

COMMUNITY BUILDING THROUGH COMMUNITY BANKING





financial group, inc.

www.foresightfg.com



STATE BANK *of* **DAVIS**



German American

S·T·A·T·E B·A·N·K

Traditional Banking ... Lifetime Solutions

State Bank

Freeport, IL



LENA STATE BANK

Dear Shareholders,

Your company completed its first 25 years in business in 2011 in an operating environment few of the company's organizers would have imagined. Yet, it is the fundamental philosophies of community banking embraced by those wise local citizens that provided the model Foresight Financial Group has followed to successfully manage through the myriad of changes that has occurred in the economy and banking industry the past 25 years. Their philosophical foundation of having individual bank charters, with local boards and decision makers serving as committed financial stewards working together with like minded community bankers through the changing dynamics of balancing the collective interests of **Customers, Communities, Shareholders, and Team Members**, has provided the means to successfully pursue our mission of **Community Building Through Community Banking** while many others have failed.

Customers have benefitted over the years from industry-wide adoption of convenient technology driven electronic products and services, with payments evolving from unwieldy paper checks to debit cards and automated bill payment. Banking using the internet and mobile phones was likely not envisioned 25 years ago when the banking industry had over 15,000 institutions. Industry consolidation driven by regulatory and economic changes has reduced that number to 7,357 at the end of 2011, with 813 of those institutions still on the FDIC's problem list after nearly 400 bank failures, when only six years ago there were less than a handful of banks on that problem list. Home mortgage loan interest rates have dropped the past 25 years from double digits to currently as low as 3% for a 15 year fixed rate loan. These stunning facts are an outcome of years of regulatory, technological, and economic change, including the great recession of 2008 that was precipitated by the Wall Street banks' credit and liquidity crisis. Those banks brought the confidence crisis upon themselves by engaging in unsound practices that included abuses in sub-prime mortgages, check "bounce protection" programs, and credit card and auto loan securitizations that community banks, including the Foresight group, chose to avoid as not in their customers' best interests. **Communities** cannot prosper when **Customers'** interests are compromised.

The following points from Foresight's history, along with charts on the next pages, are illustrative of the soundness of the fundamental philosophies put in place from the beginning, along with the prudent stewardship of our local boards of directors, and careful execution of sound community banking management practices by our executives and **Team Members** over our 25 year journey working cooperatively together:

- Organizational growth from 2 banks with \$45 million in assets with 14 employees to 5 banks with \$885 million in assets with over 190 employees;
- Pooling of resources to consolidate "back-room" operations, technology, financial, capital, and audit and compliance support that has reduced the relative cost of operating (based on asset size) by over 50% over the years, with operating overhead cost performance consistently significantly better than 80% of our peers for the past decade;
- Sharing of lending expertise and capacity, with shared loans between the Foresight Bank group reaching \$210 million at year end 2011, and a combined legal lending limit of \$21.7 million, up from less than \$1 million in 1986; this has supported **Customers and Communities**.
- Profitability that has been consistently above peers, with continuous dividend payments to **Shareholders** despite the impact of the great recession, with a 25 year growth in book value per share of common stock of over 2,000%;
- Rewarding careers for our **Team Members** nearly one third of whom have had over 20 years experience at community banks, most of which with the Foresight group.

We appreciate your recognition and support of these fundamental philosophies as we rely upon them as the basis to navigate the future changes and challenges of the next 25 years of **Community Building Through Community Banking** in our chosen markets. We think they have stood the test of time.

The 25th year of operations in 2011 was again challenged by the lingering effects of the great recession, as local unemployment improved slightly from 14% to 12%, and the national economy grew 2-3%, despite significant political turmoil in the U.S. and world-wide. Local real estate markets, both residential and commercial are still extremely weak, although manufacturing is improving, and agriculture is on a high note. With interest rates very low and even declining further during 2011, the Foresight banks were able to improve profits again despite the ongoing burden of high credit costs. For the year net income increased 12.9% to \$6,568,000 from \$5,815,000 in 2010. This was just short of our record earnings year in 2007 of \$6,591,000. Return on assets of 76 basis points was much better than peer group average of 53 basis points. Nationwide in 2011, 15% of all banks were still not profitable.

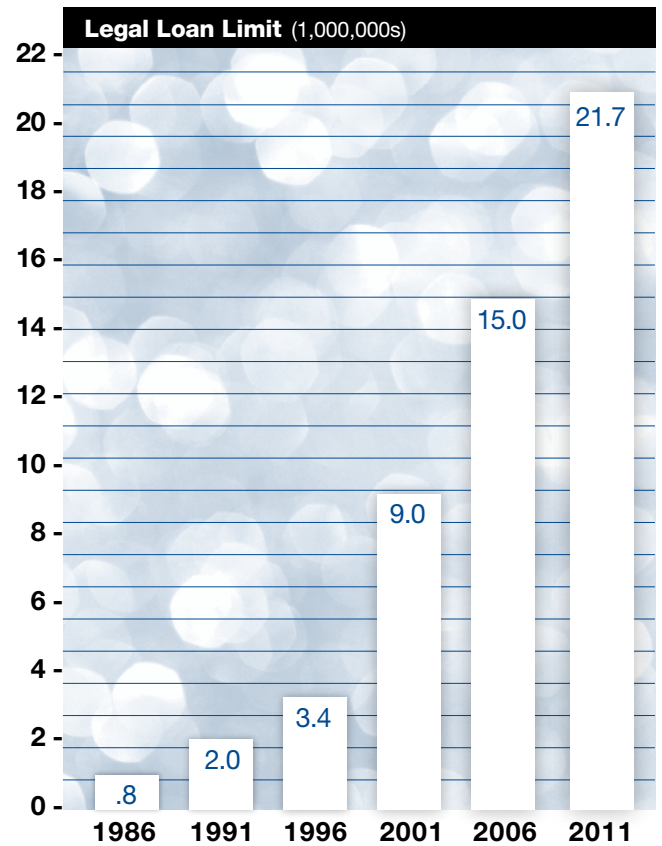
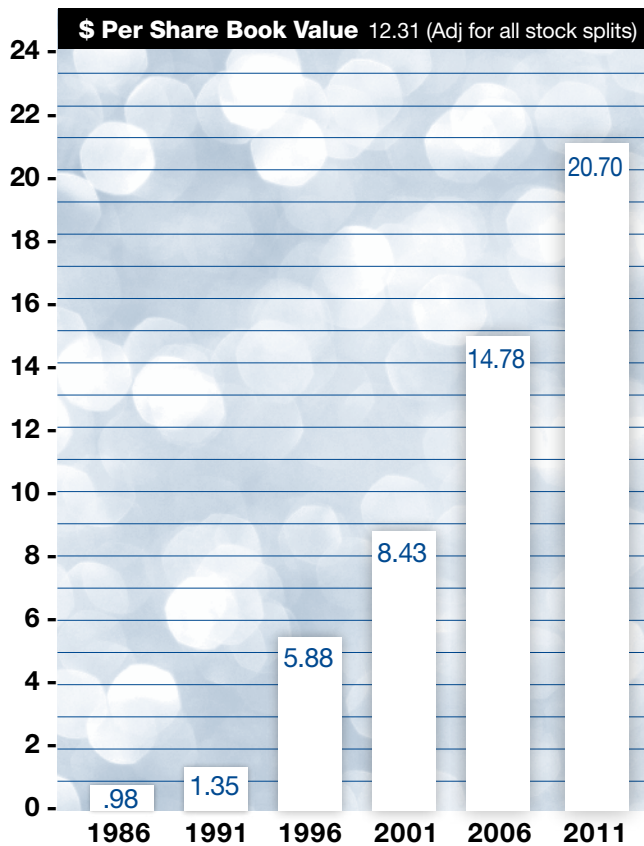
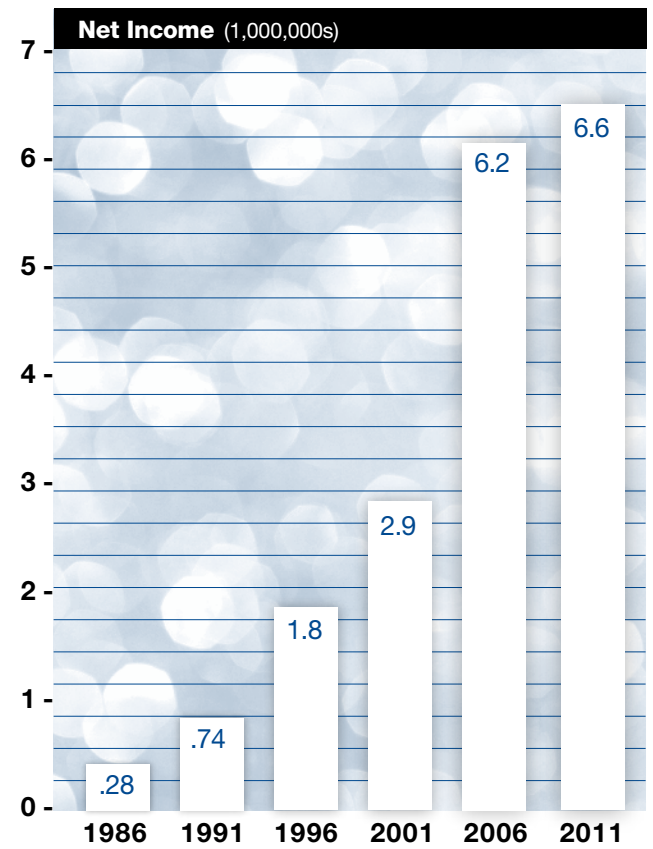
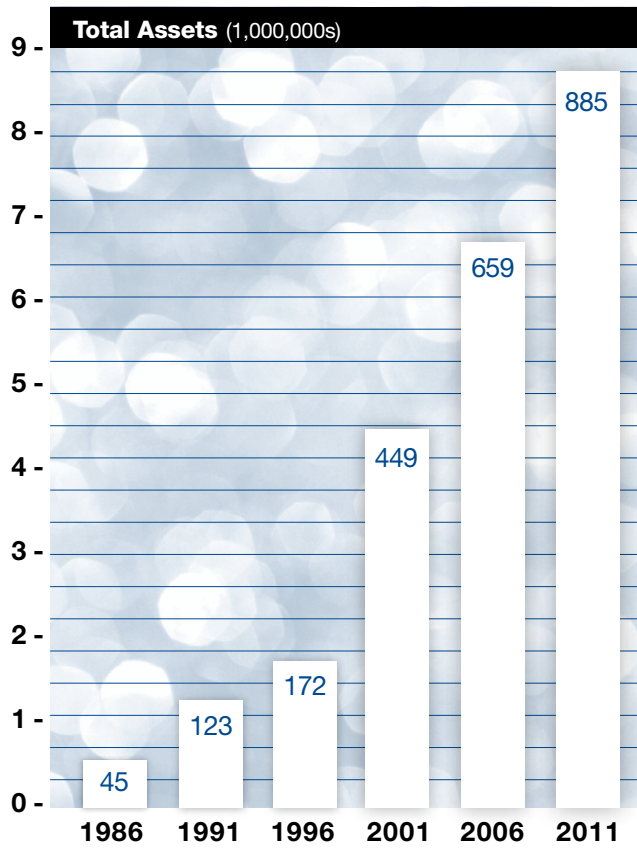
The Foresight Banks improved net income in 2011 with careful management of net interest income, which increased \$3.3 million (up 11.7%), and of noninterest overhead costs, which increased less than 2%. For a third consecutive year, the Foresight banks achieved positive loan growth (up 3.2% in 2011), while peer group banks averaged a 3% decline in loan volume. Credit costs including expense related to foreclosed assets remained burdensome, reaching \$9.96 million, up 5% from \$9.51 million in 2010. The level of non-accrual loans and foreclosed real estate did decline from \$23 million to \$19 million during 2011, but remain the biggest obstacle to the company along with the depressed real estate markets

