In conjunction with reviewing the following discussion, you should also read and review the unaudited June 2008 and 2007 financial statements and accompanying notes presented previously in this document. This analysis provides an overview of the significant changes that occurred during the periods presented.

This report may contain, in addition to historical information, various "forward looking statements" that represent our judgment concerning the future and are subject to risks and uncertainties that could cause our actual operating results and financial position to differ materially from those projected in the forward looking statements. These forward looking statements can be identified by the use of forward looking terminology, such as "may," "will," "expect," "anticipate," "estimate" or "continue" or comparable words. We caution that any such forward looking statements are further qualified by important factors that could cause our actual operating results and financial position to differ materially from the forward looking statements, including, without limitation, considerations described in connection with specific forward looking statements and other cautionary statements set forth in this report.

Critical Accounting Policies

The Bank's financial statements are prepared in accordance with accounting principles generally accepted in the United States ("GAAP"). The financial information contained within our statements is, to a significant extent, financial information that is based on measures of the financial effects of transactions and events that have already occurred. A variety of factors could affect the ultimate value that is obtained either when earning income, recognizing an expense, recovering an asset or relieving a liability. We use historical loss factors as one factor in determining the inherent loss that may be present in our loan portfolio. Actual losses could differ significantly from the historical factors that we use. In addition, GAAP itself may change from one previously acceptable method to another method. Although the economics of our transactions would be the same, the timing of events that would impact our transactions could change.

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependant.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank normally does not separately identify such loans for impairment disclosures.

In preparing consolidated financial statements in conformity with GAAP, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses.

Comparison of Financial Condition at June 30, 2008 and December 31, 2007

At the end of the second quarter, total assets were \$164.8 million, representing a \$3.6 million or 2.23% increase over the December 31, 2007 level of \$161.2 million. Total deposits amounted to \$137.6 million as of June 30, 2008, which represents a \$10.1 million or 7.92% increase from the \$127.5 million level as of December 31, 2007. On an annualized basis, deposits grew during the first two quarters at a rate of 15.84%. During the same period, total loans expanded by 2.15% or \$2.3 million to the June 30, 2008 balance of \$109.3 million. At June 30, 2008, the investment portfolio, including time deposits in other banks, was \$36.0 million, a 19.60% increase in comparison to the December 31, 2007 \$30.1 million level. Overnight federal funds sold decreased 89.47% from \$7.6 million on December 31, 2007 to \$0.8 million on June 30, 2008 as the Bank elected to retire certain Federal Home Loan Bank borrowings and reduce the overall cost of funds. Cumulatively, earning assets grew \$1.4 million for the first half of 2008 or 0.97% on an annualized basis and represent 88.65% of total assets.

The allowance for loan losses was \$957,000 as of June 30, 2008, or 0.88% of loans outstanding, compared to \$925,000 as of December 31, 2007 or 0.86% of outstanding loans. Charges to the Reserve account for loan losses amounted to \$152,000 as of June 30, 2008 or 0.12% of average outstanding loans for 2008. For the first six months of 2007, charges to the reserve of \$221,000 were taken representing 0.20% of average loans outstanding for the period. Allocations to the reserve account of \$160,000 were provisioned for the first six months of 2008 compared to provision allocations of \$20,000 for the same period of 2007.

The Bank works diligently to maintain quality in its loan portfolio and has historically maintained an average delinquency ratio well below 1%. Loans past due more than thirty days (excluding impaired and nonaccrual loans) measured \$703,000 or 0.64% of total loans at June 30, 2008 as compared to December 31, 2007 delinquencies of \$364,000, or 0.34% of total loans. Non-performing assets consist of impaired loans, non-accrual loans and real estate owned by the Bank resulting from a foreclosure proceeding. Normally, loans are placed on non-accrual when a loan is specifically determined to be impaired or when principal or interest is delinquent in excess of 90 days. On June 30, 2008, non-performing assets stood at \$1.3 million or 1.21% of quarter-end loans. This compared to non-performing assets of \$1.0 million, or 0.94%, of total loans outstanding for December 31, 2007.

Comparison of Results of Operations for the Six Months Ended June 30, 2008 and 2007

For the six-month period ended June 30, 2008, the Bank reported earnings of \$614,000, a decrease of 8.49% when compared to \$671,000 through the first six months of 2007. For the first two quarters of 2008 and 2007, earnings per basic and diluted share of \$0.32 and \$0.35, respectively, were recorded. Annualized returns on average assets and average equity for the first six months of 2008 were 0.74% and 6.63%, respectively, compared to 0.88% and 7.80%, respectively, for the same period in 2007. Margins have remained under pressure as a result of drastic rate reductions by the Federal Reserve over the past nine months. The cost of funds for deposits is dropping as this segment cycles through rate resets and improvement is anticipated over the second half of the year.

