FIRST MID ILLINOIS BANCSHARES INC
Form 10-Q
August 08, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2011

Or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____________ to ______________

Commission file number 0-13368

FIRST MID-ILLINOIS BANCSHARES, INC.
(Exact name of Registrant as specified in its charter)

Delaware	37-1103704
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification no.)
1515 Charleston Avenue, Mattoon, Illinois	61938
(Address of principal executive offices)	(Zip code)

(217) 234-7454
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [X] No [ ]

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, 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. (Check one):

Large accelerated filer [ ]	Accelerated filer [X]
Non-accelerated filer [ ]	Smaller reporting company [ ]

(Do not check if a smaller reporting company)

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

As of August 5, 2011, 6,034,398 common shares, $4.00 par value, were outstanding.

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PART I

ITEM 1. FINANCIAL STATEMENTS

Condensed Consolidated Balance Sheets

(In thousands, except share data)	(Unaudited) June 30, 2011	December 31, 2010
Assets		
Cash and due from banks:		
Non-interest bearing	$ 36,032	$ 21,008
Interest bearing	91,317	130,485
Federal funds sold	80,999	80,000
Cash and cash equivalents	208,348	231,493
Certificates of deposit investments	12,149	10,000
Investment securities:		
Available-for-sale, at fair value	418,471	342,816
Held-to-maturity, at amortized cost (estimated fair value of $51 at June 30, 2011 and $53 at December 31, 2010)	50	50
Loans held for sale	1,254	114
Loans	799,238	804,467
Less allowance for loan losses	(10,695)	(10,393)
Net loans	788,543	794,074
Interest receivable	5,827	6,390
Other real estate owned	4,649	6,127
Premises and equipment, net	28,218	28,544
Goodwill, net	25,753	25,753
Intangible assets, net	4,496	5,068
Other assets	16,253	17,816
Total assets	$ 1,514,011	$ 1,468,245
Liabilities and Stockholders' Equity		
Deposits:		
Non-interest bearing	$ 196,423	$ 183,932
Interest bearing	1,020,639	1,028,778
Total deposits	1,217,062	1,212,710
Securities sold under agreements to repurchase	111,313	94,057
Interest payable	569	701
FHLB borrowings	19,750	22,750
Junior subordinated debentures	20,620	20,620
Other liabilities	6,994	5,142
Total liabilities	1,376,308	1,355,980
Stockholders' Equity		
Convertible preferred stock, no par value; authorized 1,000,000 shares; issued 8,777 shares in 2011 and 4,927 shares in 2010	43,885	24,635
Common stock, $4 par value; authorized 18,000,000 shares; issued 7,528,199 shares in 2011 and 7,477,132 shares in 2010	30,113	29,909
Additional paid-in capital	28,970	28,223
Retained earnings	68,909	66,356
Deferred compensation	2,979	2,929
Accumulated other comprehensive gain (loss)	1,998	(2,066)

Less treasury stock at cost, 1,492,256 shares in 2011		
and 1,418,456 shares in 2010	(39,151)	(37,721)
Total stockholders' equity	137,703	112,265
Total liabilities and stockholders' equity	$ 1,514,011	$ 1,468,245

See accompanying notes to unaudited condensed consolidated financial statements.

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Condensed Consolidated Statements of Income (unaudited)
(In thousands, except per share data)

	Three months ended June 30,		Six months ended June 30,	
	2011	2010	2011	2010
Interest income:				
Interest and fees on loans	$11,280	$9,822	$22,743	$19,736
Interest on investment securities	2,728	2,181	5,172	4,416
Interest on certificates of deposit investments	19	31	40	62
Interest on federal funds sold	16	21	40	37
Interest on deposits with other financial institutions	79	16	156	30
Total interest income	14,122	12,071	28,151	24,281
Interest expense:				
Interest on deposits	1,778	2,085	3,597	4,271
Interest on securities sold under agreements to repurchase	42	31	75	61
Interest on FHLB borrowings	183	282	394	625
Interest on other borrowings	-	1	-	1
Interest on subordinated debentures	240	262	501	522
Total interest expense	2,243	2,661	4,567	5,480
Net interest income	11,879	9,410	23,584	18,801
Provision for loan losses	916	1,083	1,856	1,843
Net interest income after provision for loan losses	10,963	8,327	21,728	16,958
Other income:				
Trust revenues	739	595	1,520	1,219
Brokerage commissions	152	136	307	265
Insurance commissions	510	444	1,118	1,088
Service charges	1,201	1,181	2,297	2,257
Securities gains, net	196	5	377	246
Total other-than-temporary impairment losses	(61)	(355)	(246)	(978)
Portion of loss recognized in other comprehensive loss	-	-	-	-
Other-than-temporary impairment losses recognized in earnings	(61)	(355)	(246)	(978)
Mortgage banking revenue, net	123	105	239	201
ATM / debit card revenue	889	686	1,721	1,310
Other	310	246	731	503
Total other income	4,059	3,043	8,064	6,111
Other expense:				
Salaries and employee benefits	5,625	4,287	11,059	8,655
Net occupancy and equipment expense	1,983	1,285	3,950	2,563
Net other real estate owned expense	477	299	597	147
FDIC insurance	286	344	720	662
Amortization of intangible assets	286	176	572	352
Stationery and supplies	151	134	289	249
Legal and professional	513	702	1,080	1,131
Marketing and donations	258	207	459	410
Other	1,432	1,274	2,577	2,329
Total other expense	11,011	8,708	21,303	16,498

Income before income taxes	4,011	2,662	8,489	6,571
Income taxes	1,433	880	3,066	2,241
Net income	$2,578	$1,782	$5,423	$4,330
Dividends on preferred shares	1,011	554	1,718	1,131
Net income available to common stockholders	$1,567	$1,228	$3,705	$3,199
Per share data:				
Basic net income per common share available to common stockholders	$0.26	$0.20	$0.61	$0.52
Diluted net income per common share available to common stockholders	$0.26	$0.20	$0.61	$0.52
Cash dividends declared per common share	$0.19	$0.19	$0.19	$0.19

See accompanying notes to unaudited condensed consolidated financial statements.

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Condensed Consolidated Statements of Cash Flows (unaudited)	Six months ended June 30,	
(In thousands)	2011	2010
Cash flows from operating activities:		
Net income	$5,423	$4,330
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,856	1,843
Depreciation, amortization and accretion, net	2,605	1,636
Stock-based compensation expense	26	26
Gains on investment securities, net	(377)	(246)
Other-than-temporary impairment losses recognized in earnings	246	978
(Gains) losses on sales of other real property owned, net	345	(218)
Loss on write down of fixed assets	1	1
Gains on sale of loans held for sale, net	(239)	(214)
Origination of loans held for sale	(20,047)	(16,130)
Proceeds from sale of loans held for sale	19,146	15,833
Increase in other assets	(1,128)	(3,464)
Increase (decrease) in other liabilities	2,261	(2,540)
Net cash provided by operating activities	10,118	1,835
Cash flows from investing activities:		
Proceeds from maturities of certificates of deposit investments	4,018	4,275
Purchases of certificates of deposit investments	(6,167)	(4,931)
Proceeds from sales of securities available-for-sale	11,140	6,367
Proceeds from maturities of securities available-for-sale	60,951	42,747
Proceeds from maturities of securities held-to-maturity	-	995
Purchases of securities available-for-sale	(141,766)	(75,850)
Net decrease in loans	3,675	25,376
Purchases of premises and equipment	(896)	(448)
Proceeds from sales of other real property owned	1,820	1,640
Net cash provided by (used in) investing activities	(67,225)	171
Cash flows from financing activities:		
Net increase in deposits	4,352	28,759
(Increase) decrease in repurchase agreements	17,256	(6,628)
Repayment of long term FHLB advances	(3,000)	(10,000)
Proceeds from short term debt	-	1,500
Proceeds from issuance of common stock	254	195
Proceeds from issuance of preferred stock	19,250	-
Purchase of treasury stock	(1,379)	(560)
Dividends paid on preferred stock	(1,074)	(1,062)
Dividends paid on common stock	(1,697)	(1,714)
Net cash provided by financing activities	33,962	10,490
Increase (decrease) in cash and cash equivalents	(23,145)	12,496
Cash and cash equivalents at beginning of period	231,493	90,411
Cash and cash equivalents at end of period	$208,348	$102,907

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	Six months ended June 30,	
	2011	2010
Supplemental disclosures of cash flow information		
Cash paid during the period for:		
Interest	$4,699	$5,622
Income taxes	1,888	4,343
Supplemental disclosures of noncash investing and financing activities		
Loans transferred to other real estate owned	687	6,084
Dividends reinvested in common stock	641	645
Net tax benefit related to option and deferred compensation plans	131	38

See accompanying notes to unaudited condensed consolidated financial statements.