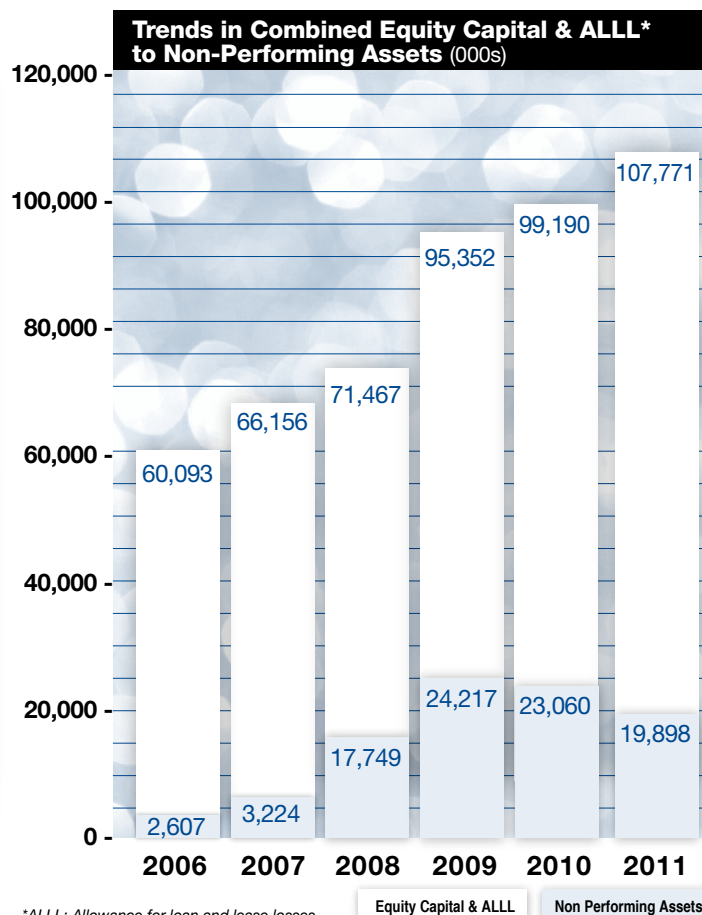
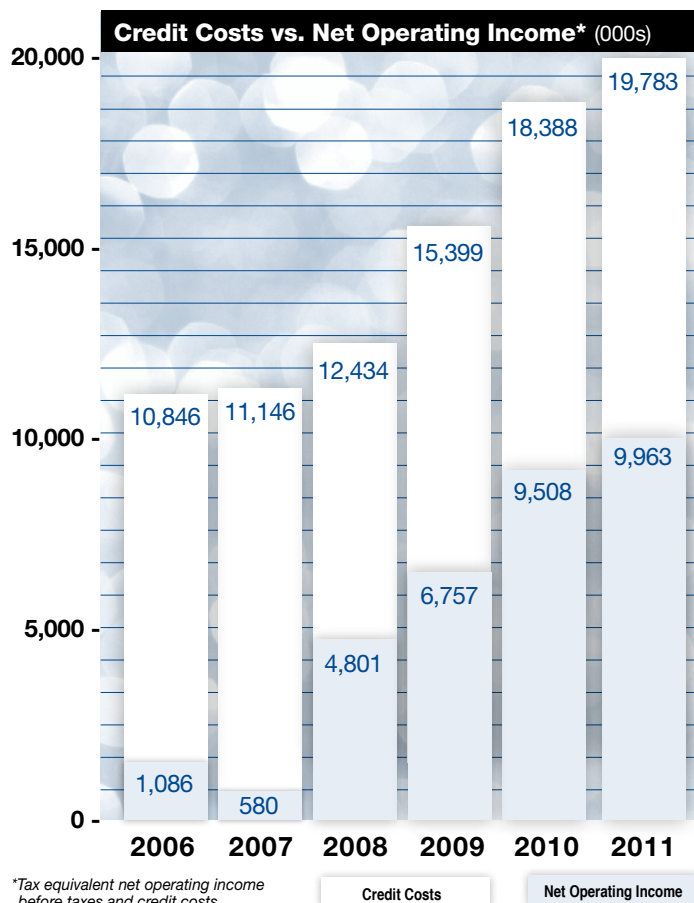
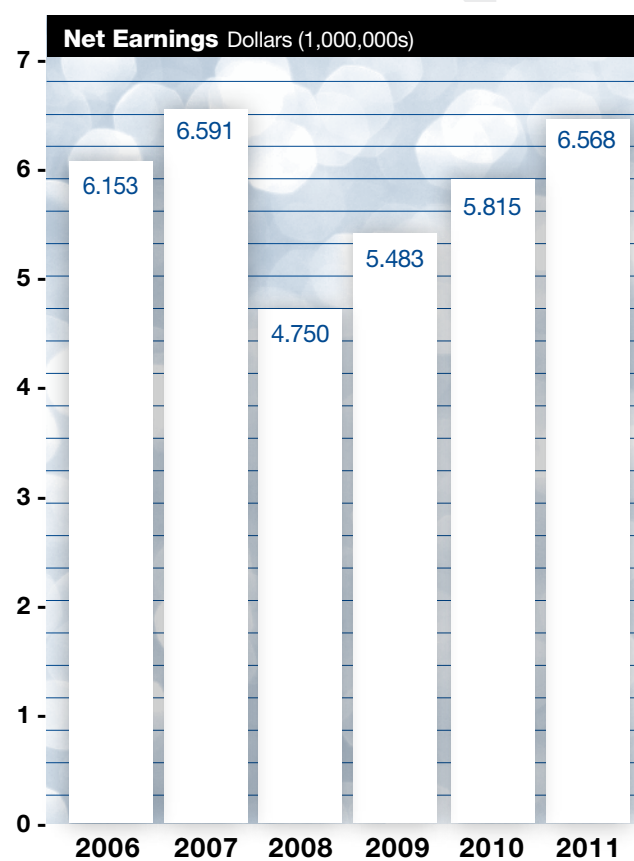
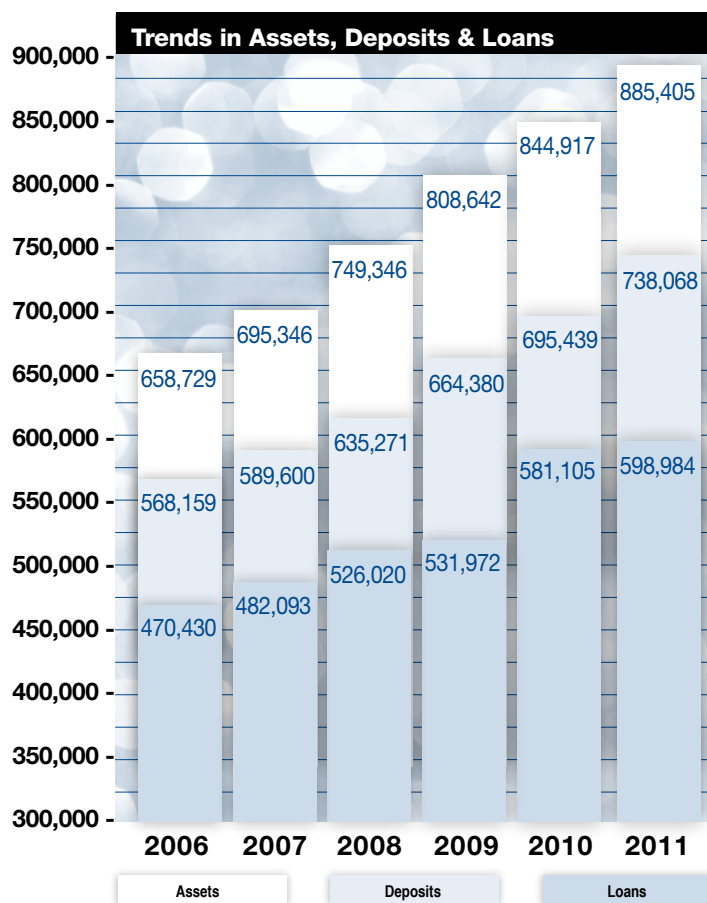
Foresight's total risk based capital remains very strong at 15.06%, and we are working toward building further upon the \$6 million in cash we hold to begin repayment of the \$15.75 redemption value of our TARP Capital in a significant amount by year end 2012. Asset quality will be the determining factor of how much progress can be made. Significant additional pages in the footnotes to the auditors' report this year discloses much more detail than in past years, as regulations and accounting principles have further addressed this important area to enhance transparency of bank financial statements. We see the restoration of asset quality to closer to pre-recession levels as the trigger for TARP repayment, and we believe for significant improvement in the market trading price of our common stock as well, from year end 2011 at \$12.10 per share, which was up over 17% from \$10.30 at the end of 2010. We appreciate your ongoing support of our mission of **Community Building Through Community Banking!**

