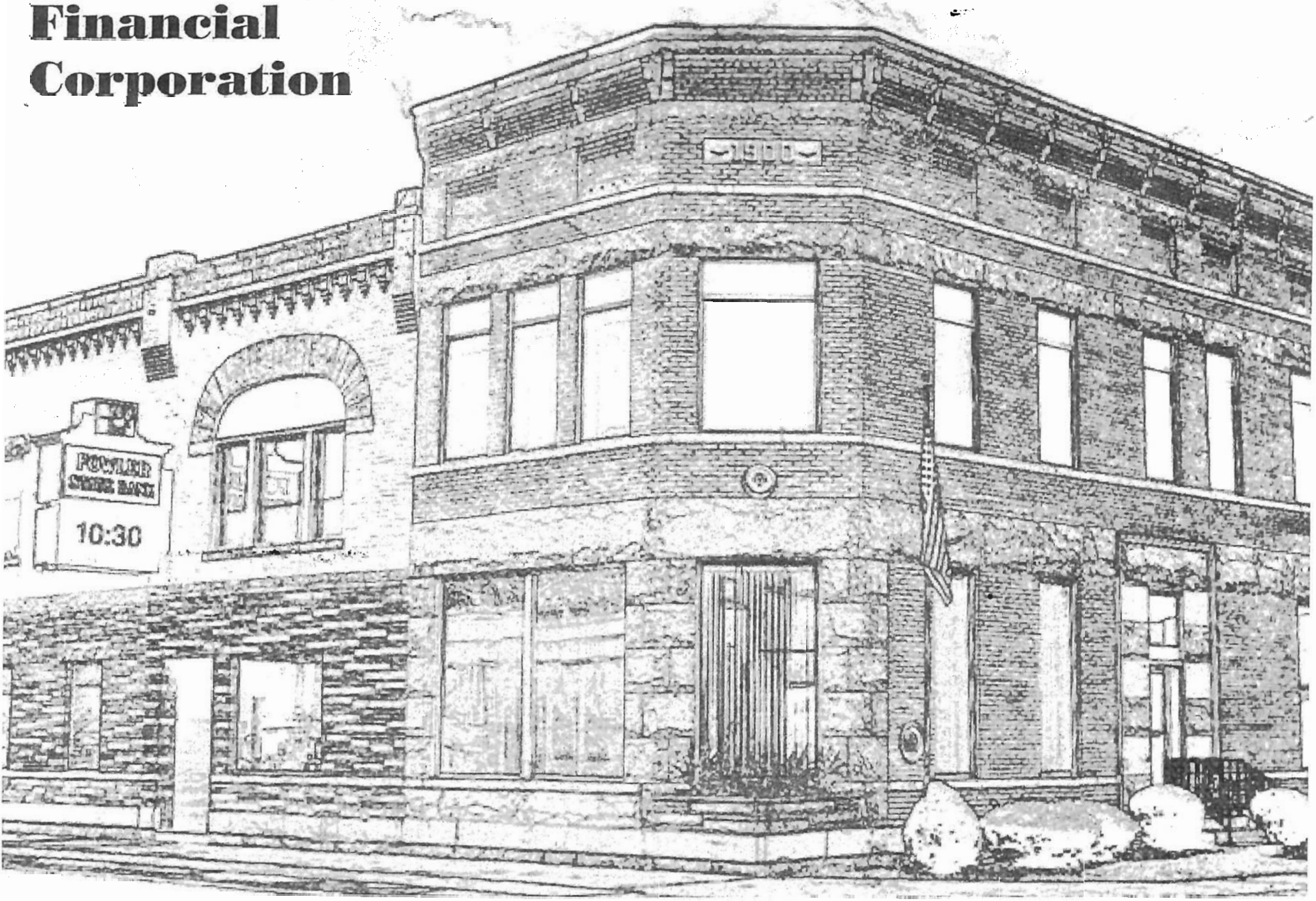
Benton Financial Corporation

Annual Report 2011



Report to Stockholders

Dear Fellow Shareholders:

2011 was an excellent year for Fowler State Bank and Benton Financial Corporation. Basic earnings per share increased 265% to $2.10 per share. Return on average assets was a very respectable 1.20%. Book value improved 16% to close the year at $23.57 per share. The Bank maintained an adequate reserve for loan loss of 2.5% of total loans while decreasing non-performing assets.

The Bank continued to increase Equity Capital throughout 2011 to remain significantly above the "Well Capitalized" ratio as defined by the FDIC. Return on equity capital was 10.02%. As a result of the aforementioned earnings and improved balance sheet, we were able to increase the cash dividend paid to our Stockholders.

Fowler State Bank celebrated its 80th Anniversary on December 14, 2011. The successful longevity of this institution is a distinct honor to its past and present employees, directors, stockholders and customers who have supported Fowler State Bank.

The recessionary years required a concentrated focus on the present. With the improving conditions of the Bank and economy, we look forward to turning our focus to the future.

On December 31, 2011, William B. Weist retired as Director from both Fowler State Bank and Benton Financial Corporation. We will miss the exemplary dedication and counsel Mr. Weist provided the past 26 years.

On January 1, 2012, Rick J. Mickle joined the Board of Directors of Fowler State Bank and Benton Financial Corporation. Mr. Mickle is serving as Vice President, Controller and Investment Officer of Fowler State Bank. Rick and his wife Kristi, and children Ariel and Seth, are lifelong resident of Benton County.

While a strong and transparent financial system is vital to this country, increasing regulatory requirements continue to apply significant pressure on earnings. Our staff strives to be a solid financial partner our customers can trust.

The Fowler State Bank Directors, Officers and Staff appreciate the support and understanding of our Stockholders during the past years. We maintain a goal of providing safe, respectable returns while supporting the communities that give us this opportunity.

Sincerely,

Steven T. Pettet
President & CEO

FINANCIAL HIGHLIGHTS

	2011	2010	2009
PER SHARE			
Basic earnings	**$2.10**	**$0.79**	$1.23
Cash dividends	**.70**	**.68**	.68
Book value	**23.57**	**20.33**	20.73
PERFORMANCE RATIOS			
Return on average equity capital	**10.02%**	**3.80%**	5.93%
Return on average assets	**1.20%**	**.44%**	.72%
EARNINGS			
Net interest income	**$5,541,353**	**$5,107,894**	$5,066,906
Provision for loan losses	**257,000**	**1,499,000**	1,420,000
Net income	**1,606,375**	**602,836**	947,266
Cash dividends	**534,420**	**519,150**	520,949
BALANCE SHEET AVERAGES			
Total assets	**$134,077,383**	**$136,938,683**	$131,820,001
Loans (net)	**67,527,381**	**65,414,847**	66,396,119
Noninterest bearing balances	**14,963,179**	**12,717,443**	10,944,864
Interest bearing balances	**80,043,541**	**85,857,937**	78,860,910
Total deposits	**95,006,720**	**98,575,380**	89,805,774
Equity capital (net of unrealized gains)	**16,028,109**	**15,858,969**	15,979,260
OTHER			
Weighted average shares outstanding	**763,550**	**763,455**	**770,934**

FIVE YEAR RECORD

	Net Income		Dividend		Capital	
Year	Amount	Earnings Per Share(1)(3)	Amount	Per Share(3)	Amount	Per Share(2)(3)
2007	$ 983,772	$1.18	$540,552	$0.65	$16,138,701	$ 19.41
2008	$ 860,435	$1.06	$531,133	$0.675	$15,091,006	$ 19.51
2009	$ 947,266	$1.23	$520,949	$0.68	$15,825,158	$ 20.73
2010	$ 602,836	$0.79	$519,150	$0.68	$15,521,533	$ 20.33
2011	$1,606,375	$2.10	$534,420	$0.70	$18,043,443	$ 23.57

(1) Based on average shares outstanding.
(2) Based on year-end outstanding shares.
(3) Adjusted for the 2 for 1 stock split.

PLEASE NOTE:

The financial statements in this Annual Report are not a replacement for the Audited Financial Statements of the Company. The Audited Financial Statements contain much more detail. Audited Financial Statements are available upon request from the Company; simply call (800) 439-3951 or visit the Bank's webpage at www.fowlerstatebank.com

If you have questions about the Audited Financials, please feel free to contact Steven T. Pettet, President & CEO or Steven K. Brunton, Executive Vice President & CFO at (765)884-1200 or (800) 439-3951.

Balance Sheet Summary
December 31, 2011, 2010 and 2009

Assets

	2011	2010	2009
Cash and equivalents	$ 5,258,393	$ 7,457,163	$ 6,134,638
Investments	54,824,197	59,035,984	53,670,874
Loans, net of allowance for loan losses of $1,821,129 and $1,711,546 and $1,153,544	69,289,601	66,071,454	65,793,148
Premises and equipment	632,657	656,271	655,202
Other assets	2,500,886	2,625,598	2,988,420
Total assets	$ 132,505,734	$ 135,846,470	$ 129,242,282