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Notes to Condensed Consolidated Financial Statements
(unaudited)

Note 1 -- Basis of Accounting and Consolidation

The unaudited condensed consolidated financial statements include the accounts of First Mid-Illinois Bancshares, Inc. ("Company") and its wholly-owned subsidiaries: Mid-Illinois Data Services, Inc. ("MIDS"), First Mid-Illinois Bank & Trust, N.A. ("First Mid Bank") and The Checkley Agency, Inc. doing business as First Mid Insurance Group ("First Mid Insurance"). All significant intercompany balances and transactions have been eliminated in consolidation. The financial information reflects all adjustments which, in the opinion of management, are necessary for a fair presentation of the results of the interim periods ended June 30, 2011 and 2010, and all such adjustments are of a normal recurring nature. Certain amounts in the prior year's consolidated financial statements have been reclassified to conform to the June 30, 2011 presentation and there was no impact on net income or stockholders' equity. The results of the interim period ended June 30, 2011 are not necessarily indicative of the results expected for the year ending December 31, 2011. The Company operates as a one-segment entity for financial reporting purposes.

The 2010 year-end consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

The unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and do not include all of the information required by U.S. generally accepted accounting principles ("GAAP") for complete financial statements and related footnote disclosures although the Company believes that the disclosures made are adequate to make the information not misleading. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's 2010 Annual Report on Form 10-K.

Website

The Company maintains a website at www.firstmid.com. All periodic and current reports of the Company and amendments to these reports filed with the Securities and Exchange Commission ("SEC") can be accessed, free of charge, through this website as soon as reasonably practicable after these materials are filed with the SEC.

Stock Plans

At the Annual Meeting of Stockholders held May 23, 2007, the stockholders approved the First Mid-Illinois Bancshares, Inc. 2007 Stock Incentive Plan ("SI Plan"). The SI Plan was implemented to succeed the Company's 1997 Stock Incentive Plan, which had a ten-year term that expired October 21, 2007. The SI Plan is intended to provide a means whereby directors, employees, consultants and advisors of the Company and its subsidiaries may sustain a sense of proprietorship and personal involvement in the continued development and financial success of the Company and its subsidiaries, thereby advancing the interests of the Company and its stockholders. Accordingly, directors and selected employees, consultants and advisors may be provided the opportunity to acquire shares of common stock of the Company on the terms and conditions established in the SI Plan.

A maximum of 300,000 shares of common stock may be issued under the SI Plan. As of December 31, 2010, the Company had awarded 59,500 shares under the plan. There were no shares awarded during the first six months of 2011.

Convertible Preferred Stock

Series B Convertible Preferred Stock. During 2009, the Company sold to certain accredited investors including directors, executive officers, and certain major customers and holders of the Company's common stock, $24,635,000, in the aggregate, of a newly authorized series of its preferred stock designated as Series B 9% Non-Cumulative Perpetual Convertible Preferred Stock (the "Series B Preferred Stock"). The Series B Preferred Stock had an issue price of $5,000 per share and no par value per share. The Series B Preferred Stock was issued in a private placement exempt from registration pursuant to Regulation D of the Securities Act of 1933, as amended.

The Series B Preferred Stock pays non-cumulative dividends semiannually in arrears, when, as and if authorized by the Board of Directors of the Company, at a rate of 9% per year. Holders of the Series B Preferred Stock will have no voting rights, except with respect to certain fundamental changes in the terms of the Series B Preferred Stock and certain other matters. In addition, if dividends on the Series B Preferred Stock are not paid in full for four dividend periods, whether consecutive or not, the holders of the Series B Preferred Stock, acting as a class with any other of the Company's securities having similar voting rights, will have the right to elect two directors to the Company's Board of Directors. The terms of office of these directors will end when the Company has paid or set aside for payment full semi-annual dividends for four consecutive dividend periods.

Each share of the Series B Preferred Stock may be converted at any time at the option of the holder into shares of the Company's common stock. The number of shares of common stock into which each share of the Series B Preferred Stock is convertible is the $5,000 liquidation preference per share divided by the Conversion Price initially set at $21.94. The Conversion Price is subject to adjustment from time to time pursuant to the terms of the Certificate of Designation (the "Series B Certificate of Designation"). If at the time of conversion, there are any authorized, declared and unpaid dividends with respect to a converted share of Series B Preferred Stock, the holder will receive cash in lieu of the dividends, and a holder will receive cash in lieu of fractional shares of common stock following conversion.

After February 11, 2014, the Company may, at its option but subject to the Company's receipt of any required prior approvals from the Board of Governors of the Federal Reserve System or any other regulatory authority, redeem the Series B Preferred Stock. Any redemption will be in exchange for cash in the amount of $5,000 per share, plus any authorized, declared and unpaid dividends, without accumulation of any undeclared dividends.

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The Company also has the right at any time on or after the fifth anniversary of the original issuance date of the Series B Preferred Stock to require the conversion of all (but not less than all) of the Series B Preferred Stock into shares of common stock if, on the date notice of mandatory conversion is given to holders, the book value of the Company's common stock equals or exceeds 115% of the book value of the Company's common stock at September 30, 2008. "Book value of the Company's common stock" at any date means the result of dividing the Company's total common stockholders' equity at that date, determined in accordance with U.S. generally accepted accounting principles, by the number of shares of common stock then outstanding, net of any shares held in the treasury. The book value of the Company's common stock at September 30, 2008 was $13.03, and 115% of this amount is approximately $14.98. The book value of the Company's common stock at June 30, 2011 was $15.54.

Pursuant to Section 3(j) of the Series B Certification of Designation, the conversion price for the Series B Preferred Stock, which was initially set at $21.94, was required to be adjusted if, among other things, the initial conversion price of any subsequently issued series of preferred stock was lower than the then current conversion price of the Series B Preferred Stock. As a result of the Series C Preferred Stock (see below) having an initial conversion price of less than $21.94, the conversion price of the Series B Preferred Stock was adjusted pursuant to the terms of the Series B Certificate of Designation based on the amount of Series C Preferred Stock sold on February 11, 2011, March 2, 2011 and May 13, 2011. The new conversion price of the Series B Preferred Stock, certified by the Company's accountant pursuant to Section 3(j) of the Series B Certificate of Designation, is $21.71. If additional Series C Preferred Stock is sold following an Investor's receipt of applicable bank regulatory approval, subsequent adjustments will be made to the conversion price of the Series B Preferred Stock

Series C Convertible Preferred Stock. On February 11, 2011, the Company accepted from certain accredited investors, including directors, executive officers, and certain major customers and holders of the Company's common stock (collectively, the "Investors"), subscriptions for the purchase of $27,500,000, in the aggregate, of a newly authorized series of preferred stock designated as Series C 8% Non-Cumulative Perpetual Convertible Preferred Stock (the "Series C Preferred Stock"). As of February 11, 2011, $11,010,000 of the Series C Preferred Stock had been issued and sold by the Company to certain Investors. On March 2, 2011, three investors subsequently completed the required bank regulatory process and an additional $2,750,000 of Series C Preferred Stock was issued and sold by the Company to these investors. On May 13, 2011, four additional investors received the required bank regulatory approval and an additional $5,490,000 of Series C Preferred Stock was issued and sold by the Company to these investors. The balance of the Series C Preferred Stock will be issued to the remaining Investors upon the completion of the bank regulatory process applicable to their purchases.