Respectfully and Gratefully,



Stephen G. Gaddis, President and CEO





*Tax equivalent net operating income before taxes and credit costs.

*ALLL: Allowance for loan and lease losses



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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
 Foresight Financial Group, Inc.

We have audited the accompanying consolidated balance sheets of Foresight Financial Group, Inc. and Subsidiaries as of December 31, 2011 and 2010, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. The consolidated statements of income, changes in stockholders' equity and cash flows of Foresight Financial Group, Inc. and Subsidiaries for the year ended December 31, 2009 were audited by Lindgren, Callihan, Van Osdol & Co., Ltd., whose practice was acquired by Wipfli LLP as of October 1, 2010 and whose report dated March 1, 2010 expressed an unqualified opinion on those statements.

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 consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated 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 Foresight Financial Group, Inc. and Subsidiaries as of December 31, 2011 and 2010, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information included in Schedules 1 and 2 is presented for purposes of additional analyses and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.



Sterling, Illinois
 March 7, 2012

CONSOLIDATED BALANCE SHEETS
(000s omitted except share data)

December 31,	ASSETS	2011	2010
	Cash and due from banks	\$17,121	\$12,676
	Interest-bearing deposits in banks	8,396	829
	Federal funds sold	0	4,988
	Total cash and cash equivalents	25,517	18,493
	Securities:		
	Securities held-to-maturity (HTM)	2,042	2,597
	Securities available-for-sale (AFS)	221,634	202,100
	Non-marketable equity securities, at cost	2,177	2,053
	Loans held for sale	2,198	1,179
	Loans, net of allowance for loan losses of \$11,173 and \$12,165, respectively	598,984	581,105
	Foreclosed assets, net	5,997	7,408
	Premises and equipment, net	10,115	10,443
	Other assets	16,741	19,539
	Total assets	\$885,405	\$844,917
	LIABILITIES AND STOCKHOLDERS' EQUITY		
	Liabilities:		
	Deposits:		
	Noninterest-bearing	\$82,036	\$62,146
	Interest-bearing	656,032	633,293
	Total deposits	738,068	695,439
	Federal funds purchased	3,899	2,084
	Securities sold under agreements to repurchase	27,698	26,327
	Federal Home Loan Bank (FHLB) advances and other borrowings	14,400	29,700
	Accrued interest payable and other liabilities	4,742	4,342
	Total liabilities	788,807	757,892
	Stockholders' equity:		
	Preferred stock (no par value; authorized 500,000 shares; 15,750 shares issued)	15,394	15,244
	Common stock (\$.25 par value; authorized 5,000,000 shares; 3,867,129 and 3,866,794 shares issued, respectively)	966	966
	Additional paid-in capital	7,666	7,568
	Retained earnings	71,193	66,179
	Treasury stock, at cost (207,657 shares)	(4,060)	(4,060)
	Accumulated other comprehensive income	5,439	1,128
	Total stockholders' equity	96,598	87,025
	Total liabilities and stockholders' equity	\$885,405	\$844,917

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF INCOME
(000s omitted except share data)

For the years ended December 31,

	2011	2010	2009
Interest and dividend income:			
Loans, including fees	\$33,830	\$32,209	\$31,848
Debt securities:			
Taxable	3,915	4,642	5,498
Tax-exempt	3,900	4,061	3,444
Interest-bearing deposits in banks	16	36	32
Federal funds sold	11	7	15
Total interest and dividend income	41,672	40,955	40,837
Interest expense:			
Deposits	9,313	11,832	15,267
Federal funds purchased	7	13	9
Securities sold under agreements to repurchase	167	180	139
FHLB and other borrowings	341	418	715
Total interest expense	9,828	12,443	16,130
Net interest and dividend income	31,844	28,512	24,707
Provision for loan losses	7,195	8,382	6,405
Net interest and dividend income, after provision for loan losses	24,649	20,130	18,302
Noninterest income:			
Customer service fees	1,369	1,520	1,553
Gain on sales and calls of AFS securities, net	334	180	437
Gain on sales of loans, net	705	797	855
Loan servicing fees, net	579	777	775
Other	2,367	2,614	2,068
Total noninterest income	5,354	5,888	5,688
Noninterest expenses:			
Salaries and employee benefits	10,540	10,045	9,201
Occupancy expense of premises, net	1,904	1,900	1,918
Outside services	723	699	575
Data processing	959	837	841
Foreclosed assets, net	2,768	1,126	352
Other	4,535	4,835	4,462
Total noninterest expenses	21,429	19,442	17,349
Income before income taxes	8,574	6,576	6,641
Income tax expense	2,006	761	1,158
Net income	\$6,568	\$5,815	\$5,483
Earnings per common share:			
Basic	\$1.53	\$1.32	\$1.36
Diluted	\$1.52	\$1.32	\$1.36

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(000s omitted except share data)