Liabilities and Stockholders' Equity

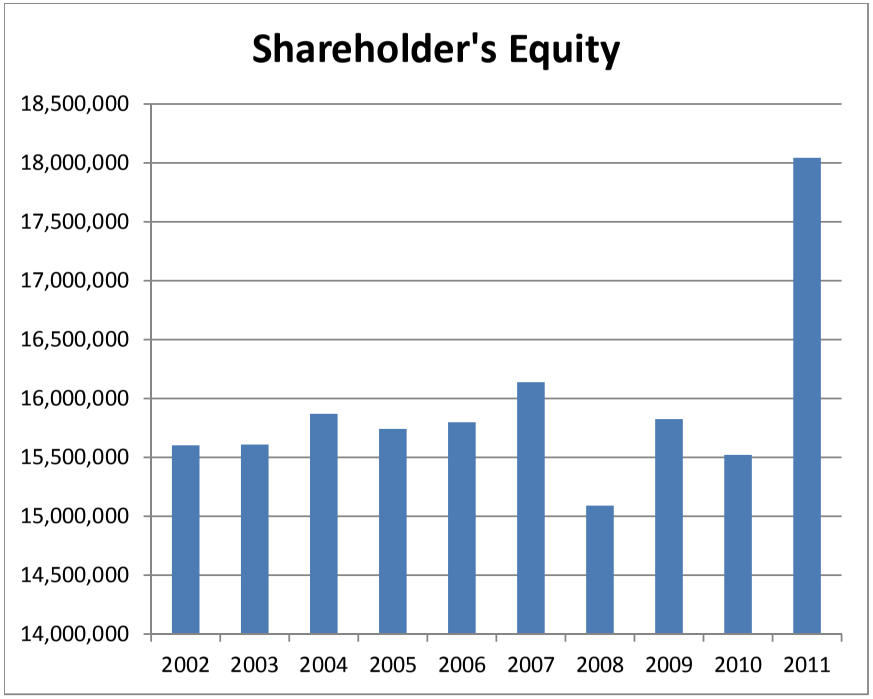
Total deposits	$ 91,186,073	$ 97,827,710	$ 86,766,196
Borrowings	22,500,000	21,500,000	26,200,000
Interest payable	99,621	139,244	144,471
Other liabilities	676,597	857,983	306,457
Total liabilities	114,462,291	120,324,937	113,417,124
Preferred stock, no par value	-	-	-
Common stock, no par value	1,975,708	1,968,661	1,968,661
Capital surplus	1,253,342	1,203,834	1,203,834
Retained earnings	13,399,650	12,327,695	12,244,009
Accumulated other comprehensive income	1,414,743	21,343	408,654
Total stockholders' equity	18,043,443	15,521,533	15,825,158
Total liabilities and stockholders' equity	$ 132,505,734	$ 135,846,470	$ 129,242,282

Income Statement Summary
Years Ended December 31, 2011, 2010 and 2009

	2011	2010	2009
Interest Income			
Cash and equivalents	$ 10,548	$ 31,765	$ 9,343
Loans receivable	4,488,995	4,433,665	4,483,529
Investment securities	2,356,502	2,295,512	2,631,102
Total interest income	6,856,045	6,760,942	7,123,974
Interest Expense			
Deposits	533,015	763,732	983,645
Borrowings	781,677	889,316	1,073,423
Total interest expense	1,314,692	1,653,048	2,057,068
Net Interest Income	5,541,353	5,107,894	5,066,906
Provision for loan loss	257,000	1,499,000	1,420,000
Net Interest Income After Provision for Loss	5,284,353	3,608,894	3,646,906
Other Income			
Service charges	369,613	399,283	423,620
Gains (losses) on securities	377,965	306,769	855,173
Other income	218,125	233,337	214,015
Total other income	965,703	939,389	1,492,808
Other Expenses			
Salaries and employee benefits	2,253,842	2,028,447	2,047,846
Premises, equipment and operating	631,095	609,567	600,875
Other expenses	1,059,563	1,117,056	1,232,865
Total other expenses	3,944,500	3,755,070	3,881,586
Income Before Income Tax	2,305,556	793,213	1,258,128
Income tax expense	699,181	190,377	310,862
Net Income	$ 1,606,375	$ 602,836	$ 947,266

Statement of Equity Summary
Years Ended December 31, 2011, 2010 and 2009

	Common Stock				Other Comprehensive	
	Shares Outstanding	Amount	Capital Surplus	Retained Earnings	Income (Loss)	Total
Balance, January 1, 2009	773,455	$ 2,002,302	$ 1,224,401	$ 12,025,484	$ (161,181)	$ 15,091,006
Net income				947,266		947,266
Change in unrealized gains on securities,					569,835	569,835
Cash dividends ($0.68 per share)				(520,949)		(520,949)
Purchase of stock	(10,000)	(33,641)	(20,567)	(207,792)		(262,000)
Balance, January 1, 2010	763,455	$ 1,968,661	$ 1,203,834	$ 12,244,009	$ 408,654	$ 15,825,158
Net income				602,836		602,836
Change in unrealized gains on securities,					(387,311)	(387,311)
Cash dividends ($0.68 per share)				(519,150)		(519,150)
Balance, January 1, 2011	763,455	1,968,661	1,203,834	12,327,695	21,343	15,521,533
Net income				1,606,375		1,606,375
Change in unrealized gains on securities,					1,393,400	1,393,400
Cash dividends ($0.70 per share)				(534,420)		(534,420)
Issuance of Stock	2,038	7,047	49,508			56,555
Balance, December 31, 2011	765,493	$ 1,975,708	$ 1,253,342	$ 13,399,650	$ 1,414,743	$ 18,043,443


Shareholder's Equity
18,500,000
18,000,000
17,500,000
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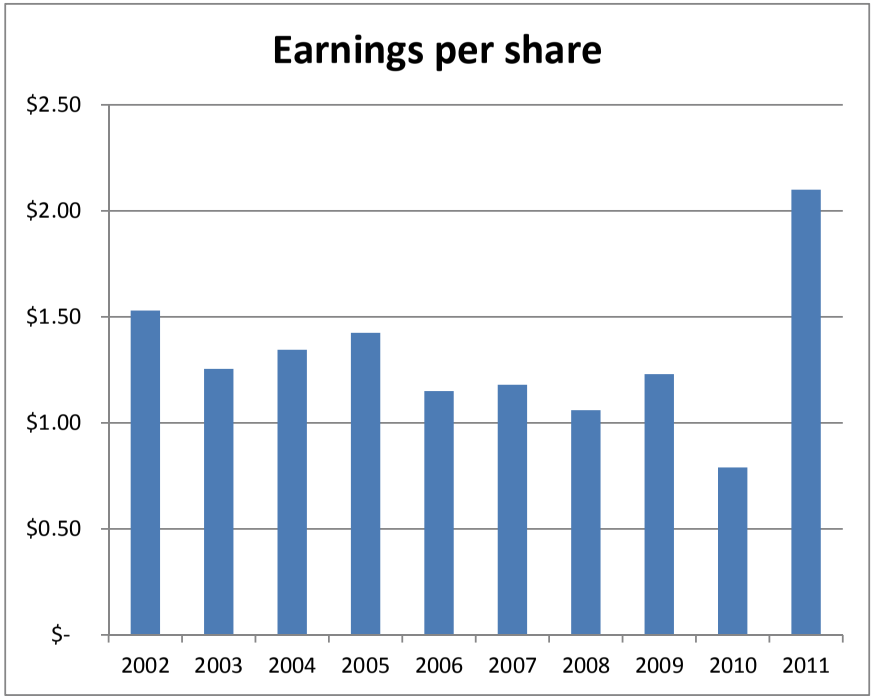
14,000,000
2002 2003 2004 2005 2006 2007 2008 2009 2010 2011