The Series C Preferred Stock has an issue price of $5,000 per share and no par value per share. The Series C Preferred Stock was issued in a private placement exempt from registration pursuant to Regulation D of the Securities Act of 1933, as amended.

The Series C Preferred Stock pays non-cumulative dividends semiannually in arrears, when, as and if authorized by the Board of Directors of the Company, at a rate of 8% per year. Holders of the Series C Preferred Stock will have no voting rights, except with respect to certain fundamental changes in the terms of the Series C Preferred Stock and certain other matters. In addition, if dividends on the Series C Preferred Stock are not paid in full for four dividend periods, whether consecutive or not, the holders of the Series C Preferred Stock, acting as a class with any other of the Company's securities having similar voting rights, including the Company's Series B Preferred Stock, will have the right to elect two directors to the Company's Board of Directors. The terms of office of these directors will end when the Company has paid or set aside for payment full semi-annual dividends for four consecutive dividend periods.

Each share of the Series C Preferred Stock may be converted at any time at the option of the holder into shares of the Company's common stock. The number of shares of common stock into which each share of the Series C Preferred Stock is convertible is the $5,000 liquidation preference per share divided by the Conversion Price of $20.29. The

Conversion Price is subject to adjustment from time to time pursuant to the terms of the Series C Certificate of Designation. If at the time of conversion, there are any authorized, declared and unpaid dividends with respect to a converted share of Series C Preferred Stock, the holder will receive cash in lieu of the dividends, and a holder will receive cash in lieu of fractional shares of common stock following conversion.

After the fifth anniversary of March 2, 2011, the original issuance date of the shares of the Series C Preferred Stock constituting a majority of the shares issued, the Company may, at its option but subject to the Company's receipt of any required prior approvals from the Board of Governors of the Federal Reserve System or any other regulatory authority, redeem the Series C Preferred Stock. Any redemption will be in exchange for cash in the amount of $5,000 per share, plus any authorized, declared and unpaid dividends, without accumulation of any undeclared dividends.

The Company also has the right at any time after March 2, 2016 to require the conversion of all (but not less than all) of the Series C Preferred Stock into shares of common stock if, on the date notice of mandatory conversion is given to holders, (a) the tangible book value per share of the Company's common stock equals or exceeds 115% of the tangible book value per share of the Company's common stock at December 31, 2010, and (b) the NASDAQ Bank Index (denoted by CBNK:IND) equals or exceeds 115% of the NASDAQ Bank Index at December 31, 2010. "Tangible book value per share of our common stock" at any date means the result of dividing the Company's total common stockholders equity at that date, less the amount of goodwill and intangible assets, determined in accordance with U.S. generally accepted accounting principles, by the number of shares of common stock then outstanding, net of any shares held in the treasury. The tangible book value of the Company's common stock at December 31, 2010 was $9.38, and 115% of this amount is approximately $10.79. The NASDAQ Bank Index value at December 31, 2010 was 1,847.35 and 115% of this amount is approximately 2,124.45. The tangible book value of the Company's common stock at June 30, 2011 was $10.53 and the NASDAQ Bank Index value at June 30, 2011 was 1,758.53.

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Comprehensive Income

The Company's comprehensive income for the three and six-month periods ended June 30, 2011 and 2010 was as follows (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2011	2010	2011	2010
Net income	$2,578	$1,782	$5,423	$4,330
Other comprehensive income:				
Unrealized gains on securities available-for-sale	5,529	1,965	6,791	2,737
Non-credit component of unrealized gains (losses) on securities available-for-sale for which a portion of an other-than-temporary impairment has been recognized in income	46	(223)	-	(552)
Other-than-temporary impairment losses recognized in earnings	61	355	246	978
Reclassification adjustment for realized gains included in income	(196)	(5)	(377)	(246)
Other comprehensive income before taxes	5,440	2,092	6,660	2,917
Tax expense	(2,121)	(816)	(2,596)	(1,137)
Total other comprehensive income	3,319	1,276	4,064	1,780
Comprehensive income	$5,897	$3,058	$9,487	$6,110

The components of accumulated other comprehensive income included in stockholders' equity are as follows:

June 30, 2011	Unrealized Gain (Loss) on Available for Sale Securities	Securities with Other-Than-Temporary Impairment Losses	Total
Net unrealized gains on securities available-for-sale	$8,703	$ -	$8,703
Securities with other-than-temporary impairment losses	-	(5,428)	(5,428)
Tax benefit (expense)	(3,393)	2,116	(1,277)
Balance at June 30, 2011	$5,310	$ (3,312)	$1,998

December 31, 2010	Unrealized Gain (Loss) on Available for Sale Securities	Securities with Other-Than-Temporary Impairment Losses	Total
Net unrealized gains on securities available-for-sale	$2,629	$ -	$2,629
Securities with other-than-temporary impairment losses	-	(6,014)	(6,014)
Tax benefit (expense)	(1,025)	2,344	1,319

Balance at December 31, 2010	$1,604	$ (3,670)	$(2,066)

See “Note 3 – Investment Securities” for more detailed information regarding unrealized losses on available-for-sale securities.

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Adoption of New Accounting Guidance

Accounting Standards Update (ASU) 2010-20 — Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses. The ASU requires expanded disclosure about the credit quality of the loan portfolio in the notes to financial statements, such as aging information and credit quality indicators. Both new and existing disclosures must be disaggregated by portfolio segment or class. The disclosures related to period-end balances and the disclosures of activity that occurs during the reporting period were effective for annual or interim reporting periods beginning after December 15, 2010. The Financial Accounting Standards Board ("FASB") elected to defer the disclosures related to troubled debt restructurings ("TDRs") included within ASU No. 2010-20. These disclosures did not have a material impact on the Company's financial statements.

ASU 2011-01 – Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20. The FASB issued ASU No. 2011-01 in January 2011. The provisions of ASU No. 2010-20 required the disclosure of more granular information on the nature and extent of troubled debt restructurings and their effect on the allowance for loan and lease losses effective for the Company's reporting period ended June 30, 2011. The amendments in ASU No. 2011-01 defer the effective date related to these disclosures, enabling creditors to provide such disclosures after the FASB completes their project clarifying the guidance for determining what constitutes a troubled debt restructuring. As the provisions of this ASU only defer the effective date of disclosure requirements related to troubled debt restructurings, the adoption of this ASU had no impact on the Company's financial statements.

ASU No. 2011-02 – A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring. In April 2011, the FASB issued ASU No. 2011-02. The provisions of ASU No. 2011-02 provide additional guidance related to determining whether a creditor has granted a concession, include factors and examples for creditors to consider in evaluating whether a restructuring results in a delay in payment that is insignificant, prohibit creditors from using the borrower's effective rate test to evaluate whether a concession has been granted to the borrower, and add factors for creditors to use in determining whether a borrower is experiencing financial difficulties. A provision in ASU No. 2011-02 also ends the FASB's deferral of the additional disclosures about troubled debt restructurings as required by ASU No. 2010-20. The provisions of ASU No. 2011-02 are effective for reporting periods ending September 30, 2011. The adoption of ASU No. 2011-02 is not expected to have a material impact on the Company's financial statements.