For the years ended December 31,

	Preferred Stock	Common Stock	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income	Total
Balance, January 1, 2009	\$0	\$966	\$7,454	\$58,547	(\$4,060)	\$1,160	<u>\$64,067</u>
Comprehensive income:							
Net income				5,483			5,483
Other comprehensive income -							
Change in unrealized gain on							
securities available-for-sale, net							
of reclassification and tax effect						1,593	<u>1,593</u>
Total comprehensive income							<u>7,076</u>
Cash dividends (\$.32 per share)				(1,174)			(1,174)
Issuance of preferred stock	15,000						15,000
Accretion of preferred stock warrants	94			(94)			0
Cash dividends on preferred stock				(409)			(409)
Stock-based compensation expense			33				33
Balance, December 31, 2009	15,094	966	7,487	62,353	(4,060)	2,753	<u>84,593</u>
Comprehensive income:							
Net income				5,815			5,815
Other comprehensive loss -							
Change in unrealized gain on							
securities available-for-sale, net							
of reclassification and tax effect						(1,625)	<u>(1,625)</u>
Total comprehensive income							<u>4,190</u>
Cash dividends (\$.28 per share)				(1,025)			(1,025)
Accretion of preferred stock warrants	150			(150)			0
Cash dividends on preferred stock				(814)			(814)
Stock-based compensation expense			81				81
Balance, December 31, 2010	15,244	966	7,568	66,179	(4,060)	1,128	<u>87,025</u>
Comprehensive income:							
Net income				6,568			6,568
Other comprehensive income -							
Change in unrealized gain on							
securities available-for-sale, net							
of reclassification and tax effect						4,311	<u>4,311</u>
Total comprehensive income							<u>10,879</u>
Cash dividends (\$.16 per share)				(586)			(586)
Accretion of preferred stock warrants	150			(150)			0
Cash dividends on preferred stock				(818)			(818)
Stock-based compensation expense			98				98
Balance, December 31, 2011	<u>\$15,394</u>	<u>\$966</u>	<u>\$7,666</u>	<u>\$71,193</u>	<u>(\$4,060)</u>	<u>\$5,439</u>	<u>\$96,598</u>

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(000s omitted except share data)

For the years ended December 31,

	2011	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	\$6,568	\$5,815	\$5,483
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Provision for loan losses	7,195	8,382	6,405
Provision for foreclosed asset losses	2,410	900	113
Depreciation	799	741	818
Net amortization (accretion) of securities	974	1,094	230
Deferred income tax benefit	(473)	(822)	(1,251)
Net gain on the sales and calls of AFS securities	(334)	(180)	(437)
Net loss on the sales of foreclosed assets	12	50	113
Stock-based compensation expense	98	81	33
Net change in:			
Servicing rights	8	(251)	(311)
Loans held for sale	(1,019)	(732)	144
Other assets	305	1,016	(3,531)
Accrued expenses and other liabilities	400	259	(689)
Net cash provided by operating activities	16,943	16,353	7,120
CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sales of AFS securities	13,966	14,551	17,736
Proceeds from maturities, calls, and paydowns of HTM securities	606	999	1,520
Proceeds from maturities, calls, and paydowns of AFS securities	48,466	56,977	43,772
Purchases of AFS securities	(75,388)	(52,762)	(110,028)
Purchases of non-marketable equity securities	(124)	(244)	(189)
Loan originations and principal collections, net	(27,693)	(66,113)	(12,931)
Proceeds from sales of foreclosed assets	1,608	810	819
Purchases of premises and equipment, net	(471)	(2,131)	(548)
Net cash used in investing activities	(39,030)	(47,913)	(59,849)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net change in deposits	42,629	31,059	29,109
Net change in securities sold under agreements to repurchase	1,371	1,973	6,507
Cash dividends paid	(1,404)	(1,839)	(1,583)
Net change in federal funds purchased	1,815	(2,648)	3,696
Proceeds from issuance of preferred stock	0	0	15,000
Proceeds from lines of credit and FHLB advances and other borrowings	10,500	19,750	18,250
Payments on lines of credit and FHLB advances and other borrowings	(25,800)	(16,550)	(18,100)
Net cash provided by financing activities	29,111	31,745	52,879
Net increase in cash and cash equivalents	7,024	185	150
Cash and cash equivalents at beginning of year	18,493	18,308	18,158
Cash and cash equivalents at end of year	\$25,517	\$18,493	\$18,308

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
(000s omitted except share data)

For the years ended December 31,

	2011	2010	2009
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SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

Cash paid during the year for:

Interest	\$10,040	\$12,790	\$16,652
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Income taxes	\$2,190	\$1,905	\$1,934
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SUPPLEMENTAL SCHEDULE OF NONCASH AND FINANCING ACTIVITIES:

Foreclosed assets acquired in settlement of loans	\$2,619	\$8,598	\$470
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See Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(1) Summary of Significant Accounting Policies

The accounting and reporting policies of Foresight Financial Group, Inc. (Company) and its wholly owned subsidiaries (Banks) conform to accounting principles generally accepted in the United States of America and to general practices within the banking industry. The following is a description of the more significant accounting policies:

(a) *Nature of Operations*

The Company provides a variety of banking services to individuals and businesses through its facilities in the Rockford, Freeport, German Valley, Davis, Lena, Winnebago, Pecatonica, and Seward, Illinois areas. Its primary deposit products are demand deposits and certificates of deposit and its primary lending products are agribusiness, commercial, real estate, and installment loans.

(b) *Basis of Consolidation*

The consolidated financial statements include the accounts and results of operations of the Company and its wholly owned subsidiaries, German-American State Bank (German), State Bank of Davis (Davis), State Bank (Freeport), Northwest Bank of Rockford (Northwest), and Lena State Bank (Lena) (Banks). All significant intercompany accounts and transactions have been eliminated in consolidation.

(c) *Subsequent Events*

The Company has evaluated subsequent events for recognition and disclosure through March 7, 2012, which is the date the financial statements were available to be issued.

(d) *Use of Estimates*

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 revenues and expenses during the reporting period. Actual results could differ from those estimates. The allowance for loan losses, fair values of securities, fair values of foreclosed assets, deferred tax assets and liabilities and fair values of financial instruments are particularly subject to change in the near-term.

(e) *Cash and Cash Equivalents*

For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash and balances due from banks, interest-bearing deposits in banks, and federal funds sold, all of which generally mature within ninety days. Cash flows from loans, deposits, federal funds purchased, securities sold under agreements to repurchase, and treasury stock are reported net.

(f) *Interest-bearing Deposits in Banks*

Interest-bearing deposits in banks are largely comprised of liquid non-maturing deposits in banks but also include some small balances in time deposits in banks with varying maturities. Interest-bearing deposits in banks are carried at cost.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (000s omitted except share data)

(1) Summary of Significant Accounting Policies (continued)

(g) Securities

Debt securities that management has the positive intent and ability to hold to maturity are classified as held to maturity (HTM) and recorded at amortized cost. Securities not classified as HTM are classified as available for sale (AFS) and recorded at fair value, with unrealized gains or 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. Declines in the fair value of HTM and AFS securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses.

In estimating other-than-temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific-identification method.

(h) Non-Marketable Equity Securities

The Banks, as members of the Federal Home Loan Bank (FHLB) system, are required to maintain a minimum investment in capital stock of the FHLB in an amount equal to the greater of 1% of their mortgage-related assets or 5% of advances from the FHLB. The Banks may choose to invest in amounts greater than the minimum investment. Excess capital stock redemptions are subject to guidelines established by the FHLB. FHLB stock is reported at cost since no ready market exists and it has no quoted market value. FHLB stock is periodically evaluated for impairment based on the ultimate recovery of par value.

(i) Loans Held for Sale

Loans originated and intended for sale in the secondary market are carried at the lower of cost or market in the aggregate.

Mortgage loans held for sale are generally sold with mortgage servicing rights retained by the Company. The carrying value of mortgage loans sold is reduced by the cost allocated to the associated mortgage servicing rights. Gains or losses on sales of mortgage loans are recognized based on the difference between the selling price and the carrying value of the related mortgage loans sold.

(j) Loans and Allowance for Loan Losses

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are stated at the amount of unpaid principal balances less the allowance for loan losses. Interest income is accrued daily on the outstanding balances.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(1) Summary of Significant Accounting Policies (continued)

(j) Loans and Allowance for Loan Losses (continued)

A loan is considered to be delinquent when payments have not been made according to contractual terms, typically evidenced by nonpayment of a monthly installment by the due date. The accrual of interest on loans is discontinued at the time the loan is 90-days delinquent unless the credit is well-secured and in the process of collection. Credit card loans and other personal loans are typically charged off no later than 180-days delinquent. Generally, loans are placed on non-accrual or charged-off at an earlier date if collection of principal or interest is considered doubtful.

Generally, interest accrued but not collected for loans that are placed on nonaccrual status or charged off is 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.

Loan origination fees approximate direct loan origination costs and are generally recognized as income upon receipt.