Earnings per share
$2.50
$2.00
$1.50
$1.00
$0.50
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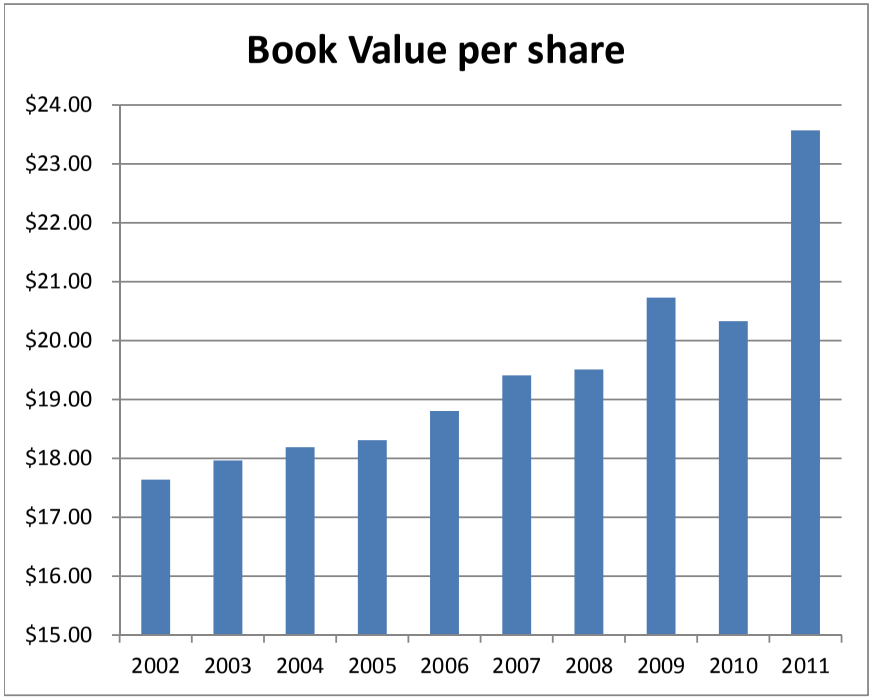
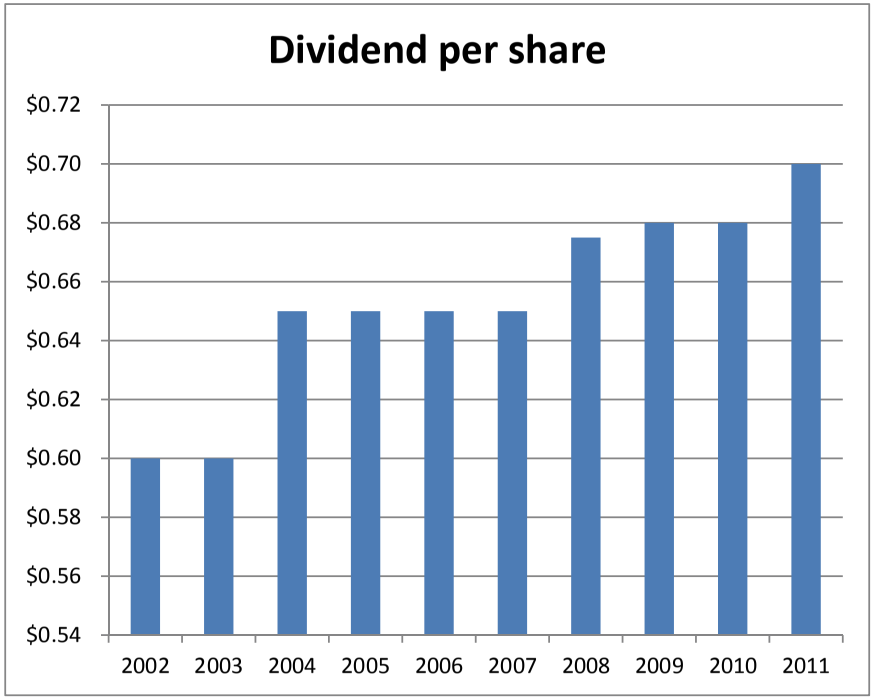
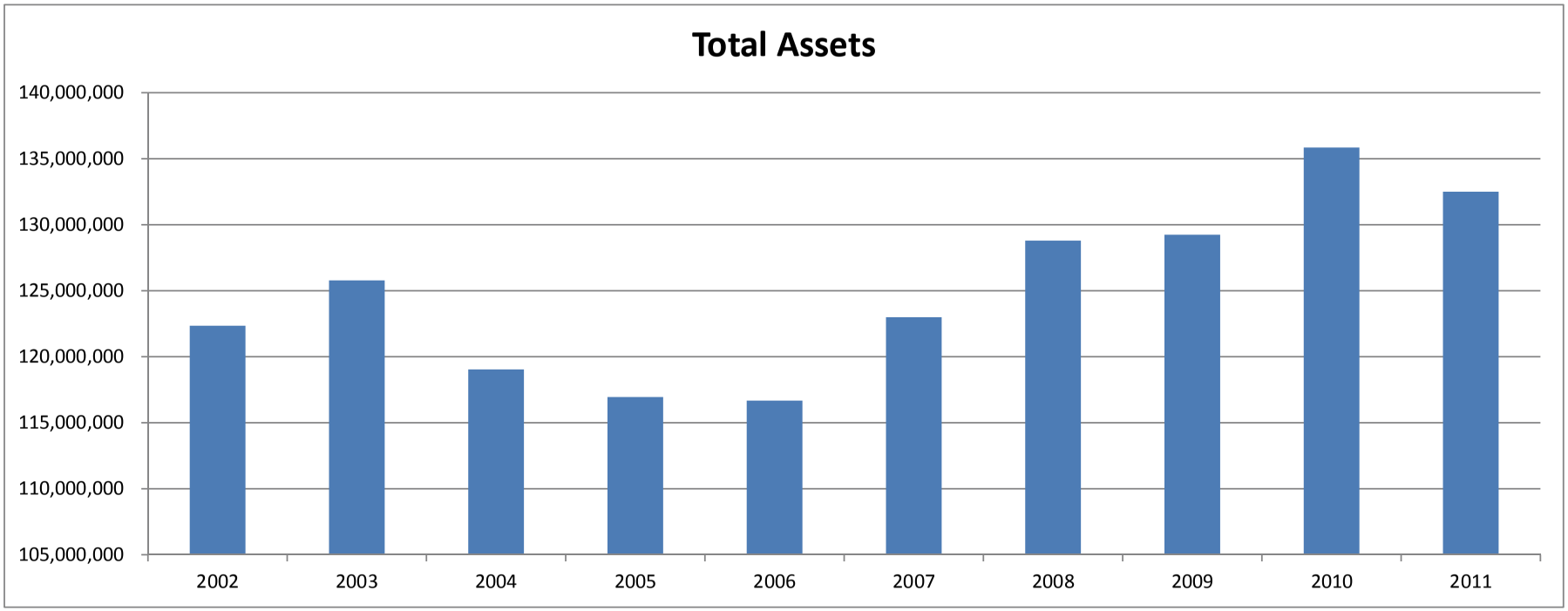
2002 2003 2004 2005 2006 2007 2008 2009 2010 2011


Book Value per share
$24.00
$23.00
$22.00
$21.00
$20.00
$19.00
$18.00
$17.00
$16.00
$15.00
2002 2003 2004 2005 2006 2007 2008 2009 2010 2011


Dividend per share
$0.72
$0.70
$0.68
$0.66
$0.64
$0.62
$0.60
$0.58
$0.56
$0.54
2002 2003 2004 2005 2006 2007 2008 2009 2010 2011


Total Assets
140,000,000
135,000,000
130,000,000
125,000,000
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2002
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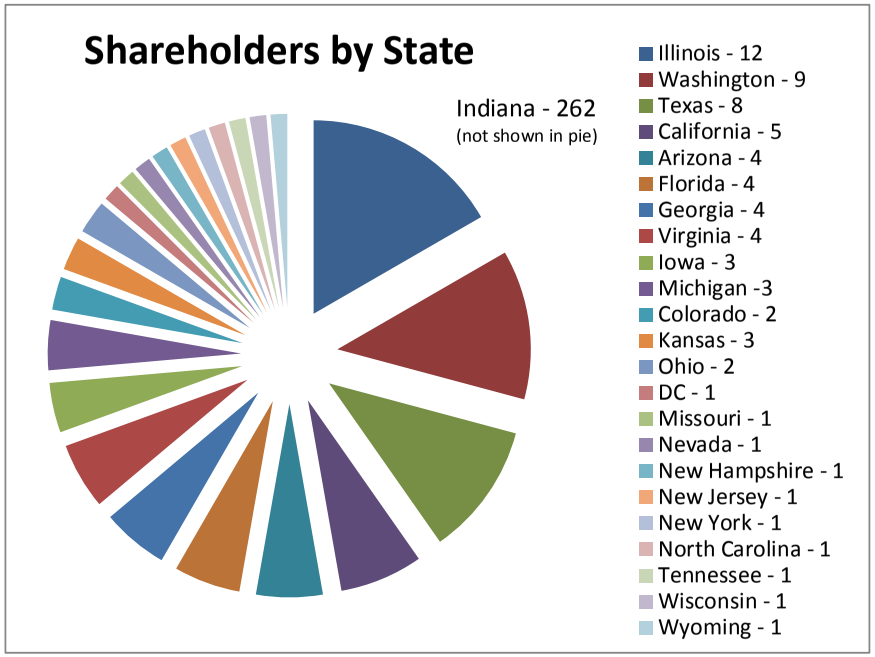
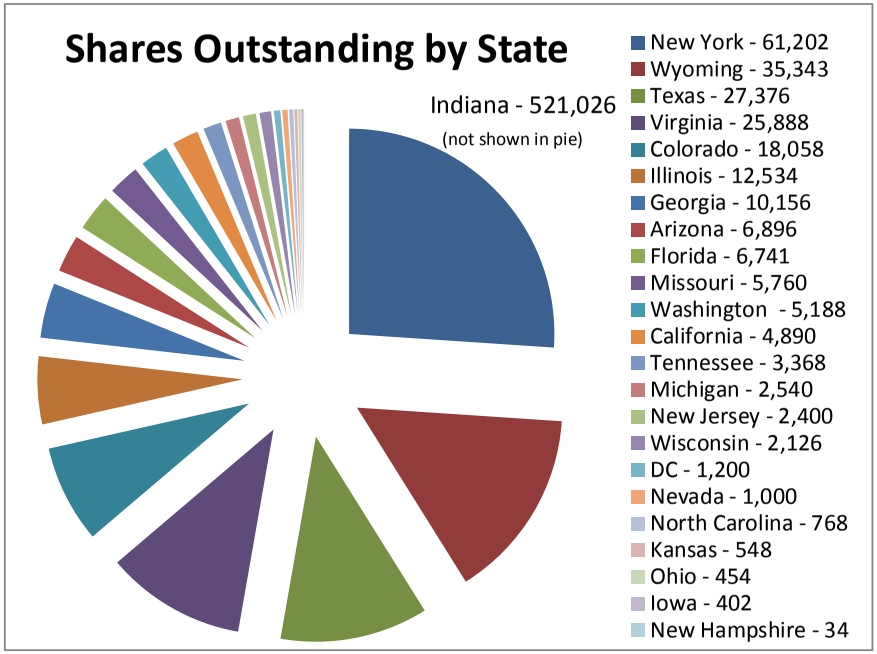
2011


Shareholders by State
Indiana - 262
(not shown in pie)
Illinois - 12
Washington - 9
Texas - 8
California - 5
Arizona - 4
Florida - 4
Georgia - 4
Virginia - 4
Iowa - 3
Michigan -3
Colorado - 2
Kansas - 3
Ohio - 2
DC - 1
Missouri - 1
Nevada - 1
New Hampshire - 1
New Jersey - 1
New York - 1
North Carolina - 1
Tennessee - 1
Wisconsin - 1
Wyoming - 1


Shares Outstanding by State
Indiana - 521,026
(not shown in pie)
New York - 61,202
Wyoming - 35,343
Texas - 27,376
Virginia - 25,888
Colorado - 18,058
Illinois - 12,534
Georgia - 10,156
Arizona - 6,896
Florida - 6,741
Missouri - 5,760
Washington - 5,188
California - 4,890
Tennessee - 3,368
Michigan - 2,540
New Jersey - 2,400
Wisconsin - 2,126
DC - 1,200
Nevada - 1,000
North Carolina - 768
Kansas - 548
Ohio - 454
Iowa - 402
New Hampshire - 34

BENTON FINANCIAL CORPORATION

DIRECTORS AND OFFICERS

STEVEN K BRUNTON, Director, Exec Vice President & CFO
KENNETH W DECKARD, Director and Chairman
MICHAEL E FISCHBACH, Director
JOHN S FREELAND, Director and Vice Chairman
RICK J MICKLE, Director
STEVEN T PETTET, Director, President & CEO
JOHN C WRIGHT, Director
SHERYL D RICHERT, Secretary
CYNTHIA L EBERHARDT, Asst. Secretary