ASU No. 2011-04 -- Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs. In May 2011, the FASB issued ASU No. 2011-04. ASU 2011-04 changes the wording used to describe many of the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. Consequently, the amendments in this update result in common fair value measurement and disclosure requirements in U.S. GAAP and International Financial Reporting Standards ("IFRS"). ASU 2011-04 is effective prospectively during interim and annual periods beginning on or after December 15, 2011. Early application by public entities is not permitted. The adoption of ASU No. 2011-04 is not expected to have a material impact on the Company's financial statements.

ASU No. 2011-05 – Presentation of Comprehensive Income. In June 2011, the FASB issued ASU No. 2011-05. The provisions of ASU No. 2011-05 allow an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. The statement(s) are required to be presented with equal prominence as the other primary financial statements. ASU No. 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of changes in shareholders' equity but does not change the items that must be reported in other

comprehensive income or when an item of other comprehensive income must be reclassified to net income. The provisions of ASU No. 2011-05 are effective for the Company's interim reporting period beginning on or after December 15, 2011, with retrospective application required. The adoption of ASU No. 2011-05 is expected to result in presentation changes to the Company's statements of income and the addition of a statement of comprehensive income. The adoption of ASU No. 2011-05 will not have a material impact on the Company's financial statements.

Note 2 -- Earnings Per Share

Basic net income per common share available to common stockholders is calculated as net income less preferred stock dividends divided by the weighted average number of common shares outstanding. Diluted net income per common share available to common stockholders is computed using the weighted average number of common shares outstanding, increased by the assumed conversion of the Company's convertible preferred stock and the Company's stock options, unless anti-dilutive.

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The components of basic and diluted net income per common share available to common stockholders for the three and six-month periods ended June 30, 2011 and 2010 were as follows:

	Three months ended June 30,		Six months ended June 30,	
	2011	2010	2011	2010
Basic Net Income per Common Share Available to Common Stockholders:				
Net income	$2,578,000	$1,782,000	$5,423,000	$4,330,000
Preferred stock dividends	(1,011,000)	(554,000)	(1,718,000)	(1,131,000)
Net income available to common stockholders	$1,567,000	$1,228,000	$3,705,000	$3,199,000
Weighted average common shares outstanding	6,058,859	6,101,028	6,065,692	6,099,922
Basic earnings per common share	$.26	$.20	$.61	$.52
Diluted Net Income per Common Share Available to Common Stockholders:				
Net income available to common stockholders	$1,567,000	$1,228,000	$3,705,000	$3,199,000
Effect of assumed preferred stock conversion	-	-	-	-
Net income applicable to diluted earnings per share	$1,567,000	$1,228,000	$3,705,000	$3,199,000
Weighted average common shares outstanding	6,058,859	6,101,028	6,065,692	6,099,922
Dilutive potential common shares:				
Assumed conversion of stock options	12,722	29,569	12,742	28,185
Assumed conversion of preferred stock	-	-	-	-
Diluted weighted average common shares outstanding	6,071,581	6,130,597	6,078,434	6,128,107
Diluted earnings per common share	$.26	$.20	$.61	$.52

The following shares were not considered in computing diluted earnings per share for the three and six-month periods ended June 30, 2011 and 2010 because they were anti-dilutive:

	Three months ended June 30,		Six months ended June 30,	
	2011	2010	2011	2010
Stock options to purchase shares of common stock	202,970	202,970	202,970	202,970
Average dilutive potential common shares associated with convertible preferred stock	1,950,933	1,118,429	1,882,586	1,118,429

Note 3 -- Investment Securities

The amortized cost, gross unrealized gains and losses and estimated fair values for available-for-sale and held-to-maturity securities by major security type at June 30, 2011 and December 31, 2010 were as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
June 30, 2011				
Available-for-sale:				
U.S. Treasury securities and obligations				

of U.S. government corporations & agencies	$175,817	$1,761	$(22)	$177,556
Obligations of states and political subdivisions	26,211	956	(53)	27,114
Mortgage-backed securities: GSE residential	204,784	6,090	(28)	210,846
Trust preferred securities	6,349	-	(5,428)	921
Other securities	2,035	1	(2)	2,034
Total available-for-sale	$415,196	$8,808	$(5,533)	$418,471
Held-to-maturity:				
Obligations of states and political subdivisions	$50	$1	$-	$51

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
December 31, 2010				
Available-for-sale:				
U.S. Treasury securities and obligations				
of U.S. government corporations & agencies	$152,086	$1,319	$(1,024)	$152,381
Obligations of states and political subdivisions	26,549	591	(226)	26,914
Mortgage-backed securities: GSE residential	158,936	3,477	(1,482)	160,931
Trust preferred securities	6,595	-	(6,014)	581
Other securities	2,035	-	(26)	2,009
Total available-for-sale	$346,201	$5,387	$(8,772)	$342,816
Held-to-maturity:				
Obligations of states and political subdivisions	$50	$3	$-	$53

The trust preferred securities are four trust preferred pooled securities issued by First Tennessee Financial ("FTN"). The unrealized losses of these securities, which have maturities ranging from four years to twenty-nine years, are primarily due to their long-term nature, a lack of demand or inactive market for these securities, and concerns regarding the underlying financial institutions that have issued the trust preferred securities. See the heading "Trust Preferred Securities" for further information regarding these securities.

Realized gains and losses resulting from sales of securities were as follows during the periods ended June 30, 2011 and 2010 and the year ended December 31, 2010 (in thousands):

	June 30, 2011	June 30, 2010	December 31, 2010
Gross gains	$377	$246	$543
Gross losses	-	-	-

The following table indicates the expected maturities of investment securities classified as available-for-sale and held-to-maturity, presented at fair value, at June 30, 2011 and the weighted average yield for each range of maturities (dollars in thousands).

	One year or less	After 1 through 5 years	After 5 through 10 years	After ten years	Total
Available-for-sale:					
U.S. Treasury securities and obligations of					
U.S. government corporations and agencies	$157,453	$16,973	$3,130	$-	$177,556
Obligations of state and					
political subdivisions	1,362	9,531	15,860	361	27,114
Mortgage-backed securities: GSE residential	3,379	150,352	57,115	-	210,846
Trust preferred securities	-	-	-	921	921

Other securities	-		1,998		-		36		2,034	
Total investments	$162,194		$178,854		$76,105		$1,318		$418,471	
Weighted average yield	1.93	%	3.52	%	3.49	%	3.72	%	2.90	%
Full tax-equivalent yield	1.95	%	3.62	%	3.89	%	3.85	%	3.02	%
Held-to-maturity:										
Obligations of state and political subdivisions	$-		$51		$-		$-		$51	
Weighted average yield	-	%	4.75	%	-	%	-	%	4.75	%
Full tax-equivalent yield	-	%	6.58	%	-	%	-	%	6.58	%

The weighted average yields are calculated on the basis of the amortized cost and effective yields weighted for the scheduled maturity of each security. Tax-equivalent yields have been calculated using a 34% tax rate. With the exception of obligations of the U.S. Treasury and other U.S. government agencies and corporations, there were no investment securities of any single issuer, the book value of which exceeded 10% of stockholders' equity at June 30, 2011.

Investment securities carried at approximately $273,471,000 and $240,838,000 at June 30, 2011 and December 31, 2010, respectively, were pledged to secure public deposits and repurchase agreements and for other purposes as permitted or required by law.