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

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability 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 specific and general components. The specific component relates to loans that are classified as impaired. For loans that are classified as impaired, an allowance is established when the discounted cash flows, collateral value or observable market price of the impaired loan is lower than the carrying value of that loan. The general component covers non-impaired loans and is based on historical loss experience adjusted for qualitative factors.

A loan is considered impaired when it is probable, based on current information and events, the Bank will be unable to collect all contractual principal and interest payments due in accordance with the terms of the loan agreement. Loans for which the terms have been modified to provide a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Impaired loans are measured on an individual basis based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. The amount of impairment, if any, and subsequent changes are included in the allowance for loan losses. Troubled debt restructurings are measured at the present value of estimated future cash flows using the loan's effective rate at inception, unless collateral dependent, then reported net of the fair value of collateral.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(1) Summary of Significant Accounting Policies (continued)

(j) Loans and Allowance for Loan Losses (continued)

For impaired loans, accrual of interest is discontinued when management believes, after considering collection efforts and other factors, the borrower's financial condition is such that the collection of interest is doubtful. Cash collections on impaired loans are credited to the loan receivable balance, and no interest income is recognized on those loans until the principal balance has been collected.

(k) Loan Commitments

The Banks enter into off-balance-sheet financial instruments consisting of commitments to extend credit and letters of credit issued to meet customer-financing needs. Loan commitments are recorded when they are funded. Standby or performance letters of credit are considered financial guarantees in accordance with accounting standards and are recorded at fair value, if material.

(l) Loan Servicing

Mortgage servicing rights are recognized as separate assets when rights are acquired through a sale of loans and are reported in other assets. When the originating mortgage loans are sold into the secondary market, the Company allocates the total cost of the mortgage loans between mortgage servicing rights and the loans, based on their relative fair values. The cost of originated mortgage-servicing rights is amortized in proportion to, and over the period of, estimated net servicing revenues. Impairment of mortgage-servicing rights is assessed based on the fair value of those rights. The amount of impairment is the amount by which the capitalized mortgage servicing rights exceed their fair value. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions.

Residential mortgage loans are generally sold to the secondary market. At the time the loans are sold, a gain or loss is calculated based on the cash received versus the carrying value of the assets transferred.

Servicing fee income is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income.

(m) Mortgage-Banking Derivatives

Commitments to fund mortgage loans (interest-rate locks) to be sold into the secondary market and mandatory delivery forward commitments for the future delivery of these mortgage loans are to be accounted for as derivatives not qualifying for hedge accounting. The fair values of these mortgage derivatives are to be estimated based on the net future cash flows related to the associated servicing of the loans and on changes in mortgage interest rates from the date of the commitments. Changes in fair values on these derivatives are to be included in net gains on sales of loans. The Company has deemed the effect of these derivatives to be immaterial to the consolidated financial statements and has elected not to record fair values associated with these derivatives.

(n) Foreclosed Assets

Assets acquired through or instead of loan foreclosure are initially recorded at fair value less estimated cost of disposal when acquired. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Costs after acquisition are generally expensed. Revenues and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(1) Summary of Significant Accounting Policies (continued)***(o) Premises and Equipment***

Premises and equipment are carried at cost less accumulated depreciation, based on the estimated useful lives of the assets. Depreciation is generally computed on the straight-line method over estimated useful lives ranging from 3 to 40 years.

(p) Bank-Owned Life Insurance

The Bank has purchased life insurance policies on certain key employees. Bank-owned life insurance is recorded at its cash surrender value, or the amount that can be realized.

(q) Significant Group Concentrations of Credit Risk

Most of the Company's activities are with customers located in the area and communities noted above. Note 3 details the types of securities in which the Company invests. Note 4 details the types of lending in which the Company engages. The Company does not have any significant concentrations with any one industry or customer.

(r) Income Taxes

Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the temporary differences between the book and tax bases of the various balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws. The Company files consolidated Federal and State income tax returns.

The Company may also recognize a liability for unrecognized tax benefits from uncertain tax positions. Unrecognized tax benefits represent the differences between a tax position taken or expected to be taken in a tax return and the benefit recognized and measured in the financial statements. Interest and penalties related to unrecognized tax benefits are classified as income taxes, if applicable. No liabilities for unrecognized tax benefits from uncertain tax positions have been recorded.

(s) Comprehensive Income

Accounting principles generally require the Company to include in net income recognized revenue, expenses, gains and losses. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the balance sheet. Such items, along with net income, are components of comprehensive income.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)**(1) Summary of Significant Accounting Policies (continued)*****(t) Earnings Per Share***

Basic earnings per share (EPS) represent income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted EPS reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate solely to outstanding stock options and are determined using the treasury stock method. The dividends on preferred stock and the accretion of the preferred warrants are subtracted from net income in arriving at the net income available to common stockholders.

(u) Loss Contingencies

Loss contingencies, including claims and legal actions arising from time to time in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there now are such matters that could have a material effect on the consolidated financial statements.

(v) Transfers of Financial Assets

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

(w) Trust Assets

Assets of the trust department of State Bank, other than trust cash on deposit at the Bank, are not included in these financial statements because they are not assets of the Company.

(x) Securities Sold Under Agreements to Repurchase

Securities sold under agreements to repurchase liabilities represent amounts advanced by various customers. Securities are pledged to cover these liabilities, which are not covered by federal deposit insurance.

(y) Stock Compensation Plans

The Company records the cost of stock-based employee compensation using the fair-value method. Compensation expense for share-based awards is recorded over the vesting period at the fair value of the award at the time of grant. The Company has historically assumed no projected forfeitures on its stock based compensation, since forfeitures have not been significant.

(z) Reclassifications

Certain amounts in the 2010 consolidated financial statements have been reclassified to conform to the 2011 presentation.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(1) Summary of Significant Accounting Policies (continued)***(aa) Adoption of New Accounting Standards***

In July 2010, the FASB issued new accounting guidance for disclosures about the credit quality of loans and the allowance for loan losses. The primary purpose of this new guidance is to provide additional information to assist financial statement users in assessing the Company's credit risk exposures and evaluating the adequacy of its allowance for loan losses. This new accounting standard is effective for financial statements issued for annual periods ending after December 15, 2011. The Company adopted this new accounting standard effective December 31, 2011.

(ab) Newly Issued Not Yet Effective Accounting Standards

In April 2011, the FASB issued new accounting guidance impacting a creditor's determination of whether a restructuring is a troubled debt restructuring. The primary purpose of this new guidance is to provide additional clarity in determining whether a restructuring constitutes a troubled debt restructuring. This new accounting standard is effective for financial statements issued for annual periods ending after December 15, 2012. The Company is evaluating the impact this standard will have on the financial statements of the Company.

(2) Cash and Due From Banks

The Banks are required to maintain reserve balances, in cash or on deposit with the Federal Reserve Bank, based upon a percentage of deposits. The total required reserve balances as of December 31, 2011 and 2010 was approximately \$2,900 and \$2,232, respectively.

In the normal course of business, the Banks maintain cash and due from bank balances in non-interest-bearing transaction accounts with correspondent banks. Balances in these accounts are temporarily guaranteed by the FDIC through December 31, 2012.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(3) Securities

The following tables reflect the amortized costs and approximate fair values of securities at December 31:

Held-to-Maturity 2011	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
State and municipal	\$2,042	\$77	(\$9)	\$2,110

Held-to-Maturity 2010	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
State and municipal	\$2,597	\$34	(\$72)	\$2,559

Available-for-Sale 2011	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Government sponsored agencies	\$43,836	\$903	(\$9)	\$44,730
State and municipal	99,179	5,830	(205)	104,804
Mortgage-backed – residential	69,513	2,640	(53)	72,100
	\$212,528	\$9,373	(\$267)	\$221,634

Available-for-Sale 2010	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Government sponsored agencies	\$36,224	\$634	(\$139)	\$36,719
State and municipal	96,295	1,075	(2,269)	95,101
Mortgage-backed - residential	67,744	2,604	(68)	70,280
	\$200,263	\$4,313	(\$2,476)	\$202,100

For the years ended December 31, 2011, 2010 and 2009, proceeds from sales of available-for-sale securities amounted to \$13,966, \$14,551 and \$17,736, respectively. Gross realized gains and losses from the sales and calls of available-for-sale securities for the years ended December 31 are as follows:

	2011	2010	2009
Realized gains	\$368	\$257	\$440
Realized losses	(\$34)	(\$77)	(\$3)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(3) Securities (continued)

Securities with carrying amounts of approximately \$101,632 and \$100,674 at December 31, 2011 and 2010, respectively, were pledged to secure public deposits and for other purposes as required or permitted by law.