FOWLER STATE BANK

OFFICERS & STAFF

STEVEN T PETTET	President & CEO
STEVEN K BRUNTON	Executive Vice President & CFO
SHERYL D RICHERT	Vice President
RICK J MICKLE	Vice President, Controller & Investment Officer
LINDA K BROUILLETTE	Vice President
TRACI L DAVIES	Vice President
CYNTHIA L EBERHARDT	Vice President
ANNE M MOLTER	Senior Trust Officer & Vice President
LINDA I BREWER	Cashier & Assistant Trust Officer
KIM M DATZMAN	Chief Technology Officer & Assistant Vice President
KASSEY L BUDREAU	Assistant Vice President & Personnel Administrator
DIANE L ROSS	Assistant Vice President & Mortgage Loan Coordinator
MARIE L ROWE	Assistant Vice President & Loan Officer
JAMES D REMSBURG	Senior Loan Officer
LORI A FRANCIS	Operations Officer & Assistant Trust Officer
MARY LOU HARDEBECK	Assistant Cashier
MARTHA L SALLA	Assistant Cashier
PAMELA S BENNER	Assistant Auditor

STAFF

ANNE K HANSON
AMY M HARDEBECK
MICHELLE E HUFF
ELIZABETH M SANFORD
LAURA S LEE
BROOKE E KRUG

PART TIME

K RENE' ADWELL
GAYLE S LEE
KRISTIN L KUNTZ
RONNIE G SLAVENS

CO-OP STUDENT

CLINT C KNOWLES

FOWLER BRANCH

LINDA K RINGLE
SANDRA S SYLVESTER
TERRI L LIVINGSTON

WILLIAMSPORT BRANCH

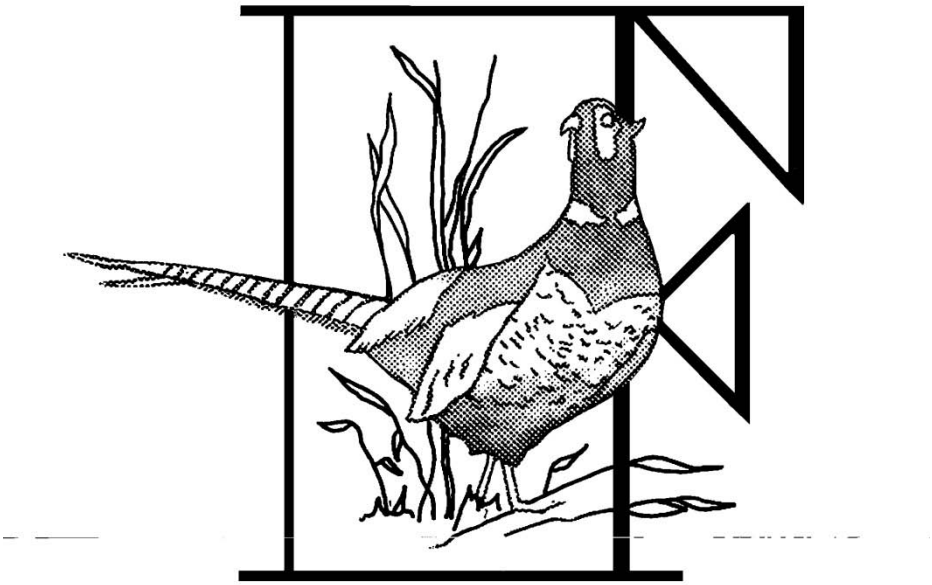
CHRISTOPHER C WILLIAMS	Vice President and Branch Manager
ROBERTA S CRONE	Branch Operations Officer
ROBERTA R DEXTER	
STEPHANIA L COLE	

PART TIME
SHARON F STRICKLAND

KENTLAND BRANCH

CURT A PUETZ	Assistant Vice President and Loan Officer
F KAY GOETZ	
RUTH A SLAVENS	
KAREN K EBERLE	

PART TIME
MYRA J MIILLER



FOWLER STATE BANK

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800.439.2802

406 South Grant Ave
Fowler, IN 47944
765.884.3241

607 East Lincoln
P O Box 27
Kentland, IN 47951-0027
219.474.5444
800.207.3615

Benton Financial Corporation

Accountants' Report and Consolidated Financial Statements

December 31, 2011 and 2010

BKD LLP
CPAs & Advisors

201 N. Illinois Street, Suite 700
P.O. Box 44998
Indianapolis, IN 46244-0998
317.383.4000 Fax 317.383.4200 www.bkd.com

Independent Accountants' Report

To the Stockholders and
Board of Directors
Benton Financial Corporation
Fowler, Indiana

We have audited the accompanying consolidated balance sheets of Benton Financial Corporation as of December 31, 2011 and 2010, and the related consolidated statements of income, stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Benton Financial Corporation as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

BKD, LLP

Indianapolis, Indiana
February 21, 2012

experience BKD

Praxity MEMBER
GLOBAL ALLIANCE OF INDEPENDENT FIRMS

Benton Financial Corporation

Consolidated Balance Sheets
December 31, 2011 and 2010

Assets

	2011	2010
Cash and due from banks	$ 5,107,567	$ 7,059,284
Interest-bearing demand deposits	150,826	397,879
Cash and cash equivalents	5,258,393	7,457,163
Trading assets	-	1,468,484
Investment securities available for sale	53,508,897	56,185,800
Loans, net of allowance for loan losses of $1,821,129 and $1,711,546 at December 31, 2011 and 2010, respectively	69,289,601	66,071,454
Premises and equipment	632,657	656,271
Federal Home Loan Bank stock	1,315,300	1,381,700
Interest receivable	1,455,602	1,401,503
Other assets	1,045,284	1,224,095
Total assets	$ 132,505,734	$ 135,846,470

Liabilities and Stockholders' Equity

Liabilities		
Deposits		
Noninterest-bearing	$ 18,968,649	$ 14,258,001
Interest-bearing	72,217,424	83,569,709
Total deposits	91,186,073	97,827,710
Borrowings	22,500,000	21,500,000
Interest payable	99,621	139,244
Other liabilities	676,597	857,983
Total liabilities	114,462,291	120,324,937
Stockholders' Equity		
Preferred stock, no par value		
Authorized and unissued - 250,000 shares		
Common stock, no par value		
Authorized - 1,200,000 shares		
Issued and outstanding - 765,493 and 763,455 shares as of December 31, 2011 and 2010, respectively	1,975,708	1,968,661
Capital surplus	1,253,342	1,203,834
Retained earnings	13,399,650	12,327,695
Accumulated other comprehensive income	1,414,743	21,343
Total stockholders' equity	18,043,443	15,521,533
Total liabilities and stockholders' equity	$ 132,505,734	$ 135,846,470

Benton Financial Corporation

Consolidated Statements of Income
Years Ended December 31, 2011 and 2010

	2011	2010
Interest Income		
Loans receivable	$ 4,488,995	$ 4,433,665
Investment securities		
Taxable	1,811,047	1,993,291
Tax-exempt	545,455	302,221
Deposits with financial institutions	10,548	31,765
Total interest income	6,856,045	6,760,942
Interest Expense		
Deposits	533,015	763,732
Long-term debt	781,677	889,316
Total interest expense	1,314,692	1,653,048
Net Interest Income	5,541,353	5,107,894
Provision for loan losses	257,000	1,499,000
Net Interest Income After Provision for Loan Losses	5,284,353	3,608,894
Other Income		
Fiduciary activities	113,514	133,931
Service charges on deposit accounts	369,613	399,283
Net realized gains on sales of available-for-sale securities	512,965	306,769
Other-than-temporary losses on investments recognized in earnings	(135,000)	-
Other income	104,611	99,406
Total other income	965,703	939,389
Other Expenses		
Salaries and employee benefits	2,253,842	2,028,447
Net occupancy expense	149,445	141,852
Equipment expense	224,595	220,591
Data processing fees	257,055	247,124
Other expenses	1,059,563	1,117,056
Total other expense	3,944,500	3,755,070
Income Before Income Tax	2,305,556	793,213
Income tax expense	699,181	190,377
Net Income	$ 1,606,375	$ 602,836
Earnings Per Share	$ 2.10	$ 0.79
Weighted-Average Shares Outstanding	763,550	763,455

Benton Financial Corporation

Consolidated Statements of Stockholders' Equity
Years Ended December 31, 2011 and 2010

	Common Stock				Accumulated Other	
	Shares Outstanding	Amount	Capital Surplus	Retained Earnings	Comprehensive Income	Total
Balance, January 1, 2010	763,455	$ 1,968,661	$ 1,203,834	$ 12,244,009	$ 408,654	$ 15,825,158
Comprehensive income						
Net income				602,836		602,836
Change in unrealized gains on securities, net of reclassification adjustment and tax					(387,311)	(387,311)
Total comprehensive income						215,525
Cash dividends ($0.68 per share)				(519,150)		(519,150)
Balance, January 1, 2011	763,455	1,968,661	1,203,834	12,327,695	21,343	15,521,533
Comprehensive income						
Net income				1,606,375		1,606,375
Change in unrealized gains on securities, net of reclassification adjustment and tax					1,393,400	1,393,400
Total comprehensive income						2,999,775
Cash dividends ($0.70 per share)				(534,420)		(534,420)
Issuance of stock	2,038	7,047	49,508			56,555
Balance, December 31, 2011	765,493	$ 1,975,708	$ 1,253,342	$ 13,399,650	$ 1,414,743	$ 18,043,443