The following table presents the aging of gross unrealized losses and fair value by investment category as of June 30, 2011 and December 31, 2010 (in thousands):

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2011						
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$4,977	$(22)	$-	$-	$4,977	$(22)
Obligations of states and political subdivisions	2,143	(50)	257	(3)	2,400	(53)
Mortgage-backed securities: GSE residential	9,900	(28)	-	-	9,900	(28)
Trust preferred securities	-	-	921	(5,428)	921	(5,428)
Other securities	1,998	(2)	-	-	1,998	(2)
Total	$19,018	$(102)	$1,178	$(5,431)	$20,196	$(5,533)
December 31, 2010:						
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$58,782	$(1,024)	$-	$-	$58,782	$(1,024)
Obligations of states and political subdivisions	7,263	(216)	252	(10)	7,515	(226)
Mortgage-backed securities: GSE residential	62,171	(1,482)	-	-	62,171	(1,482)
Trust preferred securities	-	-	581	(6,014)	581	(6,014)
Other securities	2,009	(26)	-	-	2,009	(26)
Total	$130,225	$(2,748)	$833	$(6,024)	$131,058	$(8,772)

Obligations of states and political subdivisions. At June 30, 2011, there was one obligation of states and political subdivisions issued by a municipality with a fair value of $257,000 and unrealized losses of $3,000 in a continuous unrealized loss position for twelve months or more. This position was due to yield on municipal securities increasing since the purchase of this securities resulting in the market value being lower than book value. The contractual term of this investment does not permit the issuer to settle the security at a price less than the amortized cost basis of the

investment. Because the Company does not intend to sell these securities and it is not more-likely-than-not the Company will be required to sell this security before recovery of its amortized cost basis, which may be maturity, the Company does not consider this investment to be other than temporarily impaired at June 30, 2011.

Trust Preferred Securities. At June 30, 2011, there were four trust preferred securities with a fair value of $921,000 and unrealized losses of $5,428,000 in a continuous unrealized loss position for twelve months or more. These unrealized losses were primarily due to the long-term nature of the trust preferred securities, a lack of demand or inactive market for these securities, and concerns regarding the underlying financial institutions that have issued the trust preferred securities. Cash flow analysis for these securities indicated an other-than-temporary-impairment (OTTI) and the Company performed further analysis to determine the portion of the loss that was related to credit conditions of the underlying issuers. The credit loss was calculated by comparing expected discounted cash flows based on performance indicators of the underlying assets in the security to the carrying value of the investment. Based on this analysis, the Company recorded impairment charges of approximately $61,000 for the credit portion of the unrealized loss of these trust preferred securities during the quarter ended June 30, 2011. This loss established a new, lower amortized cost basis for these securities and reduced non-interest income as of June 30, 2011. Because the Company does not intend to sell these securities and it is not more-likely-than-not that the Company will be required to sell these securities before recovery of their new, lower amortized cost basis, which may be maturity, the Company does not consider the remainder of the investment in these securities to be other-than-temporarily impaired at June 30, 2011. However, future downgrades or additional deferrals and defaults in these securities, in particular the PreTSL XXVIII security which has the largest current book value, could result in additional OTTI and, consequently, have a material impact on future earnings.

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Following are the details for each trust preferred security (in thousands):

	Book Value	Market Value	Unrealized Loss	Other-than-temporary Impairment Recorded To-date
PreTSL I	$829	$335	$(494)	$691
PreTSL II	1,047	156	(891)	2,167
PreTSL VI	200	87	(113)	127
PreTSL XXVIII	4,273	343	(3,930)	491
Total	$6,349	$921	$(5,428)	$3,476

The Company does not believe any other individual unrealized loss as of June 30, 2011 represents OTTI. However, given the continued disruption in the financial markets, the Company may be required to recognize OTTI losses in future periods with respect to its available for sale investment securities portfolio. The amount and timing of any additional OTTI will depend on the decline in the underlying cash flows of the securities. 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 the period the other-than-temporary impairment is identified.

Other-than-temporary Impairment. Upon acquisition of a security, the Company decides whether it is within the scope of the accounting guidance for beneficial interests in securitized financial assets or will be evaluated for impairment under the accounting guidance for investments in debt and equity securities.

The accounting guidance for beneficial interests in securitized financial assets provides incremental impairment guidance for a subset of the debt securities within the scope of the guidance for investments in debt and equity securities. For securities where the security is a beneficial interest in securitized financial assets, the Company uses the beneficial interests in securitized financial asset impairment model. For securities where the security is not a beneficial interest in securitized financial assets, the Company uses debt and equity securities impairment model.

The Company routinely conducts periodic reviews to identify and evaluate each investment security to determine whether OTTI has occurred. Economic models are used to determine whether OTTI has occurred on these securities. While all securities are considered, the securities primarily impacted by OTTI testing are pooled trust preferred securities. For each pooled trust preferred 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 OTTI has occurred. Various inputs to the economic models are used to determine if an unrealized loss is other-than-temporary. The most significant inputs are the following:

- Prepayments
- Defaults
- Loss severity

These pooled trust preferred securities relate to trust preferred securities issued by financial institutions. The pools typically consist of financial institutions throughout the United States. Other inputs to the economic models may include the actual collateral attributes, which include credit ratings and other performance indicators of the underlying financial institutions including profitability, capital ratios, and asset quality.

To determine if the unrealized losses for pooled trust preferred securities is other-than-temporary, the Company considers the impact of each of these inputs. The Company considers the likelihood that issuers will prepay their securities. During the third quarter of 2010, the Dodd-Frank Act eliminated Tier 1 capital treatment for trust preferred securities issued by holding companies with consolidated assets greater than $15 billon. As a result, issuers may prepay their securities which reduces the amount of expected cash flows. Additionally, the Company projects total estimated defaults of the underlying assets (financial institutions) and multiplies that calculated amount by an estimate of realizable value upon sale in the marketplace (severity) in order to determine the projected collateral loss. The Company also evaluates the current credit enhancement underlying the security to determine the impact on cash flows. If the Company determines that a given pooled trust preferred security position will be subject to a write-down or loss, the Company records the expected credit loss as a charge to earnings.

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Credit Losses Recognized on Investments. As described above, some of the Company's investments in trust preferred securities have experienced fair value deterioration due to credit losses but are not otherwise other-than-temporarily impaired. The following table provides information about those trust preferred securities for which only a credit loss was recognized in income and other losses are recorded in other comprehensive income (loss) for the three months ended June 30, 2011 and 2010 (in thousands).

	Accumulated Credit Losses June 30, 2011	Accumulated Credit Losses June 30, 2010
Credit losses on trust preferred securities held		
Beginning of period	$ 3,230	$ 1,812
Additions related to OTTI losses not previously recognized	-	-
Reductions due to sales	-	-
Reductions due to change in intent or likelihood of sale	-	-
Additions related to increases in previously recognized OTTI losses	246	978
Reductions due to increases in expected cash flows	-	-
End of period	$ 3,476	$ 2,790

Note 4 – Loans and Allowance for Loan Losses

Loans are stated at the principal amount outstanding net of unearned discounts, unearned income and allowance for loan losses. Unearned income includes deferred loan origination fees reduced by loan origination costs and is amortized to interest income over the life of the related loan using methods that approximated the effective interest rate method. Interest on substantially all loans is credited to income based on the principal amount outstanding. A summary of loans at June 30, 2011 and December 31, 2010 follows (in thousands):

	June 30, 2011	December 31, 2010
Construction and land development	$23,087	$20,382
Farm loans	63,190	65,036
1-4 Family residential properties	183,102	179,535
Multifamily residential properties	20,231	22,159
Commercial real estate	309,637	302,220
Loans secured by real estate	599,247	589,332
Agricultural loans	50,713	58,246
Commercial and industrial loans	121,728	126,391
Consumer loans	17,476	19,668
All other loans	12,333	12,464
Gross loans	801,497	806,101
Less:		
Net deferred loan fees, premiums and discounts	1,005	1,520
Allowance for loan losses	10,695	10,393
Net loans	$789,797	$794,188

Loans expected to be sold are classified as held for sale in the consolidated financial statements and are recorded at the lower of aggregate cost or market value, taking into consideration future commitments to sell the loans. The 1-4 family residential properties balance in the above table includes loans held for sale of $1,254,000 and $114,000 at June 30, 2011 and December 31, 2010, respectively.