The amortized costs and fair values of securities at December 31, 2011 are shown below by contractual maturities, except for U.S. agencies which are shown by contractual maturities or their expected call dates if the call dates are considered likely to occur based on present market conditions. Expected maturities may differ from contractual maturities on mortgage-backed securities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Held-to-Maturity	Amortized Cost	Fair Value
Due in one year or less	\$128	\$132
Due after one year through five years	554	561
Due after five years through ten years	392	420
Due after ten years	968	997
	\$2,042	\$2,110

Available-for-Sale	Amortized Cost	Fair Value
Due in one year or less	\$25,962	\$26,189
Due after one year through five years	24,838	25,738
Due after five years through ten years	26,698	28,111
Due after ten years	65,517	69,496
	143,015	149,534
Mortgage-backed - residential	69,513	72,100
	\$212,528	\$221,634

The following tables show the fair values and unrealized losses aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2011 and 2010:

	2011					
	Held-to-Maturity					
	Less than 12 Months			12 Months or More		
	Gross Unrealized Fair Value	No. of Loss	No. of Securities	Gross Unrealized Fair Value	No. of Loss	No. of Securities
State and municipal	\$285	\$1	1	\$145	\$8	2
Total temporarily impaired	\$285	\$1	1	\$145	\$8	2

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(3) Securities (continued)

	2010					
	Held-to-Maturity					
	Less than 12 Months			12 Months or More		
	Fair Value	Gross Unrealized Loss	No. of Securities	Fair Value	Gross Unrealized Loss	No. of Securities
State and municipal	\$342	\$17	2	\$258	\$55	3
Total temporarily impaired	\$342	\$17	2	\$258	\$55	3

	2011					
	Available-for-Sale					
	Less than 12 Months			12 Months or More		
	Fair Value	Gross Unrealized Loss	No. of Securities	Fair Value	Gross Unrealized Loss	No. of Securities
U.S. Government sponsored agencies	\$2,749	\$9	9	\$0	\$0	0
State and municipal	2,401	26	18	1,203	179	10
Mortgage-backed - residential	8,537	53	14	0	0	0
Total temporarily impaired	\$13,687	\$88	41	\$1,203	\$179	10

	2010					
	Available-for-Sale					
	Less than 12 Months			12 Months or More		
	Fair Value	Gross Unrealized Loss	No. of Securities	Fair Value	Gross Unrealized Loss	No. of Securities
U.S. Government sponsored agencies	\$7,884	\$139	26	\$0	\$0	0
State and municipal	49,925	1,831	195	1,722	438	17
Mortgage-backed - residential	5,519	68	10	0	0	0
Total temporarily impaired	\$63,328	\$2,038	231	\$1,722	\$438	17

Unrealized losses on securities have not been recognized into income because the bonds are of high credit quality, management has the intent and ability to hold for the foreseeable future and the decline in fair value is largely due to market interest rate fluctuations and current bond markets. The fair value is expected to recover as the bonds approach their maturity dates and/or market rates. The unrealized losses on the remaining securities have not been recognized into income because the bonds are of high credit quality and management has the intent and ability to hold for the foreseeable future.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(4) Loans

The following table presents total loans at December 31 by portfolio segment and class of loan:

	2011	2010
Real estate:		
Commercial real estate	\$173,480	\$164,029
Agricultural real estate	60,229	57,802
Consumer real estate	128,210	133,139
Commercial:		
Commercial & industrial	183,844	177,249
Agricultural production	48,589	39,865
Consumer and other	15,805	21,186
	610,157	593,270
Allowance for loan losses	(11,173)	(12,165)
	\$598,984	\$581,105

The following is a summary of the activity in the allowance for loan losses for the years ended December 31:

	2011	2010	2009
Balance at beginning of year	\$12,165	\$10,759	\$7,400
Provision charged to operations, net	7,195	8,362	6,405
Recoveries on loans previously charged-off	286	442	95
	19,646	19,563	13,900
Less loans charged-off	(8,473)	(7,398)	(3,141)
Balance at end of year	\$11,173	\$12,165	\$10,759

Detailed analysis of the allowance for loan losses by portfolio segment for the year ended December 31, 2011 follows:

	Real Estate	Commercial	Consumer	Total
Balance at beginning of year	\$7,331	\$4,594	\$240	\$12,165
Provision charged to operations, net	5,888	1,376	(69)	7,195
Recoveries on loans previously charged-off	124	97	65	286
	13,343	6,067	236	19,646
Less loans charged-off	(6,127)	(2,231)	(115)	(8,473)
Balance at end of year	\$7,216	\$3,836	\$121	\$11,173
Allowance for loan losses:				
Individually evaluated for impairment	\$2,934	\$812	\$8	\$3,754
Collectively evaluated for impairment	4,282	3,024	113	7,419
Totals	\$7,216	\$3,836	\$121	\$11,173

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(4) Loans (continued)

Detailed analysis of loans evaluated for impairment by portfolio segment for the year ended December 31, 2011 follows:

	Real Estate	Commercial	Consumer	Total
Loans:				
Individually evaluated for impairment	\$28,256	\$5,398	\$190	\$33,844
Collectively evaluated for impairment	333,663	227,035	15,615	576,313
Totals	\$361,919	\$232,433	\$15,805	\$610,157

The following is a summary of information pertaining to impaired and non-accrual loans as of December 31:

	2011	2010
Impaired loans without a valuation allowance	\$21,562	\$6,440
Impaired loans with a valuation allowance	12,282	16,375
Total impaired loans	\$33,844	\$22,815
Valuation allowance related to impaired loans	\$3,754	\$3,922
Total non-accrual loans	\$13,622	\$13,622
Average balance of impaired loans	\$27,283	\$26,920
Total loans past-due 90-days or more and still accruing	\$279	\$2,030

Interest income and other loan income recognized on impaired loans during 2011, 2010, and 2009 approximated \$1,183, \$347, and \$260, respectively. The Banks have no commitments to loan additional funds to the borrowers of impaired or non-accrual loans.

Detailed information regarding impaired loans by class of loan for the year ended December 31, 2011 follows:

	Recorded Investment	Principal Balance	Related Allowance	Average Investment	Interest Recognized
Loans with no related allowance for loan losses:					
Real estate:					
Commercial real estate	\$9,557	\$10,163	N/A	\$6,965	\$227
Residential real estate	7,543	8,535	N/A	6,086	227
Farm real estate	295	295	N/A	215	0
Commercial					
Commercial & industrial	4,037	5,039	N/A	4,086	176
Agricultural production	0	0	N/A	0	0
Consumer and other	130	130	N/A	131	9
Total	21,562	24,162		17,483	639

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(4) Loans (continued)

Detailed information regarding impaired loans by class of loan for the year ended December 31, 2011 follows (continued):

	Recorded Investment	Principal Balance	Related Allowance	Average Investment	Interest Recognized
Loans with an allowance for loan losses:					
Real estate:					
Commercial real estate	3,402	3,448	714	2,489	149
Residential real estate	7,459	8,072	2,220	6,211	339
Farm real estate	0	0	0	0	0
Commercial					
Commercial & industrial	998	1,015	472	771	54
Agricultural production	363	363	340	267	0
Consumer and other	60	99	8	62	2
Total	12,282	12,997	3,754	9,800	544
Grand Total	\$33,844	\$37,159	\$3,754	\$27,283	\$1,183

The Company regularly evaluates various attributes of loans to determine the appropriateness of the allowance for loan losses. The Company generally monitors credit quality indicators for all loans using the following internally prepared ratings:

'Pass' ratings are assigned to loans with adequate collateral and debt service ability such that collectibility of the contractual loan payments is highly probable.

'Special Mention' ratings are assigned to loans where management has some concern that the collateral or debt service ability may not be adequate, though the collectibility of the contractual loan payments is still probable.

'Substandard' ratings are assigned to loans that do not have adequate collateral and/or debt service ability such that collectibility of the contractual loan payments is no longer probable.

'Doubtful' ratings are assigned to loans that do not have adequate collateral and/or debt service ability, and collectibility of the contractual loan payments is unlikely.