Net interest income. For the first six months of 2008, net interest income increased to \$2,897,000 from \$2,876,000 in the comparable period in 2007. Average loans through the second quarter of 2008, when compared to the same period in 2007, grew to \$109.0 million from \$102.7 million, an increase of 6.13%. The average investment portfolio climbed from a 2007 first half average balance of \$27.0 million to a \$31.8 million average through the second quarter of 2008, or an increase of 17.78%. Average deposit growth has increased 11.92% or \$11.6 million to \$108.9 million over the same prior year period's average of \$97.3 million. The Bank's prime based loan portfolio yields decreased 16 basis points when comparing the first half of 2008 to that period in 2007 while the investment portfolio in the same periods gained 29 basis points. Cumulatively, yields on earning assets decreased 27 basis points from a 2007 first-half average of 7.07% to an average of 6.80% for the current year's first half. Volume growth in the bank's interest bearing deposit products coupled with the negative short-term effects resulting from the recent and rapid monetary policy changes have pressured the net interest margin downward by 30 basis points to 3.94%. This growth in liquidity prompted a \$6.0 million or 44.44% reduction in Federal Home Loan Bank borrowings later in the second quarter. These once extremely attractive rates had begun adversely affecting margins due to the aforementioned rate cuts, and this move should help boost margins going forward. Moreover, the shorter-lived deposit rate cycle has now begun re-pricing at substantially lower rates and will quickly result in added margin support through a much lower cost of funds.

Noninterest income. Noninterest income, exclusive of securities transactions, rose 3.25% or \$26,000 to \$827,000 when compared to \$801,000 for the same period in 2007. Service charges posted higher results with a \$13,000 or 3.19% increase when comparing the first half of 2008 to that of 2007. In comparing these same two periods, the mortgage originations department climbed \$56,000 or 29.63%. Other noninterest income decreased by \$43,000 from the \$203,000 level recorded in the first half 2007; however, the prior year's level included gains of \$52,000 posted from the sale of a former branch office after its consolidation with newer offices nearby.

Noninterest expense. Noninterest expense increased \$193,000 or 6.97% to \$2,961,000 during the first two quarters of 2008 from \$2,768,000 for the same period in 2007. Separately within this category, salaries and benefits rose 6.07% or \$104,000 while occupancy and furniture & equipment expenses increased \$41,000 or 11.02%. Other operating expenses through June 30, 2008 grew \$47,000 or 6.86% to a level of \$732,000.

Provision for loan losses. Provisions for loan losses amounted to \$160,000 through June 30, 2008 as growth and charges taken in 2008 to the reserve permitted additional provisions being made. During the same period in 2007, \$20,000 was allocated in provisions to the reserve for loan losses.

Comparison of Results of Operations for the Three Months Ended June 30, 2008 and 2007

For the three-month period ending June 30, 2008, net income amounted to \$320,000, a slight decrease of 0.62% compared to net income of \$322,000 for the same period in 2007. Basic and diluted earnings per share of \$0.17 were reported for the three months ended June 30, 2008, equaling those of the prior year's results for the same period. During both periods there were 1,926,656 weighted average shares outstanding.

Net interest income. Net interest income increased to \$1,450,000 in the second quarter of 2008 from \$1,419,000 in the comparable period in 2007. Volume growth in the bank's interest bearing deposit products coupled with the negative short-term effects resulting from the recent and rapid monetary policy changes have added downward pressure on the net interest margin; however, the cost of funds for deposits is dropping as this segment cycles through rate resets and improvement is anticipated over the second half of the year.

Noninterest income. Noninterest income, exclusive of securities transactions, declined 9.17% or \$41,000 in the second quarter of 2008 to \$405,000 when compared to \$447,000 for the same period in 2007. Service charges posted slightly lower results with a \$1,000 or 0.46% decline when comparing the second quarter of 2008 to the second quarter of 2007. Lower mortgage rates in the second quarter moderately enticed the appetite of borrowers as the mortgage originations department experienced a \$9,000 or 8.33% gain in the category for the second quarter of 2008 when compared to the same period of 2007. Other noninterest products and services, including those of the insurance and investment departments, decreased by \$49,000 from \$120,000 level recorded in the second quarter of 2007 to a second quarter 2008 balance of \$71,000.