The structure of the Company's loan approval process is based on progressively larger lending authorities granted to individual loan officers, loan committees, and ultimately the Board of Directors. Outstanding balances to one borrower or affiliated borrowers are limited by federal regulation; however, limits well below the regulatory thresholds are generally observed. The vast majority of the Company's loans are to businesses located in the geographic market areas served by the Company's branch bank system. Additionally, a significant portion of the collateral securing the loans in the portfolio is located within the Company's primary geographic footprint. In general, the Company adheres to loan underwriting standards consistent with industry guidelines for all loan segments.

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Commercial Real Estate Loans
Commercial real estate loans are generally comprised of loans to small business entities to purchase or expand structures in which the business operations are housed, loans to owners of real estate who lease space to non-related commercial entities, loans for construction and land development, loans to hotel operators, and loans to owners of multi-family residential structures, such as apartment buildings. Commercial real estate loans are underwritten based on historical and projected cash flows of the borrower and secondarily on the underlying real estate pledged as collateral on the debt. For the various types of commercial real estate loans, minimum criteria have been established within the Company’s loan policy regarding debt service coverage while maximum limits on loan-to-value and amortization periods have been defined. Maximum loan-to-value ratios range from 65% to 80% depending upon the type of real estate collateral, while the desired minimum debt coverage ratio is 1.20x. Amortization periods for commercial real estate loans are generally limited to twenty years. The Company’s commercial real estate portfolio is well below the thresholds that would designate a concentration in commercial real estate lending, as established by the federal banking regulators.

Commercial and Industrial Loans
Commercial and industrial loans are primarily comprised of working capital loans used to purchase inventory and fund accounts receivable that are secured by business assets other than real estate. These loans are generally written for one year or less. Also, equipment financing is provided to businesses with these loans generally limited to 80% of the value of the collateral and amortization periods limited to seven years. Commercial loans are often accompanied by a personal guaranty of the principal owners of a business. Like commercial real estate loans, the underlying cash flow of the business is the primary consideration in the underwriting process. The financial condition of commercial borrowers is monitored at least annually with the type of financial information required determined by the size of the relationship. Measures employed by the Company for businesses with higher risk profiles include the use of government-assisted lending programs through the Small Business Administration and U.S. Department of Agriculture.

Agricultural and Agricultural Real Estate Loans
Agricultural loans are generally comprised of seasonal operating lines to cash grain farmers to plant and harvest corn and soybeans and term loans to fund the purchase of equipment. Agricultural real estate loans are primarily comprised of loans for the purchase of farmland. Specific underwriting standards have been established for agricultural-related loans including the establishment of projections for each operating year based on industry developed estimates of farm input costs and expected commodity yields and prices. Operating lines are typically written for one year and secured by the crop. Loan-to-value ratios on loans secured by farmland generally do not exceed 80% and have amortization periods limited to twenty five years. Federal government-assistance lending programs through the Farm Service Agency are used to mitigate the level of credit risk when deemed appropriate.

Residential Real Estate Loans
Residential real estate loans generally include loans for the purchase or refinance of residential real estate properties consisting of one-to-four units and home equity loans and lines of credit. The Company sells substantially all of its long-term fixed rate residential real estate loans to secondary market investors. The Company also releases the servicing of these loans upon sale. The Company retains all residential real estate loans with balloon payment features. Balloon periods are limited to five years. Residential real estate loans are typically underwritten to conform to industry standards including criteria for maximum debt-to-income and loan-to-value ratios as well as minimum credit scores. Loans secured by first liens on residential real estate held in the portfolio typically do not exceed 80% of the value of the collateral and have amortization periods of twenty five years or less. The Company does not originate subprime mortgage loans.

Consumer Loans

Consumer loans are primarily comprised of loans to individuals for personal and household purposes such as the purchase of an automobile or other living expenses. Minimum underwriting criteria have been established that consider credit score, debt-to-income ratio, employment history, and collateral coverage. Typically, consumer loans are set up on monthly payments with amortization periods based on the type and age of the collateral.

Other Loans

Other loans consist primarily of loans to municipalities to support community projects such as infrastructure improvements or equipment purchases. Underwriting guidelines for these loans are consistent with those established for commercial loans with the additional repayment source of the taxing authority of the municipality.

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, collateral support, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis includes loans with an outstanding balance greater than $100,000 and non-homogenous loans, such as commercial and commercial real estate loans. This analysis is performed on a continuous basis. The Company uses the following definitions for risk ratings:

Watch. Loans classified as watch have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

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

Doubtful. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing factors, conditions and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered pass rated loans.

The following tables present the credit risk profile of the Company's loan portfolio based on rating category and payment activity as of June 30, 2011 and December 31, 2010 (in thousands):

	Construction & Land Development		Farm Loans		1-4 Family Residential Properties		Multifamily Residential Properties	
	2011	2010	2011	2010	2011	2010	2011	2010
Pass	$19,036	$15,778	$57,851	$58,751	$179,102	$174,782	$20,015	$10,381
Watch	2,194	2,219	2,155	4,710	659	267	-	6,204
Substandard	1,857	1,494	3,165	1,531	3,381	4,478	211	5,561
Doubtful	-	888	-	-	-	-	-	-
Total	$23,087	$20,379	$63,171	$64,992	$183,142	$179,527	$20,226	$22,146

	Commercial Real Estate (Nonfarm/Nonresidential)		Agricultural Loans		Commercial & Industrial Loans		Consumer Loans	
	2011	2010	2011	2010	2011	2010	2011	2010
Pass	$ 274,953	$ 276,174	$44,357	$53,293	$118,001	$120,284	$17,469	$19,655
Watch	25,062	14,598	2,543	3,269	483	2,519	-	-
Substandard	8,508	10,053	3,891	1,745	3,285	3,516	-	-
Doubtful	-	-	-	-	-	-	-	-
Total	$ 308,523	$ 300,825	$50,791	$58,307	$121,769	$126,319	$17,469	$19,655

	All Other Loans		Total Loans	
	2011	2010	2011	2010
Pass	$12,314	$12,431	$743,098	$741,529
Watch	-	-	33,096	33,786
Substandard	-	-	24,298	28,378
Doubtful	-	-	-	888
Total	$12,314	$12,431	$800,492	$804,581

The following table presents the Company's loan portfolio aging analysis at June 30, 2011 and December 31, 2010 (in thousands):

June 30, 2011	30-59 days Past Due	60-89 days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans Receivable	Total Loans > 90 days & Accruing
Construction and land development	$-	$-	$332	$332	$22,755	$23,087	$-
Farm loans	336	-	757	1,093	62,078	63,171	-
	763	533	1,523	2,819	180,323	183,142	-

1-4 Family residential properties							
Multifamily residential properties	-	-	-	-	20,226	20,226	-
Commercial real estate	366	281	1,676	2,323	306,200	308,523	-
Loans secured by real estate	1,465	814	4,288	6,567	591,582	598,149	-
Agricultural loans	-	-	745	745	50,046	50,791	-
Commercial and industrial loans	407	5	861	1,273	120,496	121,769	-
Consumer loans	188	14	-	202	17,267	17,469	-
All other loans	-	-	-	-	12,314	12,314	-
Total loans	$2,060	$833	$5,894	$8,787	$791,705	$800,492	$-