See Notes to Consolidated Financial Statements

Benton Financial Corporation

Consolidated Statements of Cash Flows
Years Ended December 31, 2011 and 2010

	2011	2010
Operating Activities		
Net income	$ 1,606,375	$ 602,836
Items not requiring (providing) cash		
Provision for loan losses	257,000	1,499,000
Depreciation and amortization	105,642	89,803
Deferred income taxes	23,013	(112,299)
Investment securities amortization, net	49,529	152,706
Investment securities gains	(512,965)	(306,769)
Other-than-temporary losses on investments	135,000	-
Net change in		
Trading assets	1,468,484	860,478
Interest receivable	(54,099)	64,410
Interest payable	(39,623)	(5,227)
Other assets	(758,138)	663,642
Other liabilities	(181,386)	58,701
Net cash provided by operating activities	2,098,832	3,567,281
Investing Activities		
Purchases of securities available for sale	(26,112,517)	(42,677,934)
Proceeds from maturities of securities available for sale	5,146,366	5,025,964
Proceeds from sales of securities available for sale	26,278,826	31,365,028
Proceeds from federal funds purchased	2,000,000	-
Proceeds from redemption of FHLB stock	66,400	68,000
Net change in loans	(3,475,147)	(1,777,306)
Net change in interest-bearing time deposits	-	500,000
Purchase of premises and equipment	(82,028)	(90,872)
Net cash provided by (used in) investing activities	3,821,900	(7,587,120)
Financing Activities		
Net change in		
Noninterest-bearing, interest-bearing demand and savings deposits	(17,974,307)	2,437,779
Certificates of deposit	11,332,670	8,623,735
Repayment of FHLB advances	(7,500,000)	(4,700,000)
Proceeds from FHLB advances	6,500,000	-
Cash dividends	(534,420)	(519,150)
Issuance of stock	56,555	-
Net cash provided by (used in) financing activities	(8,119,502)	5,842,364
Net Change in Cash and Cash Equivalents	(2,198,770)	1,822,525
Cash and Cash Equivalents, Beginning of Year	7,457,163	5,634,638
Cash and Cash Equivalents, End of Year	$ 5,258,393	$ 7,457,163
Additional Cash Flows Information		
Interest paid	$ 1,354,315	$ 1,658,275
Income tax paid	962,939	4,905
Investment purchased in 2010 but not settled until 2011	-	492,825

Benton Financial Corporation

Notes to Consolidated Financial Statements
December 31, 2011 and 2010
(Table Dollar Amounts in Thousands)

Note 1: Nature of Operations and Summary of Significant Accounting Policies

The accounting and reporting policies of Benton Financial Corporation (Company) and its wholly owned subsidiary, Fowler State Bank (Bank), conform to accounting principles generally accepted in the United States of America and reporting practices followed by the banking industry. The more significant of the policies are described below.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, other-than-temporary impairments (OTTI) and fair values of financial instruments.

The Company is a bank holding company whose principal activity is the ownership and management of the Bank. The Bank operates under a state bank charter and provides full banking services, including trust services. As a state bank, the Bank is subject to regulation by the Department of Financial Institutions, State of Indiana and the Federal Deposit Insurance Corporation.

The Bank generates commercial, mortgage and consumer loans and receives deposits from customers located primarily in Benton, Newton and Warren Counties, Indiana and surrounding counties. The Bank's loans are generally secured by specific items of collateral including real property, consumer assets and business assets. Although the Bank has a diversified loan portfolio, a substantial portion of its debtors' ability to honor their contracts is dependent upon economic conditions in the agricultural industry.

Consolidation

The consolidated financial statements include the accounts of the Company and Bank after elimination of all material intercompany transactions.

Cash and Cash Equivalents

The Company considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2011 and 2010, cash and cash equivalents consisted primarily of cash on hand and deposits with other institutions.

Effective July 21, 2010, the FDIC's insurance limits were permanently increased to $250,000. At December 31, 2011, the Company had $250,000 in interest-bearing cash accounts exceeding federally insured limits.

Pursuant to legislation enacted in 2010, the FDIC will fully insure all noninterest-bearing transaction accounts through December 31, 2012, at all FDIC-insured institutions.

Additionally, the Company had approximately $531,000 on deposit with the Federal Reserve Bank and the Federal Home Loan Bank of Indianapolis as of December 31, 2011, which are not FDIC-insured.

Trading Activities

Trading activities are engaged in by the Bank for its own account. Securities that are held principally for resale in the near term are recorded in the trading assets account at fair value with changes in fair value recorded in earnings. Interest is included in net interest income.

Investment Securities

Certain debt securities that management has the positive intent and ability to hold to maturity are classified as "held to maturity" and recorded at amortized cost. Trading securities are recorded at fair value with changes in fair value included in earnings. Securities not classified as held to maturity or trading, including equity securities with readily determinable fair values, are classified as "available for sale" and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

For debt securities with fair value below amortized cost when the Company does not intend to sell a debt security, and it is more likely than not, the Company will not have to sell the security before recovery of its cost basis, it recognizes the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income. For held-to-maturity debt securities, the amount of an other-than-temporary impairment recorded in other comprehensive income for the noncredit portion of a previous other-than-temporary impairment is amortized prospectively over the remaining life of the security on the basis of the timing of future estimated cash flows of the security.

The Company's consolidated statement of income as of December 31, 2011, reflects the full impairment (that is, the difference between the security's amortized cost basis and fair value) on debt securities. They are available-for-sale securities that management has no intent to sell and believes that it more likely than not will not be required to sell prior to recovery, only the credit loss component of the impairment is recognized in earnings, while the noncredit loss is recognized in accumulated other comprehensive income. The credit loss component recognized in earnings is identified as the amount of principal cash flows not expected to be received over the remaining term of the security as projected based on cash flow projections.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoffs are reported at their outstanding principal balances adjusted for unearned income, charge-offs, the allowance for loan losses, any unamortized deferred fees or costs on originated loans and unamortized premiums or discounts on purchased loans.

For loans carried at amortized cost, interest income is accrued based on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, as well as premiums and discounts, are deferred and amortized as a level yield adjustment over the respective term of the loan.

For all loan classes, the accrual of interest is discontinued at the time the loan is 90 days past due unless the credit is well-secured and in process of collection. Past due status is based on contractual terms of the loan. For all loan classes, the entire balance of the loan is considered past due if the minimum payment contractually required to be paid is not received by the contractual due date. For all loan classes, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

Management's general practice is to proactively charge down loans individually evaluated for impairment to the fair value of the underlying collateral. Consistent with regulatory guidance, charge-offs on all loan segments are taken when specific loans, or portions thereof, are considered uncollectible. The Company's policy is to promptly charge these loans off in the period the uncollectible loss is reasonably determined.

For all loan portfolio segments except residential and consumer loans, the Company promptly charges off loans, or portions thereof, when available information confirms that specific loans are uncollectible based on information that includes, but is not limited to, (1) the deteriorating financial condition of the borrower, (2) declining collateral values, and/or (3) legal action, including bankruptcy, that impairs the borrower's ability to adequately meet its obligations. For impaired loans that are considered to be solely collateral dependent, a partial charge-off is recorded when a loss has been confirmed by an updated appraisal or other appropriate valuation of the collateral.

For all classes, all interest accrued but not collected for loans that are placed on nonaccrual or charged off are reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. Nonaccrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to the timely collection of interest or principal. The Company requires a period of satisfactory performance of not less than three months before returning a nonaccrual loan to accrual status.

When cash payments are received on impaired loans in each loan class, the Company records the payment as interest income unless collection of the remaining recorded principal amount is doubtful, at which time payments are used to reduce the principal balance of the loan. Interest income on troubled debt restructured loans is recognized on an accrual basis at the renegotiated rate if the loan is in compliance with the modified terms, no principal reduction has been granted and the loan has demonstrated the ability to perform in accordance with the renegotiated terms for a period of at least six months.

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to income. 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.

The allowance consists of allocated and general components. The allocated component relates to loans that are classified as impaired. For those loans that are classified as impaired, an allowance is established when the collateral value of the impaired loan is lower than the carrying value of that loan. The general component covers nonimpaired loans and is based on historical charge-off experience by segment. The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the three years. Management believes the three year historical loss experience methodology is appropriate in the current economic environment. Other adjustments (qualitative/environmental considerations) for each segment may be added to the allowance for each loan segment after an assessment of internal or external influences on credit quality that are not fully reflected in the historical loss or risk rating data.

A loan is considered impaired when, based on current information and events, it is probable that the Company 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 based on the loan's current payment status and the borrower's financial condition including available sources of cash flows. 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 nonhomogenous type loans such as commercial, nonowner residential 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 dependent. For impaired loans where the Company utilizes the discounted cash flows to determine the level of impairment, the Company includes the entire change in the present value of cash flows as bad debt expense.

The fair values of collateral dependent impaired loans are based on independent appraisals of the collateral. In general, the Company acquires an updated appraisal or evaluation upon identification of impairment and annually thereafter for commercial, commercial real estate and multi-family loans. If the most recent appraisal is over a year old and a new appraisal is not performed, due to lack of comparable values or other reasons, the existing appraisal is utilized and discounted 20% - 30% based on the age of the appraisal, condition of the subject property, and overall economic conditions. After determining the collateral value as described, the fair value is calculated based on the determined collateral value less selling expenses. The potential for outdated appraisal values is considered in our determination of the allowance for loan losses through our analysis of various trends and conditions including the local economy, trends in charge-offs and delinquencies, etc. and the related qualitative adjustments assigned by the Company.

Segments of loans with similar risk characteristics are collectively evaluated for impairment based on the segment's historical loss experience adjusted for changes in trends, conditions and other relevant factors that affect repayment of the loans. Accordingly, the Company does not separately identify individual consumer and residential loans for impairment measurements, unless such loans are the subject of a restructuring agreement due to financial difficulties of the borrower.

In the course of working with borrowers, the Company may choose to restructure the contractual terms of certain loans. In this scenario, the Company attempts to work-out an alternative payment schedule with the borrower in order to optimize collectability of the loan. Any loans that are modified are reviewed by the Company to identify if a troubled debt restructuring ("TDR") has occurred, which is when, for economic or legal reasons related to a borrower's financial difficulties, the Company grants a concession to the borrower that it would not otherwise consider. Terms may be modified to fit the ability of the borrower to repay in line with the borrower's current financial status, and the restructuring of the loan may include the transfer of assets from the borrower to satisfy the debt, a modification of loan terms, or a combination of the two. If such efforts by the Company do not result in a satisfactory arrangement, foreclosure proceedings are initiated. At any time prior to a sale of the property at foreclosure, the Company may terminate foreclosure proceedings if the borrower is able to work-out a satisfactory payment plan.