Noninterest expense. Noninterest expense increased \$123,000 or 8.87% to \$1,510,000 during the second quarter 2008 from \$1,387,000 for the same period in 2007. Salaries and benefits rose 5.18% or \$45,000 while occupancy and furniture & equipment expenses increased \$20,000 or 10.70%. Other operating expenses for the second quarter of 2008 grew \$58,000 or 17.52% to level of \$390,000.

Provision for loan losses. Provision for loan losses increased from \$20,000 in the second quarter of 2007 to \$130,000 in the same period in 2008. This increase is reflective of the prevailing economic state, charges taken during the second quarter, and assessment of the loan portfolio.

The following table illustrates average balances of total interest earning assets and total interest bearing liabilities for the periods indicated, showing the average distribution of assets, liabilities, shareholders' equity and related income, expense and corresponding weighted average yields and rates. The average balances used in these tables and other statistical data were calculated using daily average balances.

Average Balances, Interest Income and Expense and Average Yields and Rates

	Period Ended June 30,					
	2008			2007		
	Average Balance	Income / Expense	Yield / ⁽⁴⁾ Rate	Average Balance	Income / Expense	Yield / ⁽⁴⁾ Rate
(Dollars in Thousands)						
Assets:						
Interest earning assets:						
Investment securities ⁽¹⁾	\$ 31,819	\$ 750	4.71%	\$ 27,018	\$ 598	4.42%
Interest-bearing balances with banks	1,298	22	3.41%	-	-	0.00%
Loans	109,012	4,182	7.71%	102,721	4,009	7.87%
Federal funds sold	7,087	94	2.67%	8,057	221	5.53%
Total interest earning assets	<u>149,216</u>	<u>5,048</u>	<u>6.80%</u>	<u>137,796</u>	<u>4,828</u>	<u>7.07%</u>
Non-interest earning assets:						
Cash and due from banks	4,756			4,442		
Premises and equipment	8,310			6,874		
Other assets	5,631			5,503		
Less: Allowance for loan losses	<u>(961)</u>			<u>(1,000)</u>		
	<u>17,736</u>			<u>15,819</u>		
	<u>\$166,952</u>			<u>\$153,615</u>		
Liabilities and Stockholders' Equity						
Interest bearing liabilities:						
Interest-bearing demand deposits	\$ 13,201	\$ 73	1.11%	\$ 10,035	\$ 20	0.40%
Money market deposit accounts	6,725	46	1.38%	7,086	64	1.82%
Savings accounts	12,055	36	0.60%	13,442	40	0.60%
Time deposits	76,968	1,654	4.32%	66,777	1,484	4.48%
Total interest-bearing deposits	<u>108,949</u>	<u>1,809</u>	<u>3.34%</u>	<u>97,340</u>	<u>1,608</u>	<u>3.33%</u>
Securities sold under repurchase agreeme	-	-	0.00%	-	-	0.00%
Other borrowings	-	0	0.00%	-	-	0.00%
Total interest-bearing liabilities	<u>122,344</u>	<u>2,124</u>	<u>3.49%</u>	<u>111,265</u>	<u>1,934</u>	<u>3.51%</u>
Non-interest bearing liabilities:						
Demand deposits	24,421			23,662		
Other liabilities	1,586			1,334		
Total liabilities	<u>148,351</u>			<u>136,261</u>		
Shareholders' Equity	<u>18,601</u>			<u>17,354</u>		
Total Liabilities & Shareholders' Equity	<u>\$166,952</u>			<u>\$153,615</u>		
Interest Spread ⁽²⁾			3.31%			3.56%
Net Interest Margin ⁽³⁾		<u>\$ 2,924</u>	3.94%		<u>\$ 2,894</u>	4.24%

⁽¹⁾ Income and yields are reported on tax equivalent basis assuming a federal tax rate of 34%.

⁽²⁾ Interest Spread is the average yield earned on earning assets, less the average rate incurred on interest bearing liabilities.

⁽³⁾ Net interest margin is net interest income, expressed as a percentage of average earning assets.

⁽⁴⁾ Yields and rates are annualized.

Liquidity and Capital

The liquidity ratio at June 30, 2008 dipped to 28.96% compared to 29.26% reported as of December 31, 2007. The overall Asset/Liability strategy of the organization takes into account the need for the Bank to maintain adequate liquidity to fund asset growth and deposit runoff. The management of the Bank monitors the liquidity position daily in conjunction with the Federal Reserve position monitoring. The Bank has credit lines both secured and unsecured available from several correspondent banks. Additionally, the Bank may borrow funds from the Federal Home Loan Bank of Atlanta. The credit facilities are used in conjunction with the normal deposit strategies, which include pricing changes to increase deposits as necessary. The organization can sell or pledge investment securities to create additional liquidity for the Bank. From time to time the organization may sell or participate out loans to create additional liquidity as required.