Information regarding the credit quality indicators most closely monitored by class of loan for the year ended December 31, 2011 follows:

	Pass	Special Mention	Substandard	Doubtful	Totals
Real estate:					
Commercial estate	\$157,749	\$7,762	\$7,969		\$173,480
Residential	111,061	6,511	10,547	\$91	128,210
Farm real estate	56,606	3,328	295		60,229
Commercial:					
Commercial & industrial	164,626	14,699	4,444	75	183,844
Agricultural production	48,058	168	304	59	48,589
Consumer and other	15,519	97	189		15,805
Total	\$553,619	\$32,565	\$23,748	\$225	\$610,157

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(4) Loans (continued)

Loan aging information by class of loan for the year ended December 31, 2011 follows:

	Loans Past Due 30-89 Days	Loans Past Due 90+ Days	Total Past Due
Real estate:			
Commercial real estate	\$539	\$5,184	\$5,723
Residential real estate	908	6,274	7,182
Farm real estate		295	295
Commercial			
Commercial & industrial	259	1,329	1,588
Agricultural production		304	304
Consumer and other	101	121	222
Total	\$1,807	\$13,507	\$15,314

	Total Past Due	Total Current	Total Loans	90+ Days Due and Accruing Interest	Total Non-accrual Loans
Real Estate:					
Commercial estate	\$5,723	\$167,757	\$173,480		\$5,519
Residential real estate	7,182	121,028	128,210	\$224	6,050
Farm real estate	295	59,934	60,229		295
Commercial:					
Commercial & industrial	1,588	182,256	183,844	5	1,324
Agricultural production	304	48,285	48,589		363
Consumer and other	222	15,583	15,805	50	71
Total	\$15,314	\$594,843	\$610,157	\$279	\$13,622

When, for economic or legal reasons related the borrower's financial difficulties, the Company grants a concession to the borrower that the Company would not otherwise consider, the modified loan is classified as a troubled debt restructuring. Loan modifications may consist of forgiveness of interest and/or principal, a reduction of the interest rate, interest only payments for a period of time, and/or extending amortization terms. All troubled debt restructurings are classified as impaired loans. The following table presents information regarding modifications of loans that are classified as troubled debt restructurings by class of loan during the year ended December 31, 2011:

	Number of Loans	Pre-Modification Investment	Post-Modification Investment
Real Estate:			
Commercial real estate	13	\$8,535	\$8,177
Residential real estate	60	9,646	9,646
Farm real estate	0		
Commercial			
Commercial & industrial	7	3,585	2,440
Agricultural production	0		
Consumer and Other	1	7	7
Total	81	\$21,773	\$20,270

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(4) Loans (continued)

The following table summarizes troubled debt restructurings that defaulted during the year ended December 31, 2011, within 12 months of their modification date.

	Number of Loans	Recorded Investment
Real Estate:		
Commercial real estate	2	\$1,270
Residential real estate	6	1,038
Total	8	\$2,308

(5) Loan Servicing

Loans serviced for others are not included in the accompanying consolidated balance sheets. Mortgage loans serviced for others as of December 31, 2011 and 2010, were approximately \$249,326 and \$235,528, respectively. Custodial escrow balances maintained in conjunction with serviced loans were approximately \$1,910 and \$1,905 at December 31, 2011 and 2010, respectively.

The following summarizes the activity pertaining to mortgage servicing rights for the years ended December 31:

	2011	2010	2009
Mortgage servicing rights:			
Balance at beginning of year	\$1,529	\$1,277	\$970
Mortgage servicing rights capitalized	643	970	1,174
Mortgage servicing rights amortized	(651)	(718)	(867)
Balance at end of year	\$1,521	\$1,529	\$1,277

The approximate fair values of the mortgage servicing rights were deemed to be greater than their carrying values as of December 31, 2011, 2010, and 2009. The differences between the fair values and carrying values were considered immaterial.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(6) Mortgage Banking Loan Commitments

The Company enters into commitments to fund residential mortgage loans (interest rate locks) at specified times in the future, with the intention that these loans will be subsequently sold to third-party investors. A mortgage loan commitment binds the Company to lend funds to a potential borrower at a specified interest rate and within a specified period of time, generally up to 60-days after inception of the rate lock. It is the Company's practice to enter into mandatory delivery forward commitments for the future delivery of residential mortgage loans to third-party investors when an interest rate lock commitment is granted. These mandatory delivery forward commitments bind the Company to deliver a residential mortgage loan to a third-party investor even if the underlying loan never funds. As of December 31, 2011 and 2010, the Company had approximately \$4,055 and \$706 in interest rate lock commitments outstanding. As of December 31, 2011 and 2010, the Company had approximately \$7,053 and \$706 in mandatory delivery forward commitments outstanding. These outstanding mortgage loan commitments are considered to be derivatives. The fair values associated with these derivatives were considered to be immaterial as of December 31, 2011 and 2010.

(7) Allowance for Losses on Foreclosed Assets

Foreclosed assets are presented in the balance sheets net of an allowance for losses. Activity in the allowance for losses on foreclosed assets for the years ended December 31, was as follows:

	2011	2010	2009
Balance at beginning of year	\$910	\$20	\$0
Provision for losses	2,410	900	20
Charge-offs	0	10	0
Recoveries	0	0	0
Balance at end of year	\$3,320	\$910	\$20

(8) Premises and Equipment

The components of premises and equipment at December 31 are as follows:

	2011	2010
Land	\$1,969	\$2,049
Buildings and leasehold improvements	10,726	10,593
Furniture, fixtures, and equipment	9,057	8,650
	21,752	21,292
Less accumulated depreciation	11,637	10,849
	\$10,115	\$10,443

Depreciation expense for the years ended December 31, 2011, 2010 and 2009 amounted to \$799, \$741, and \$818, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(9) Other Assets

The components of other assets at December 31 are as follows:

	2011	2010
Cash surrender value of bank-owned life insurance	\$4,933	\$4,759
Accrued interest receivable	5,341	5,644
Mortgage servicing rights, net of amortization	1,521	1,529
Net deferred tax assets	1,098	3,583
Federal Deposit Insurance Corporation assessments	1,910	2,531
Other	1,938	1,493
	\$16,741	\$19,539

(10) Time Deposits

The aggregate amount of time deposits with minimum a denomination of \$100 was approximately \$143,916 and \$154,686 at December 31, 2011 and 2010, respectively.

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

2012	\$206,798
2013	90,013
2014	45,371
2015	29,996
2016 and thereafter	27,917
	\$400,095

(11) Dividends

State banking regulations restrict the amount of dividends that a bank may pay to its stockholders. The regulations provide that dividends are limited to the balance of undivided profits, subject to capital-adequacy requirements, plus an additional amount equal to the bank's current-year earnings through the date of any declaration of dividends. Additionally, dividends are limited under the terms of the TARP agreement as described in Note 23.

(12) Employee Benefit Plans

The Company and the Banks maintain a 401(k) plan with profit sharing features covering substantially all employees under which they match 50% of eligible employee contributions to a maximum employee contribution of 6% of annual salary. Total 401(k) expense was approximately \$247, \$237, and \$206, for 2011, 2010, and 2009, respectively. Each plan participant elects how the employer contributions are invested. Participants choose between purchasing the Company's common stock and investing in the plan's investment funds.

In addition, Northwest, German-American, and Lena maintain salary-continuation plans whereby certain officers are provided with guaranteed annual payments for periods ranging from ten to thirteen years after reaching a retirement age of 65. The salary-continuation plans are funded by whole life insurance policies purchased by the Banks which had an aggregate death benefit of approximately \$8,961 and \$8,943 as of December 31, 2011 and 2010, respectively (see Note 9 for cash surrender value of bank-owned life insurance). The Banks accrue for the total amounts to be paid over the employee's active service life. The accrued benefits were \$894, \$912, and \$963 at December 31, 2011, 2010, and 2009, respectively. Salary-continuation expenses were \$51, \$48, and \$47 in 2011, 2010, and 2009, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(13) Income Taxes

The components of income tax expense (benefit) for the years ended December 31 are as follows:

	2011	2010	2009
Current – federal	\$1,623	\$1,140	\$1,854
– state	857	443	555
	2,480	1,583	2,409
Deferred – federal	(144)	(752)	(1,091)
– state	(330)	(70)	(160)
	(474)	(822)	(1,251)
Total income tax expense	\$2,006	\$761	\$1,158

A reconciliation of the differences between the statutory federal income tax rate and the effective federal income tax rate with the resulting dollar amounts is shown in the following table:

	2011		2010		2009	
	Amount	% of Pretax Earnings	Amount	% of Pretax Earnings	Amount	% of Pretax Earnings
Statutory federal tax	\$2,915	34.0%	\$2,236	34.0%	\$2,258	34.0%
Increase (decrease) in taxes resulting from:						
Tax-exempt interest	(1,452)	(16.9%)	(1,518)	(23.1%)	(1,318)	(19.8%)
Bank-owned life insurance	(63)	(0.7%)	(346)	(5.3%)	(164)	(2.5%)
State taxes, net of federal benefit	348	4.1%	246	3.7%	260	3.9%
Other	258	3.0%	143	2.2%	122	1.8%
Effective tax rates	\$2,006	23.5%	\$761	11.5%	\$1,158	17.4%

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(13) Income Taxes (continued)

The tax effects of existing temporary differences that give rise to significant portions of the deferred tax liabilities and deferred tax assets at December 31, 2011 and 2010 are summarized as follows:

	2011	2010
Deferred tax assets:		
Allowance for loan losses	\$4,358	\$4,744
Allowance for losses on foreclosed assets and non-accrual interest	1,396	435
Deferred compensation and other	562	642
Total gross deferred tax assets	6,316	5,821
Deferred tax liabilities:		
FHLB stock dividend	129	129
Security accretion	35	34
Available-for-sale securities	3,666	708
Tax depreciation in excess of book depreciation	788	772
Mortgage servicing rights and other	600	595
Total gross deferred tax liabilities	5,218	2,238
Net deferred tax assets	\$1,098	\$3,583

No valuation allowance has been recorded since deferred tax assets are expected to be realized.