It is the Company's policy that any restructured loans which are on nonaccrual status prior to being restructured remain on nonaccrual status until three months of satisfactory borrower performance at which time management would consider its return to accrual status. If a loan was accruing at the time of restructuring, the Company reviews the loan to determine if it is appropriate to continue the accrual of interest on the restructured loan.

With regard to determination of the amount of the allowance for credit losses, trouble debt restructured loans are considered to be impaired. As a result, the determination of the amount of impaired loans for each portfolio segment within troubled debt restructurings is the same as detailed previously.

Premises and Equipment

Premises and equipment are carried at cost, net of accumulated depreciation. Depreciation is computed using the straight-line method for premises and the declining balance method for equipment, based principally on the estimated useful lives of the assets. Maintenance and repairs are expensed as incurred, while major additions and improvements are capitalized. Gains and losses on dispositions are included in current operations.

Federal Home Loan Bank Stock

Federal Home Loan Bank stock is a required investment for institutions that are members of the Federal Home Loan Bank system. The required investment in the common stock is based on a predetermined formula.

Income Tax

The Company accounts for income taxes in accordance with income tax accounting guidance (ASC 740, *Income Taxes*). The income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Company determines deferred income taxes using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax basis of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur.

Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are reduced by a valuation allowance if, based on the weight of evidence available, it is more likely than not that some portion or all of a deferred tax asset will not be realized.

Uncertain tax positions are recognized if it is more likely than not, based on the technical merits, that the tax position will be realized or sustained upon examination. The term more likely than not means a likelihood of more than 50 percent; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any. A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances and information available at the reporting date and is subject to management's judgment. The Company recognizes interest and penalties on income taxes as a component of income tax expense.

The Company files consolidated income tax returns with its subsidiaries.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive income, net of applicable income taxes. Other comprehensive income includes unrealized appreciation on available-for-sale securities.

Earnings Per Share

Earnings per share have been computed based upon the weighted-average common shares outstanding during each year.

Current Economic Conditions

The current protracted economic decline continues to present financial institutions with circumstances and challenges, which in some cases have resulted in large and unanticipated declines in the fair values of investments and other assets, constraints on liquidity and capital and significant credit quality problems, including severe volatility in the valuation of real estate and other collateral supporting loans.

The accompanying consolidated financial statements have been prepared using values and information currently available to the Company.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the consolidated financial statements could change rapidly, resulting in material future adjustments in asset values, the allowance for loan losses and capital that could negatively impact the Company's ability to meet regulatory capital requirements and maintain sufficient liquidity. Furthermore, the Company's regulators could require material adjustments to asset values or the allowance for loan losses for regulatory capital purposes that could affect the Company's measurement of regulatory capital and compliance with the capital adequacy guidelines under the regulatory framework for prompt corrective action.

Note 2: Restriction on Cash and Due From Banks

The Bank is required to maintain reserve funds in cash and/or on deposit with the Federal Reserve Bank. The reserve required at December 31, 2011 was $100,000.

Note 3: Trading Assets

Trading assets, at fair value, consist of the following:

	2010
State and municipal securities	$ 1,468

The net unrealized gains on trading activities are as follows:

	2010
State and municipal securities	$ 1

Note 4: Investment Securities

The amortized cost and approximate fair values, together with gross unrealized gains and losses, of securities are as follows:

	2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Value
Available for sale				
Federal agencies	$ 4,032	$ 9	$ (1)	$ 4,040
State and municipal	36,871	2,294	(17)	39,148
Corporate	1,052	39	(174)	917
Mortgage-backed securities and CMO's - governmental-sponsored enterprises (GSE) residential	9,212	206	(14)	9,404
Total available for sale	$ 51,167	$ 2,548	$ (206)	$ 53,509

	2010			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Value
Available for sale				
Federal agencies	$ 13,056	$ 49	$ (138)	$ 12,967
State and municipal	34,819	537	(605)	34,751
Corporate	748	32	(144)	636
Mortgage-backed securities and CMO's - governmental-sponsored enterprises (GSE) residential	7,528	308	(4)	7,832
Total available for sale	$ 56,151	$ 926	$ (891)	$ 56,186

The amortized cost and fair value of securities available for sale at December 31, 2011, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Within one year	$ 3,590	$ 3,596
One to five years	11,737	12,271
Five to ten years	20,580	21,936
After ten years	6,048	6,302
	41,955	44,105
Mortgage-backed securities and CMO's - GSE residential	9,212	9,404
Totals	$ 51,167	$ 53,509

Securities with a carrying value of $15,937,000 and $19,012,000 were pledged at December 31, 2011 and 2010, respectively, to secure certain deposits and for other purposes as permitted or required by law.

Proceeds from sales of securities available for sale during 2011 and 2010 were $26,279,000 and $31,365,000, respectively. Gross gains of $568,000 and $403,000 and gross losses of $55,000 and $94,000 were realized on those sales during 2011 and 2010, respectively. In addition, gross gains of $1,000 and $3,000 and gross losses of $0 and $5,000 were realized on calls of securities during 2011 and 2010, respectively.

Certain investments in debt securities are reported in the consolidated financial statements at an amount less than their historical cost. Total fair value of these investments at December 31, 2011 and 2010 was $6,639,000 and $24,298,000, which is approximately 12% and 43% of the Company's available-for-sale investment portfolio. These declines primarily resulted from changes in market interest rates.

Based on evaluation of available evidence, including recent changes in market interest rates, credit rating information and information obtained from regulatory filings, management believes the declines in fair value for these securities are temporary.

Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income in the period the other-than-temporary impairment is identified.

Securities with unrealized losses at December 31, 2011 were as follows:

	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-sale securities						
Federal agencies	$ 999	$ (1)	$ -	$ -	$ 999	$ (1)
State and municipal	1,212	(16)	120	(1)	1,332	(17)
Corporate	296	(7)	330	(167)	626	(174)
Mortgage-backed securities and CMO's - GSE residential	3,502	(13)	180	(1)	3,682	(14)
Total temporarily impaired	$ 6,009	$ (37)	$ 630	$ (169)	$ 6,639	$ (206)

Securities with unrealized losses at December 31, 2010 were as follows:

	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-sale securities						
Federal agencies	$ 7,861	$ (138)	$ -	$ -	$ 7,861	$ (138)
State and municipal	14,242	(553)	870	(52)	15,112	(605)
Corporate	-	-	353	(144)	353	(144)
Mortgage-backed securities and CMO's - GSE residential	972	(4)	-	-	972	(4)
Total temporarily impaired	$ 23,075	$ (695)	$ 1,223	$ (196)	$ 24,298	$ (891)

State and Municipal

The unrealized losses on the Company's investments in securities of state and municipals were caused by interest rate changes. Because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at December 31, 2011.

Mortgage-Backed Securities, Collateralized Mortgage Obligations and Corporate Securities

The unrealized losses on the Company's investment in these securities were caused by interest rate changes. The Company expects to recover the amortized cost basis over the term of the securities. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at December 31, 2011.

Other-Than-Temporary Impairment

The Company routinely conducts periodic reviews to identify and evaluate each investment security to determine whether an other-than-temporary impairment has occurred. Economic models and payment defaults are evaluated to determine whether an other-than-temporary impairment has occurred on these securities. For each security in the investment portfolio (including but not limited to those whose fair value is less than their amortized cost basis), an extensive, regular review is conducted to determine if an other-than-temporary impairment has occurred. The Company has recognized a loss equal to the credit loss, establishing a new lower amortized cost basis for two municipal securities, totaling $135,000 during December 31, 2011.

Credit Losses Recognized on Investments

	2011
Credit losses on debt securities held	
Beginning of year	$ -
Additions related to other-than-temporary losses not previously recognized	135,000
End of year	$ 135,000

Note 5: Loans and Allowance for Loan Losses

Classes of loans at December 31, include:

	2011	2010
Agricultural	$ 22,854	$ 21,799
Commercial	9,669	9,199
Commercial real estate	12,851	11,604
Residential	19,964	19,419
Consumer	5,773	5,762
	71,111	67,783
Allowance for loan losses	(1,821)	(1,712)
Total loans	$ 69,290	$ 66,071

	2011	2010
Allowance for loan losses		
Balances, January 1	$ 1,712	$ 1,154
Provision for losses	257	1,499
Loans charged off	(478)	(1,040)
Recoveries on loans	330	99
Balances, December 31	$ 1,821	$ 1,712

The risk characteristics of each loan portfolio segment are as follows:

Commercial and Agricultural

The commercial and agricultural loans consist of two segments. The commercial and agricultural loans are primarily analyzed on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected, and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets, such as accounts receivable or inventory, and may include a personal guarantee. Short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

Commercial Real Estate Including Construction

Commercial real estate loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts, and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. The characteristics of properties securing the Company's commercial real estate portfolio are diverse, but with geographic location almost entirely in the Company's market area. Management monitors and evaluates commercial real estate loans based on collateral, geography and risk grade criteria. In general, the Company avoids financing single purpose projects unless other underwriting factors are present to help mitigate risk. In addition, management tracks the level of owner-occupied commercial real estate versus nonowner-occupied loans.

Construction loans are underwritten utilizing feasibility studies, independent appraisal reviews and financial analysis of the developers and property owners. Construction loans are generally based on estimates of costs and value associated with the complete project. These estimates may be inaccurate. Construction loans often involve the disbursement of substantial funds with repayment substantially dependent on the success of the ultimate project. Sources of repayment for these types of loans may be pre-committed permanent loans from approved long-term lenders, sales of developed property or an interim loan commitment from the Company until permanent financing is obtained. These loans are closely monitored by on-site inspections and are considered to have higher risks than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, governmental regulation of real property, general economic conditions and the availability of long-term financing.