The Bank's capital ratios exceed regulatory requirements. The following table presents these ratios for the periods ending June 30, 2008 and December 31, 2007:

Risk Based Capital Analysis			
	June 30, 2008	December 31, 2007	
(Dollars in Thousands)			
Tier 1 Capital:			
Common stock	\$ 3,853	\$ 3,853	
Capital surplus	5,894	5,894	
Retained earnings	8,510	8,321	
Reverse: Unrealized (Gains)/Losses	344	(81)	
Total tier 1 capital	<u>18,601</u>	<u>17,987</u>	
Tier 2 Capital:			
Allowance for loan losses	<u>957</u>	<u>925</u>	
Tier 3 Capital:			
Deductions for investments in banking and finance subsidiaries	<u>(140)</u>	<u>(140)</u>	
Total Risk Based Capital	<u>\$ 19,418</u>	<u>\$ 18,772</u>	
Risk weighted assets	<u>\$ 127,708</u>	<u>\$ 115,914</u>	
Quarterly average assets	<u>\$ 169,704</u>	<u>\$ 158,577</u>	
Capital Ratios:	June 30, 2008	December 31, 2007	Regulatory Minimum
Tier 1 risk based capital ratio	14.57%	15.52%	4.00%
Total risk based capital ratio	15.20%	16.19%	8.00%
Leverage ratio	10.96%	11.34%	4.00%

Recent Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 141(R), “Business Combinations” (SFAS 141(R)). The Standard will significantly change the financial accounting and reporting of business combination transactions. SFAS 141(R) establishes the criteria for how an acquiring entity in a business combination recognizes the assets acquired and liabilities assumed in the transaction; establishes the acquisition date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose to investors and other users all of the information they need to evaluate and understand the nature and financial effect of the business combination. Acquisition related costs including finder's fees, advisory, legal, accounting valuation and other professional and consulting fees are required to be expensed as incurred. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008 and early implementation is not permitted. The Bank does not expect the implementation to have a material impact on its consolidated financial statements.

In December 2007, the FASB issued Statement of Financial Accounting Standards No.160, “Noncontrolling Interests in Consolidated Financial Statements” (SFAS 160). SFAS 160 requires the Bank to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. This Statement is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. The Bank does not expect the implementation of SFAS 160 to have a material impact on its consolidated financial statements.

In March 2008, the FASB issued Statement of Financial Accounting Standards No. No. 161, “Disclosures about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133” (SFAS 161). SFAS 161 changes the disclosure requirements for derivative instruments and hedging activities. Entities are required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity’s financial position, financial performance and cash flows. SFAS 161 is effective for fiscal years and interim periods beginning after November 15, 2008, with early application permitted. The Bank does not expect the implementation of SFAS 161 to have a material impact on its consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Not Required for Small Reporting Companies

Item 4. Controls and Procedures

Disclosure Controls and Procedures

The Bank’s management, with the participation of the Bank’s Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Bank’s disclosure controls and procedures as of the end of the period covered by this report. Based on such evaluation, the Bank’s Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Bank’s disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Bank in the reports that it files or furnishes under the Securities Exchange Act of 1934.

Management reviews and evaluates the design and effectiveness of the Bank’s disclosure controls and procedures on an ongoing basis, which may result in the discovery of deficiencies, and improves its controls and procedures over time, correcting any deficiencies, as needed, that may have been discovered.

Changes in Internal Control Over Financial Reporting

Management reviews and evaluates the design and effectiveness of the Bank's internal control over financial reporting on an ongoing basis, which may result in the discovery of deficiencies, some of which may be significant. Management changes its internal control over financial reporting as needed to maintain its effectiveness, correcting any deficiencies, as needed, in order to ensure the continued effectiveness of the Bank's internal control over financial reporting. There have not been any changes in the Bank's internal control over financial reporting during the second quarter of 2008 that have materially affected, or are reasonably likely to materially affect, the Bank's internal control over financial reporting.

For management's assessment of the Bank's internal control over financial reporting, refer to the Bank's 2007 Annual Report on Form 10-KSB, "Management's Report on Internal Control over Financial Reporting."