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June 30, 2011	30-59 days Past Due	60-89 days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans Receivable	Total Loans > 90 days & Accruing
Construction and land development	$-	$-	$332	$332	$22,755	$23,087	$-
Farm loans	336	-	757	1,093	62,078	63,171	-
1-4 Family residential properties	763	533	1,523	2,819	180,323	183,142	-
Multifamily residential properties	-	-	-	-	20,226	20,226	-
Commercial real estate	366	281	1,676	2,323	306,200	308,523	-
Loans secured by real estate	1,465	814	4,288	6,567	591,582	598,149	-
Agricultural loans	-	-	745	745	50,046	50,791	-
Commercial and industrial loans	407	5	861	1,273	120,496	121,769	-
Consumer loans	188	14	-	202	17,267	17,469	-
All other loans	-	-	-	-	12,314	12,314	-
Total loans	$2,060	$833	$5,894	$8,787	$791,705	$800,492	$-

Within all loan portfolio segments, loans are considered impaired when, based on current information and events, it is probable the Company will be unable to collect all amounts due from the borrower in accordance with the contractual terms of the loan. The entire balance of a loan is considered delinquent if the minimum payment contractually required to be made is not received by the specified due date. Impaired loans, excluding certain troubled debt restructured loans, are placed on nonaccrual status. Impaired loans include nonaccrual loans and loans modified in troubled debt restructurings where concessions have been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in the interest rate on the loan, payment extensions, forgiveness of principal, forbearance or other actions intended to maximize collection. It is the Company’s policy to have any restructured loans which are on nonaccrual status prior to being modified remain on nonaccrual status until, 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. If the restructured loan is on accrual status prior to being modified, the loan is reviewed to determine if the modified loan should remain on accrual status.

The Company’s policy is to discontinue the accrual of interest income on all loans for which principal or interest is ninety days past due. The accrual of interest is discontinued earlier when, in the opinion of management, there is reasonable doubt as to the timely collection of interest or principal. Once interest accruals are discontinued, accrued but uncollected interest is charged against current year income. Subsequent receipts on non-accrual loans are recorded as a reduction of principal, and interest income is recorded only after principal recovery is reasonably assured. Interest on loans determined to be troubled debt restructurings is recognized on an accrual basis in accordance with the restructured terms if the loan is in compliance with the modified terms. 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 six months before returning a nonaccrual loan to accrual status.

The following tables present impaired loans as of June 30, 2011 and December 31, 2010 (in thousands):

	June 30, 2011			December 31, 2010		
	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Recorded Balance	Unpaid Principal Balance	Specific Allowance
Loans with a specific allowance:						
Construction and land development	$1,430	$1,706	$264	$1,804	$1,804	$478
Farm loans	-	-	-	-	-	-
1-4 Family residential properties	472	472	82	917	917	273
Multifamily residential properties	-	-	-	573	669	69
Commercial real estate	650	650	147	1,120	1,120	79
Loans secured by real estate	2,552	2,828	493	4,414	4,510	899
Agricultural loans	-	-	-	-	-	-
Commercial and industrial loans	413	508	168	231	231	187
Consumer loans	-	-	-	-	-	-
All other loans	-	-	-	-	-	-
Total loans	$2,965	$3,336	$661	$4,645	$4,741	$1,086

	June 30, 2011			December 31, 2010		
	Recorded Balance	Unpaid Principal Balance	Specific Allowance	Recorded Balance	Unpaid Principal Balance	Specific Allowance
Loans without a specific allowance:						
Construction and land development	$-	$-	$-	$151	$151	$-
Farm loans	534	534	-	540	540	-
1-4 Family residential properties	1,856	1,930	-	1,648	1,678	-
Multifamily residential properties	-	-	-	-	-	-
Commercial real estate	3,815	5,112	-	1,916	3,095	-
Loans secured by real estate	6,205	7,576	-	4,255	5,464	-
Agricultural loans	745	745	-	828	828	-
Commercial and industrial loans	725	1,027	-	692	804	-
Consumer loans	-	-	-	14	14	-
All other loans	-	-	-	0	-	-
Total loans	$7,675	$9,348	$-	$5,789	$7,110	$-
Total loans:						
Construction and land development	$1,430	$1,706	$264	$1,955	$1,955	$478
Farm loans	534	534	-	540	540	-
1-4 Family residential properties	2,328	2,402	82	2,565	2,595	273
Multifamily residential properties	-	-	-	573	669	69
Commercial real estate	4,465	5,762	147	3,036	4,215	79
Loans secured by real estate	8,757	10,404	493	8,669	9,974	899
Agricultural loans	745	745	-	828	828	-
Commercial and industrial loans	1,138	1,535	168	923	1,035	187
Consumer loans	-	-	-	14	14	-
All other loans	-	-	-	-	-	-
Total loans	$10,640	$12,684	$661	$10,434	$11,851	$1,086

The following tables present average recorded investment and interest income recognized on impaired loans for the three and six month periods ended June 30, 2011 and 2010 (in thousands):

	For the three months ended			
	June 30, 2011		June 30, 2010	
	Average Investment in Impaired Loans	Interest Income Recognized	Average Investment in Impaired Loans	Interest Income Recognized
Construction and land development	$1,430	$ -	$1,680	$ -
Farm loans	535	-	1,027	-

1-4 Family residential properties	2,320	-	2,102	-
Multifamily residential properties	-	-	188	-
Commercial real estate	4,074	1	5,184	14
Loans secured by real estate	8,359	1	10,181	14
Agricultural loans	752	-	986	-
Commercial and industrial loans	1,366	-	1,137	5
Consumer loans	-	-	24	-
All other loans	-	-	-	-
Total loans	$10,477	$ 1	$12,328	$ 19

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	For the six months ended			
	June 30, 2011		June 30, 2010	
	Average Investment in Impaired Loans	Interest Income Recognized	Average Investment in Impaired Loans	Interest Income Recognized
Construction and land development	$1,422	$ -	$1,680	$ -
Farm loans	536	-	1,397	-
1-4 Family residential properties	2,331	-	2,111	-
Multifamily residential properties	-	-	188	-
Commercial real estate	4,483	7	5,187	28
Loans secured by real estate	8,772	7	10,563	28
Agricultural loans	756	-	1,038	-
Commercial and industrial loans	1,171	-	1,140	6
Consumer loans	-	-	24	-
All other loans	-		-	-
Total loans	$10,699	$7	$12,765	$34

For the three and six months ended June 30, 2011, the amount of interest income recognized by the Company within the period that the loans were impaired was related to loans modified in a troubled debt restructuring that remained on accrual status. The balance of loans modified in a troubled debt restructuring included in the impaired loan stated above that were still accruing was $398,000 of commercial real estate at June 30, 2011 and $888,000 of commercial real estate and $218,000 of commercial and industrial at June 30, 2010. For the three and six months ended June 30, 2011, the amount of interest income recognized using a cash-basis method of accounting during the period that the loans were impaired was not material.

The following table presents the Company's nonaccrual loans at June 30, 2011 and December 31, 2010 (in thousands). This table excludes purchased impaired loans and performing troubled debt restructurings.

	June 30, 2011	December 31, 2010
Construction and land development	$1,430	$1,955
Farm loans	534	540
1-4 Family residential properties	2,328	2,565
Multifamily residential properties	-	573
Commercial real estate	4,067	2,149
Loans secured by real estate	8,359	7,782
Agricultural loans	745	828
Commercial and industrial loans	1,138	708
Consumer loans	-	14
All other loans	-	-
Total loans	$10,242	$9,332

Interest income which would have been recorded under the original terms of such nonaccrual loans totaled $255,000 and $350,000 for the six month periods ended June 30, 2011 and 2010, respectively.