Residential and Consumer

Residential and consumer loans consist of two segments. For residential mortgage loans that are secured by 1-4 family residences and are generally owner-occupied, the Company generally establishes a maximum loan-to-value ratio. Home equity loans are typically secured by a subordinate interest in 1-4 family residences, and consumer personal loans are secured by consumer personal assets, such as automobiles or recreational vehicles. Some consumer personal loans are unsecured, such as small installment loans and certain lines of credit. Repayment of these loans is primarily dependent on the personal income of the borrowers, which can be impacted by economic conditions in their market areas, such as unemployment levels. Repayment can also be impacted by changes in property values on residential properties. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

The following presents by portfolio segment, the activity in the allowance for loan losses for the year ended December 31, 2011:

	Agricultural	Commercial	Commercial Real Estate	Residential	Consumer	Total
Beginning Balance	$ 97	$ 539	$ 691	$ 300	$ 85	$ 1,712
Provision	78	(322)	356	74	71	257
Loans charged off	-	(37)	(375)	-	(66)	(478)
Recoveries	-	22	250	6	52	330
Ending Balance	$ 175	$ 202	$ 922	$ 380	$ 142	$ 1,821

The following tables present the balance in the allowance for loan losses and the recorded investment in loans based on the portfolio segment and impairment method as of December 31, 2011:

	Agricultural	Commercial	Commercial Real Estate	Residential	Consumer	Total
Allowance Balances:						
Individually evaluated for impairment	$ -	$ 15	$ 273	$ 130	$ 3	$ 421
Collectively evaluated for impairment	175	187	649	250	139	1,400
Total allowance for loan losses	$ 175	$ 202	$ 922	$ 380	$ 142	$ 1,821
Loan Balances:						
Individually evaluated for impairment	$ -	$ 26	$ 420	$ 452	$ 3	$ 901
Collectively evaluated for impairment	22,854	9,643	12,431	19,512	5,770	70,210
Total loan balances	$ 22,854	$ 9,669	$ 12,851	$ 19,964	$ 5,773	$ 71,111

Internal Risk Categories

The use and application of these grades by the bank will be uniform and shall conform to the bank's policy.

Pass loans have risk that is considered reasonable or satisfactory, but are overall not as desirable as Excellent or Good grade loans. Financial statements reveal earnings' performance generally in line with industry averages, but not always consistent from year to year. Financial statement ratios are generally in line with industry averages. Any weaknesses in financial performance and/or management strength are offset by such things as adequate collateral, guarantor support, and so forth.

Watch loans have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution's credit position at some future date. Special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification. Ordinarily, special mention credits have characteristics which corrective management action would remedy.

Substandard loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful loans have all the weaknesses inherent in those classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of current known facts, conditions and values, highly questionable and improbable.

Loss loans are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value but rather it is not practical or desirable to defer writing off even though partial recovery may be affected in the future.

The following table presents the credit risk profile of the Company's loan portfolio based on rating category and payment activity as of December 31, 2011:

	Agricultural	Commercial	Commercial Real Estate	Residential	Consumer	Total
Grade:						
Pass	$ 22,854	$ 6,034	$ 11,901	$ 19,327	$ 5,698	$ 65,814
Watch	-	3,609	350	244	39	4,242
Substandard	-	-	550	340	36	926
Doubtful	-	26	50	53	-	129
Total	$ 22,854	$ 9,669	$ 12,851	$ 19,964	$ 5,773	$ 71,111

The following table presents the Company's loan portfolio aging analysis as of December 31, 2011:

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans
Agricultural	$ 2	$ 62	$ -	$ 64	$ 22,726	$ 22,854
Commercial	51	373	26	450	8,769	9,669
Commercial real estate	63	226	421	710	11,431	12,851
Residential	448	126	261	835	18,294	19,964
Consumer	62	23	18	103	5,567	5,773
Total loans	$ 626	$ 810	$ 726	$ 2,162	$ 66,787	$ 71,111

At December 31, 2011 and 2010, accruing loans delinquent 90 days or more totaled $0 and $549,000, respectively.

The following table presents the Company's nonaccrual loans at December 31, 2011:

Agricultural	$ -
Commercial	25
Commercial real estate	417
Residential	305
Consumer	19
Total nonaccrual loans	$ 766

Nonaccruing loans at December 31, 2010 were $1,033,000.

The following table presents impaired loans for the year ended December 31, 2011:

	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Average Investment in Impaired Loans	Interest Income Recognized
Impaired loans without a specific valuation allowance:					
Agricultural	$ -	$ -	$ -	$ -	$ -
Commercial	-	-	-	2,843	56
Commercial real estate	31	31	-	127	-
Residential	115	115	-	146	5
Consumer	-	-	-	2	-
Total impaired loans with no related specific reserve	$ 146	$ 146	$ -	$ 3,118	$ 61
Impaired loans with a specific valuation allowance:					
Agricultural	$ -	$ -	$ -	$ -	$ -
Commercial	26	26	15	18	-
Commercial real estate	389	475	173	485	-
Residential	337	368	230	282	11
Consumer	3	3	3	3	-
Total impaired loans with an allowance recorded	$ 755	$ 872	$ 421	$ 788	$ 11
Total impaired loans	$ 901	$ 1,018	$ 421	$ 3,906	$ 72

Impaired loans totaled $1,152,000 at December 31, 2010. An allowance for loan losses of $28,000 relates to impaired loans of $32,000 at December 31, 2010. At December 31, 2010, impaired loans of $1,120,000 had no related allowance for loan losses. Interest income of $66,000 was recognized on average impaired loans of $1,738,000 for 2010. Interest income of $66,000 was recognized on impaired loans on a cash basis during 2010.

There were no newly classified troubled debt restructured loans during 2011.

Note 6: Premises and Equipment

Major classifications of premises and equipment, stated at cost, are as follows:

	2011	2010
Land	$ 77	$ 77
Buildings	1,293	1,284
Leasehold improvements	46	46
Equipment	1,396	1,324
Total cost	2,812	2,731
Accumulated depreciation and amortization	(2,179)	(2,075)
Net	$ 633	$ 656

Note 7: Deposits

	2011	2010
Demand deposits	$ 57,610	$ 53,222
Savings deposits	9,239	8,936
Certificates and other time deposits of $100,000 or more	17,340	16,370
Other certificates and time deposits	6,997	19,300
Total deposits	$ 91,186	$ 97,828

At December 31, 2011, the scheduled maturities of time deposits are as follows:

2012	$ 14,084
2013	5,522
2014	1,690
2015	763
2016	944
Thereafter	1,334
	$ 24,337

The Company had $7,291,000 and $7,335,000 in deposits from one customer, which is a municipality, as of December 31, 2011 and 2010, respectively.

Note 8: Borrowings

Borrowings included the following at December 31:

	2011	2010
Federal funds purchased	$ 2,000	$ -
Federal Home Loan Bank advances	20,500	21,500
Total short-term borrowings	$ 22,500	$ 21,500

The terms of a security agreement with the Federal Home Loan Bank require the Bank to pledge as collateral for advances qualifying first mortgage loans or Agency securities in an amount equal to 170 percent of these advances. Advances are subject to restrictions or penalties in the event of prepayment and include rates from .85% to 4.68%. Federal Home Loan Bank advances totaled $20,500,000 and $21,500,000 at December 31, 2011 and 2010, respectively. Advances totaling $7,000,000 are subject to an option for the FHLB to convert the entire advance to a periodic adjustable rate one year after the date of the advance and quarterly thereafter. The adjustable rate would be for the remaining term at the predetermined rate. If the FHLB exercises its option to convert the advance to an adjustable rate, the advance will be prepayable at the Company's option, at par and without a penalty.

Federal funds purchased mature daily. Maturities of Federal Home Loan Bank advances were as follows at December 31, 2011:

2012	$ 6,000
2013	7,000
2014	5,000
2015	-
2016	2,500
	$ 20,500

Note 9: Stockholders' Equity

Preferred Stock

The Company has authorized 250,000 shares of no par value preferred stock. The Company's Articles of Incorporation permit the Board of Directors, without further stockholder approval, to establish the relative rights, designations, preferences and limitations or restrictions of the Company's preferred stock prior to the issuance thereof. At December 31, 2011 and 2010, no preferred shares had been issued.

Note 10: Income Tax

The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction and various states and foreign jurisdictions. With a few exceptions, the Company is no longer subject to U.S. federal, state and local or non-U.S. income tax examinations by tax authorities for years before 2008.

The provision for income taxes includes these components:

	2011	2010
Income tax expense (benefit)		
Currently payable		
Federal	$ 475	$ 237
State	201	65
Deferred		
Federal	41	(89)
State	(18)	(23)
Total income tax expense	$ 699	$ 190

A reconciliation of income tax expense at the statutory rate to the Company's actual income tax expense is shown below:

Reconciliation of federal statutory to actual tax expense		
Federal statutory income tax at 34%	$ 784	$ 270
Tax-exempt interest	(180)	(115)
Effect of state income taxes	121	28
Other	(26)	7
Actual tax expense	$ 699	$ 190

A cumulative net deferred tax asset (liability) is included in other assets (liabilities). The components of the asset (liability) are as follows:

	2011	2010
Assets		
Depreciation	$ 23	$ 22
Allowance for loan losses	479	438
Deferred compensation	84	94
AMT credit	-	129
Other real estate owned	94	34
Other	8	2
Total assets	688	719
Liabilities		
State income tax	(46)	(40)
FHLB stock	(55)	(58)
Securities available for sale	(928)	(14)
Other	(11)	(21)
Total liabilities	(1,040)	(133)
	$ (352)	$ 586

Note 11: Other Comprehensive Income (Loss)

Other comprehensive income (loss) components and related taxes were as follows:

	Before-Tax Amount	2011 Tax (Expense) Benefit	Net-of-Tax Amount
Unrealized losses on securities:			
Unrealized holding gains (losses) arising during the year	$ 1,929	$ (764)	$ 1,165
Less: reclassification adjustment for gain realized in net income	(378)	150	(228)
	$ 2,307	$ (914)	$ 1,393

	2010 Before-Tax Amount	2010 Tax (Expense) Benefit	2010 Net-of-Tax Amount
Unrealized gains on securities:			
Unrealized holding gains (losses) arising during the year	$ (334)	$ 132	$ (202)
Less: reclassification adjustment for gain realized in net income	307	(122)	185
	$ (641)	$ 254	$ (387)

Note 12: Commitments and Contingent Liabilities

In the normal course of business, there are outstanding commitments and contingent liabilities, such as commitments to extend credit and standby letters of credit, which are not included in the accompanying consolidated financial statements. The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual or notional amount of those instruments. The Bank uses the same credit policies in making such commitments as it does for instruments that are included in the consolidated balance sheet.