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

None

Item 2. Unregistered Sales of Equity Securities or Use of Proceeds

None

Item 3. Defaults Upon Senior Securities

Not applicable

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

At an annual meeting of the shareholders of Bank of McKenney which was properly convened at 3:00 p.m. on May 13, 2008 in the boardroom of the corporate headquarters, the following two matters, and results thereto, were submitted to a vote:

1. The election of the following Directors to serve for one year and until their successors have been duly elected, have qualified, and have taken office:

	<i>For</i>	<i>Against</i>	<i>Withheld</i>
W. D. Allen III	1,520,323	0	7,614
Harry D. Baird III	1,490,793	0	37,144
Lewis J. Blaha, Jr.	1,517,548	0	10,389
Joan D. Clarke	1,517,948	0	9,989
L. M. Harrison, Jr.	1,520,323	0	7,614
Rudy L. Hawkins	1,517,748	0	10,189
Richard M. Liles	1,520,323	0	7,614
Joseph W. Lyle	1,519,323	0	8,614
Edward B. Titmus	1,520,323	0	7,614

2. The ratification of "Yount, Hyde, & Barbour, P.C." as the accounting firm to perform Bank of McKenney's independent audit for the year ending December 31, 2008.

<i>For</i>	<i>Against</i>	<i>Abstain</i>
1,523,267	1,337	3,333

Item 5. Other Information

(a) Required 8-K Disclosures

None

(b) Changes in Procedures for Director Nominations by Security Holders

None

Item 6. Exhibits

The following exhibits are filed as part of this Form 10-Q and this list includes the Exhibit Index:

<u>Exhibit Number</u>	<u>Description</u>	<u>Page</u>
3.1	Articles of Incorporation of Bank of McKenney	*
3.2	Amended and Restated Bylaws of Bank of McKenney	**
10.1	Employment Agreement, dated December 8, 1992, by and between Bank of McKenney and Richard M. Liles	*
10.2	Split-Dollar Life Insurance Agreement (as amended), dated February 1, 1989, by and between Bank of McKenney and Richard M. Liles	*
10.3	Deferred Compensation Agreement, dated February 1, 1989, between Bank of McKenney and Richard M. Liles	*
10.4	Deferred Compensation Agreement, dated February 1, 1993, between Bank of McKenney and Richard M. Liles	*
10.5	Form of Change in Control Employment Agreement between Bank of McKenney and each of the following officers: James B. Neville, Jr., Ruth M. Wray, Lynda P. Cunningham, and Mark H. Stevens	***
21.1	Subsidiary - McKenney Group, LLC (a Virginia corporation)	*
31.1	CEO Section 302 Certification	†
31.2	CFO Section 302 Certification	†
32	Section 906 Certification	†

* Incorporated herein by reference from the Bank's Registration Statement on Form 10-SB, filed with the Board of Governors of the Federal Reserve System on September 9, 2002.

** Incorporated herein by reference from the Bank's report on Form 8-K filed with the Board of Governors of the Federal Reserve System on August 15, 2007.

*** Incorporated herein by reference from the Bank's Annual Report on Form 10-KSB for the year ended December 31, 2004, filed with the Board of Governors of the Federal Reserve System on March 8, 2005.

† Filed herewith.

SIGNATURES

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

BANK OF MCKENNEY

Date: August 11, 2008

Richard M. Liles
President and Chief Executive Officer

Date: August 11, 2008

James B. Neville, Jr.
Executive Vice President and Chief Financial Officer

SECTION 302 CERTIFICATION

I, Richard M. Liles, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Bank of McKenney;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit any material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer of, and for, the periods presented in this report;
4. The small business issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:
 - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and
5. The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: August 11th, 2008

Richard M. Liles
President and Chief Executive Officer

SECTION 302 CERTIFICATION

I, James B. Neville, Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Bank of McKenney;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit any material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer of, and for, the periods presented in this report;
4. The small business issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:
 - (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and
5. The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: August 11th, 2008

James B. Neville, Jr.
Executive Vice President and Chief Financial Officer

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Bank of McKenney (the “Bank”) on Form 10-Q for the period ending June 30, 2008 as filed with the Board of Governors of the Federal Reserve System on the date hereof (the “Report”), the undersigned Chief Executive Officer and Chief Financial officer of the Bank hereby certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002 that based on their knowledge and belief: 1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and 2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank as of and for the periods covered in the Report.

Richard M. Liles
President and Chief Executive Officer

James B. Neville, Jr.
Executive Vice President and Chief Financial Officer

Dated: August 11th, 2008