Most of the Company's business activities are with customers located within central Illinois. At June 30, 2011, the Company's loan portfolio included $113.9 million of loans to borrowers whose businesses are directly related to agriculture. Of this amount, $103.1 million was concentrated in other grain farming. Total loans to borrowers whose businesses are directly related to agriculture decreased $14.6 million from $123.3 million at December 31, 2010 while loans concentrated in other grain farming decreased $9.4 million from $123.3 million at December 31, 2010 primarily due to seasonal cash flow paydowns. While the Company adheres to sound underwriting practices, including collateralization of loans, any extended period of low commodity prices, significantly reduced yields on crops and/or reduced levels of government assistance to the agricultural industry could result in an increase in the level of problem agriculture loans and potentially result in loan losses within the agricultural portfolio.

In addition, the Company has $48.9 million of loans to motels and hotels. The performance of these loans is dependent on borrower specific issues as well as the general level of business and personal travel within the region. While the Company adheres to sound underwriting standards, a prolonged period of reduced business or personal travel could result in an increase in nonperforming loans to this business segment and potentially in loan losses. The Company also has $87.8 million of loans to lessors of non-residential buildings and $45.9 million of loans to lessors of residential buildings and dwellings.

The allowance for loan losses represents the Company's best estimate of the reserve necessary to adequately account for probable losses existing in the current portfolio. The provision for loan losses is the charge against current earnings that is determined by the Company as the amount needed to maintain an adequate allowance for loan losses. In determining the adequacy of the allowance for loan losses, and therefore the provision to be charged to current earnings, the Company relies predominantly on a disciplined credit review and approval process that extends to the full range of the Company's credit exposure. The review process is directed by the overall lending policy and is intended to identify, at the earliest possible stage, borrowers who might be facing financial difficulty. Once identified, the magnitude of exposure to individual borrowers is quantified in the form of specific allocations of the allowance for loan losses. The Company considers collateral values and guarantees in the determination of such specific allocations. Additional factors considered by the Company in evaluating the overall adequacy of the allowance include historical net loan losses, the level and composition of nonaccrual, past due and troubled debt restructurings, trends in volumes and terms of loans, effects of changes in risk selection and underwriting standards or lending practices, lending staff changes, concentrations of credit, industry conditions and the current economic conditions in the region where the Company operates.

The Company estimates the appropriate level of allowance for loan losses by separately evaluating large impaired loans, large adversely classified loans and nonimpaired loans.

Impaired loans. The Company individually evaluates certain loans for impairment. In general, these loans have been internally identified via the Company's loan grading system as credits requiring management's attention due to underlying problems in the borrower's business or collateral concerns. This evaluation considers expected future cash flows, the value of collateral and also other factors that may impact the borrower's ability to make payments when due. For loans greater than $100,000 in the commercial, commercial real estate, agricultural, agricultural real estate segments, impairment is individually measured each quarter using one of three alternatives: (1) the present value of expected future cash flows discounted at the loan's effective interest rate; (2) the loan's observable market price, if available; or (3) the fair value of the collateral less costs to sell for collateral dependent loans and loans for which foreclosure is deemed to be probable. A specific allowance is assigned when expected cash flows or collateral do not justify the carrying amount of the loan. The carrying value of the loan reflects reductions from prior charge-offs.

Adversely classified loans. A detailed analysis is also performed on each adversely classified (substandard or doubtful rated) borrower with an aggregate, outstanding balance of $100,000 or more. This analysis includes commercial, commercial real estate, agricultural, and agricultural real estate borrowers who are not currently identified as impaired but pose sufficient risk to warrant in-depth review. Estimated collateral shortfalls are then calculated with allocations for each loan segment based on the five-year historical average of collateral shortfalls adjusted for environmental factors including changes in economic conditions, changes in credit policies or underwriting standards, and changes in the level of credit risk associated with specific industries and markets. Because the economic and business climate in any given industry or market, and its impact on any given borrower, can change rapidly, the risk profile of the loan portfolio is periodically assessed and adjusted when appropriate.

Non-classified and Watch loans. For loans, in all segments of the portfolio, that are considered to possess levels of risk commensurate with a pass rating, management establishes base loss estimations which are derived from the historical loss experience over the past five years. Use of a five-year historical loss period eliminates the effect of any significant losses that can be attributed to a single event or borrower during a given reporting period. The base loss estimations for each loan segment are adjusted after consideration of several environmental factors influencing the level of credit risk in the portfolio. In addition, loans rated as watch are further segregated in the commercial / commercial real estate and agricultural / agricultural real estate segments. These loans possess potential weaknesses that, if go unchecked, may result in deterioration to the point of becoming a problem asset. Due to the elevated risk inherent in these loans, an allocation of twice the adjusted base loss estimation of the applicable loan segment is determined appropriate.

Due to weakened economic conditions during recent years, the Company established allocations for each of the loan segments at levels above the base loss estimations. Some of the economic factors included the potential for reduced cash flow for commercial operating loans from reduction in sales or increased operating costs, decreased occupancy rates for commercial buildings, reduced levels of home sales for commercial land developments, the uncertainty regarding grain prices and increased operating costs for farmers, and increased levels of unemployment and bankruptcy impacting consumer’s ability to pay. Each of these economic uncertainties was taken into consideration in developing the level of the reserve.

The Company has not materially changed any aspect of its overall approach in the determination of the allowance for loan losses. However, on an on-going basis the Company continues to refine the methods used in determining management’s best estimate of the allowance for loan losses.

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The following tables present the balance in the allowance for loan losses and the recorded investment in loans based on portfolio segment and impairment method for the three and six months ended June 30, 2011 and 2010 and for the year ended December 31, 2010 (in thousands):

	Three months ended						
	June 30, 2011						June 30, 2010
	Commercial/ Commercial Real Estate	Agricultural/ Agricultural Real Estate	Residential Real Estate	Consumer	Unallocated	Total	Total
Allowance for loan losses:							
Balance, beginning of year	$8,737	$ 360	$ 448	$403	$703	$10,651	$9,529
Provision charged to expense	377	196	63	14	266	916	1,083
Losses charged off	(877)	-	(49)	(40)	-	(966)	(582)
Recoveries	75	-	-	19	-	94	35
Balance, end of period	$8,312	$ 556	$ 462	$396	$969	$10,695	$10,065
Ending balance:							
Individually evaluated for impairment	$661	$ -	$ -	$-	$-	$661	$657
Collectively evaluated for impairment	$7,651	$ 556	$ 462	$396	$969	$10,034	$9,408
Loans acquired with deteriorated credit quality	$-	$ -	$ -	$-	$-	$-	$-
Loans:							
Ending balance	$466,332	$ 109,788	$ 186,522	$17,471	$20,379	$800,492	$804,581
Ending balance:							
Individually evaluated for impairment	$7,411	$ 1,149	$ -	$-	$-	$8,560	$9,986
Collectively evaluated for impairment	$458,921	$ 108,639	$ 186,522	$17,471	$20,379	$791,932	$794,595
Loans acquired with deteriorated credit quality	$-	$ -	$ -	$-	$-	$-	$-

Six months ended

	June 30, 2011						June 30, 2010
	Commercial/ Commercial Real Estate	Agricultural/ Agricultural Real Estate	Residential Real Estate	Consumer	Unallocated	Total	Total
Allowance for loan losses:							
Balance, beginning of year	$8,307	$ 404	$ 440	$392	$850	$10,393	$9,462
Provision charged to expense	1,468	152	84	33	119	1,856	1,843
Losses charged off	(1,569)	-	(63)	(76)	-	(1,708)	(1,318)
Recoveries	106	-	1	47	-	154	78
Balance, end of period	$8,312	$ 556	$ 462	$396	$969	$10,695	$10,065
Ending balance:							
Individually evaluated for impairment	$661	$ -	$ -	$-	$-	$661	$657
Collectively evaluated for impairment	$7,651	$ 556	$ 462	$396	$969	$10,034	$9,408
Loans acquired with deteriorated							