Financial instruments whose contract amount represents credit risk as of December 31 were as follows:

	2011	2010
Commitments to extend credit	$ 18,273	$ 21,569
Standby letters of credit	204	255

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 drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include accounts receivable, inventory, property and equipment and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party.

The Company and Bank have entered into an employment agreement with certain officers which provides for continuation of salary and certain benefits under certain conditions. Under the terms of the agreement, payment could occur in the event of a change in control of the Company or Bank, as defined, along with other specified conditions. The contingent liability under the agreement in the event of a change in control is approximately $404,000.

Note 13: Regulatory Capital

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies and is assigned to a capital category. The assigned capital category is largely determined by three ratios that are calculated according to the regulations: total risk adjusted capital, Tier 1 capital and Tier 1 leverage ratios. The ratios are intended to measure capital relative to assets and credit risk associated with those assets and off-balance sheet exposures of the entity. The capital category assigned to an entity can also be affected by qualitative judgments made by regulatory agencies about the risk inherent in the entity's activities that are not part of the calculated ratios. Furthermore, the Company's regulators could require adjustments to regulatory capital not reflected in these financial statements.

Quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier I capital to average assets (as defined). Management believes, as of December 31, 2011 and 2010, that the Company meets all capital adequacy requirements to which it is subject.

There are five capital categories defined in the regulations, ranging from well capitalized to critically undercapitalized. Classification of a bank in any of the undercapitalized categories can result in actions by regulators that could have a material effect on a bank's operations. At December 31, 2011 and 2010, the Bank is categorized as well capitalized and met all subject capital adequacy requirements. There are no conditions or events since December 31, 2011, that management believes have changed the Bank's classification.

The Bank's actual and required capital amounts and ratios are as follows:

	Actual		Minimum Required for Adequate Capital		Minimum Required To Be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2011						
Total capital (to risk-weighted assets)	$ 17,486	19.3%	$ 7,232	8.0%	$ 9,041	10.0%
Tier I capital (to risk-weighted assets)	16,347	18.1%	3,616	4.0%	5,424	6.0%
Tier I capital (to average assets)	16,347	12.3%	5,322	4.0%	6,652	5.0%
As of December 31, 2010						
Total capital (to risk-weighted assets)	$ 16,448	18.5%	$ 7,105	8.0%	$ 8,881	10.0%
Tier I capital (to risk-weighted assets)	15,330	17.3%	3,552	4.0%	5,329	6.0%
Tier I capital (to average assets)	15,330	10.9%	5,645	4.0%	7,056	5.0%

The Bank is subject to certain restrictions on the amount of dividends that it may declare without prior regulatory approval. Generally, the Bank's payment of dividends is limited to net income for the current year plus the two preceding calendar years, less capital distributions paid over the comparable time period.

Note 14: Employee Benefits

The Bank has a profit-sharing plan which covers all officers and employees with one year of service and over age 21. The Bank has generally contributed the maximum permissible amount to the plan, which is 15% of covered wages. Employee benefits in the plan vest over a period of years and reach 100% after six years. The Bank's expense for the plan was $208,000 for 2011 and $195,000 for 2010.

Note 15: Related Party Transactions

The Bank has entered into transactions with certain directors, executive officers, significant stockholders and their affiliates or associates (related parties). Such transactions were made in the ordinary course of business on substantially the same terms and conditions, including interest rates and collateral, as those prevailing at the same time for comparable transactions with other customers, and did not, in the opinion of management, involve more than normal credit risk or present other unfavorable features. The aggregate amount of loans to such related parties at December 31, 2011 and 2010 was $2,391,000 and $2,559,000, respectively.

Deposits from related parties held by the Bank at December 31, 2011 and 2010 totaled $928,000 and $2,958,000, respectively.

Note 16: Disclosures About Fair Value of Assets and Liabilities

ASC Topic 820, *Fair Value Measurements*, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Topic 820 also specifies a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The standard describes three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

The following is a description of the valuation methodologies and inputs used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy.

Trading and Available-for-Sale Securities

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include exchange traded preferred securities included in corporate securities. 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 flows. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the security's terms and conditions. Additionally, matrix pricing is used for certain investment securities and is a mathematical technique widely used in the banking industry to value investment securities without relying exclusively on quoted prices for specific investment securities but rather relying on the investment securities' relationship to other benchmark quoted investment securities. Level 2 securities include state and municipal, federal agencies, corporate and mortgage-backed securities and CMOs. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

The following tables present the fair value measurements of assets and liabilities measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall:

		2011 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Federal agencies	$ 4,040	$ -	$ 4,040	$ -
State and municipal	39,148	-	39,148	-
Corporate	917	-	917	-
Mortgage-backed securities and CMO's - GSE residential	9,404	-	9,404	-
	$ 53,509	$ -	$ 53,509	$ -

		2010 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Trading assets				
State and municipal	$ 1,468	$ -	$ 1,468	$ -
Federal agencies	12,967	-	12,967	-
State and municipal	34,751	-	34,751	-
Corporate	636	-	636	-
Mortgage-backed securities and CMO's - GSE residential	7,832	-	7,832	-
	$ 57,654	$ -	$ 57,654	$ -

The following is a description of the valuation methodologies and inputs used for instruments measured at fair value on a nonrecurring basis, as well as the general classification of such instruments pursuant to the valuation hierarchy.

Impaired Loans (Collateral Dependent)

Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms are measured for impairment. Allowable methods for determining the amount of impairment include estimating fair value using the fair value of the collateral for collateral-dependent loans.

If the impaired loan is identified as collateral dependent, then the fair value method of measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor to the value.

Impaired loans that are collateral dependent are classified within Level 3 of the fair value hierarchy when impairment is determined using the fair value method.

The following tables present the fair value measurements of assets and liabilities measured at fair value on a nonrecurring basis and the level within the fair value hierarchy in which the fair value measurements fall:

		2011 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	$ 616	$ -	$ -	$ 616

		2010 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	$ 2,784	$ -	$ -	$ 2,784

The following table presents estimated fair values of the Company's financial instruments.

	2011		2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets				
Cash and cash equivalents	$ 5,258	$ 5,258	$ 7,457	$ 7,457
Trading assets	-	-	1,468	1,468
Available-for-sale securities	53,509	53,509	56,186	56,186
Loans, net	69,290	68,985	66,071	66,368
Stock in FHLB	1,315	1,315	1,382	1,382
Interest receivable	1,456	1,456	1,402	1,402
Financial liabilities				
Deposits	91,186	91,918	97,828	98,266
Borrowings	22,500	21,240	21,500	22,485
Interest payable	100	100	139	139

For purposes of the above disclosures of estimated fair value, the following assumptions were used as of December 31, 2011 and 2010. The estimated fair value for cash and cash equivalents, interest-bearing time deposits, FHLB stock, accrued interest receivable, demand deposits, savings accounts, NOW accounts, certain money market deposits, short-term borrowings and interest payable is considered to approximate cost. The estimated fair value for loans receivable, net, is based on estimates of the rate the Bank would charge for similar loans at December 31, 2011 and 2010, applied for the time period until the loans are assumed to reprice or be paid. The estimated fair value for fixed-maturity time deposits as well as borrowings is based on estimates of the rate the Bank would pay on such liabilities at December 31, 2011 and 2010, applied for the time period until maturity.

Note 17: Condensed Financial Information (Parent Company Only)

Presented below is condensed financial information as to financial position, results of operations and cash flows of the Company:

Condensed Balance Sheets

	2011	2010
Assets		
Cash and due from banks	$ 60	$ 79
Investment in common stock of subsidiary	17,862	15,351
Other assets	121	92
Total assets	$ 18,043	$ 15,522
Stockholders' Equity	$ 18,043	$ 15,522

Condensed Statements of Income

	2011	2010
Income		
Dividends from subsidiary	$ 535	$ 547
Expenses		
Other expenses	46	60
Income Before Income Tax and Equity in Undistributed Income of Subsidiary	489	487
Income Tax Benefit	-	(24)
Income Before Equity in Undistributed Income of Subsidiary	489	511
Equity in Undistributed Income of Subsidiary	1,117	92
Net Income	$ 1,606	$ 603

Condensed Statements of Cash Flows

	2011	2010
Operating Activities		
Net income	$ 1,606	$ 603
Adjustments to reconcile net income to net cash used in operating activities	(1,148)	(68)
Net cash provided by operating activities	458	535
Financing Activities		
Cash dividends	(534)	(519)
Issuance of common stock	57	-
Net cash used in financing activities	(477)	(519)
Net Change in Cash and Due From Banks	(19)	16
Cash and Due From Banks at Beginning of Year	79	63
Cash and Due From Banks at End of Year	$ 60	$ 79

Note 18: Subsequent Events

Subsequent events have been evaluated through the date of the Independent Accountants' Report, which is the date the consolidated financial statements were available to be issued.