With few exceptions, the Company is no longer subject to federal or state examinations by tax authorities for years before 2009.

(14) Transactions with Related Parties

The Company and subsidiary banks have had, and may be expected to have in the future, loans or other banking transactions in the ordinary course of business with directors, significant stockholders, principal officers, their immediate families, and affiliated companies in which they are principal stockholders (commonly referred to as related parties). In management's opinion, these loans and transactions were on the same terms as those for comparable loans and transactions with non-related parties.

Loans to related parties amounted to approximately \$14,209 and \$10,637 at December 31, 2011 and 2010, respectively.

Deposit accounts from related parties totaled approximately \$10,612 and \$8,647 at December 31, 2011 and 2010, respectively.

(15) Financial Instruments with Off-Balance-Sheet Risk and Commitments

Financial instruments with off-balance-sheet risk:

The Banks are parties to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of their customers. These financial instruments include commitments to extend credit, credit lines, letters of credit, and overdraft protection. They involve, to varying degrees, elements of credit risk in excess of amounts recognized on the consolidated balance sheets.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(15) Financial Instruments with Off-Balance-Sheet Risk and Commitments (continued)

Financial instruments with off-balance-sheet risk (continued):

The Banks' exposures to credit losses in the event of nonperformance by the other parties to the financial instruments, for commitments to extend credit, and letters of credit are represented by the contractual amounts of those instruments. The Banks use the same credit policies in making commitments and issuing letters of credit as they do for on-balance-sheet instruments.

A summary of the contractual amounts of the Banks' exposure to off-balance-sheet risk as of December 31 is approximately as follows:

	2011	2010
Unused lines of credit and other loan commitments	\$123,099	\$112,593
Commercial letters of credits	1,352	808
Performance and standby letters of credit	761	475
	\$125,212	\$113,876

Commitments to extend credit are agreements to lend to customers as long as there are no violations of any conditions established in the contracts. Commitments generally have fixed expiration dates or other termination clauses and may require the 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 credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Banks evaluate each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Banks upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, crops, livestock, property and equipment, residential real estate, and income-producing commercial properties.

Standby, performance and commercial letters of credit are conditional commitments issued by the Banks to guarantee the performance of a customer to a third party. They are considered financial guarantees under FASB guidance. The fair value of these financial guarantees is considered immaterial.

Concentration of credit risk:

The Company and its subsidiary banks provide several types of loans to customers including real estate, agricultural, commercial, and installment loans. The largest component of loans is secured by residential real estate, commercial real estate, or other interest in real property. Lending activities are conducted with customers in a wide variety of industries as well as with individuals with a wide variety of credit requirements. The Company does not have a concentration of loans in any specific industry. Credit risk, as it relates to the Company's business activities, tends to be geographically concentrated in that the majority of the customer base lies within the surrounding communities served by its subsidiary banks.

(16) Securities Sold Under Agreements to Repurchase

Securities sold under agreements to repurchase amounted to \$27,698 and \$26,327 at December 31, 2011 and 2010, respectively, and are secured by investment securities with fair values of approximately \$37,563 and \$34,449. The weighted-average interest rates on these agreements were 0.54% and 0.76% at December 31, 2011 and 2010, respectively. Securities sold under agreements to repurchase mature on a daily basis.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(17) Federal Home Loan Bank (FHLB) Advances and Other Borrowings

<i>FHLB:</i>	2011	2010
Fixed-rate advances with rates ranging from .98% to 3.16% with weighted-average rates of 1.82% and 1.32% as of December 31, 2011 and 2010, respectively. Interest is payable monthly with principal due at maturity.	\$14,400	\$29,200
Variable-rate advances with weighted-average rates of .58% as of December 31, 2010. Interest was payable monthly with principal due at maturity.	0	500
	\$14,400	\$29,700

Advances are collateralized by 1-4 family mortgage loans and other qualifying loans. The total amounts of collateral securing FHLB advances were approximately \$86,879 and \$90,624 as of December 31, 2011 and 2010, respectively.

The Banks participate in the Federal Reserve Bank of Chicago's Discount Window Lending Program. Primary advances generally mature daily and bear interest at a general approved rate in relation to the federal funds rate. The primary advance interest rate at December 31, 2011 was 75-basis points. Outstanding advances were \$0 at December 31, 2011 and 2010. Advances are secured by investment securities pledged to the Federal Reserve Bank.

At December 31, 2011, the scheduled maturities of Federal Home Loan Bank advances and other borrowings are as follows:

	2011	2010
2011	\$0	\$19,300
2012	3,050	3,050
2013	4,600	4,600
2014	2,750	1,750
2015	2,500	1,000
2016	1,500	0
	\$14,400	\$29,700

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(18) Fair Value Measurements

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the Company has the ability to access as of the measurement date.

Level 2: Significant other 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.

Level 3: Significant unobservable inputs that reflect the Company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The following is a description of valuation methodologies used for assets recorded at fair value:

Securities available-for-sale: The fair values of the Company's securities available-for-sale are primarily determined by matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities. The values determined by matrix pricing are considered Level 2 fair value measurements.

Collateral-dependent impaired loans: The Company does not record loans at fair value on a recurring basis. However, from time to time, fair value adjustments are recorded on these loans to reflect (1) partial write-downs, through charge-offs or specific reserve allowances, that are based on the current appraised or market-quoted value of the underlying collateral or (2) the full charge-off of the loan carrying value. In some cases, the properties for which market quotes or appraised values have been obtained are located in areas where comparable sales data is limited, outdated, or unavailable. Fair-value estimates for collateral-dependent impaired loans are obtained from real-estate brokers or other third-party consultants. The values determined are considered Level 3 fair value measurements.

Foreclosed assets: Periodic valuation adjustments to certain commercial and residential and real estate properties classified as foreclosed assets are measured at the lower of carrying amount or fair value, less selling costs. Fair values are generally based on third party appraisals of the property, resulting in a Level 3 classification. In cases where the carrying amount exceeds the fair value, less costs to sell, an impairment loss is recognized.

Mortgage servicing rights: Loan servicing rights are initially recorded at approximate fair value and are subsequently measured using the amortization method which requires servicing rights to be amortized into non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying loans. The values determined are considered Level 3 fair value measurements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(18) Fair Value Measurements (continued)

The following table presents the Company's approximate fair-value hierarchy for the assets measured at fair value as of December 31:

As of December 31, 2011	Fair Value Measurements at Reporting Date Using			
	Total	(Level 1)	(Level 2)	(Level 3)
Assets measured at fair value on a recurring basis:				
Assets:				
Securities available-for-sale	\$221,634		\$221,634	
Assets measured at fair value on a non-recurring basis:				
Assets:				
Collateral-dependent impaired loans	\$8,528			\$8,528
Foreclosed assets	\$5,997			\$5,997
Mortgage servicing rights	\$1,521			\$1,521
As of December 31, 2010	Fair Value Measurements at Reporting Date Using			
	Total	(Level 1)	(Level 2)	(Level 3)
Assets measured at fair value on a recurring basis:				
Assets:				
Securities available-for-sale	\$202,100		\$202,100	
Assets measured at fair value on a non-recurring basis:				
Assets:				
Collateral-dependent impaired loans	\$12,453			\$12,453
Foreclosed assets	\$7,408			\$7,408
Mortgage servicing rights	\$1,529			\$1,529

Collateral-dependent impaired loans, which are measured for impairment using the fair value of collateral, had a carrying value of \$12,282 and \$16,375, with specific reserves of \$3,754 and \$3,922 as of December 31, 2011 and 2010, respectively.

Foreclosed assets, which are measured at the lower of carrying or fair value less costs to sell, had a carrying amount of \$5,997 and \$7,408, which is comprised of the outstanding balance of \$9,317 and \$8,318, net of an allowance for losses of \$3,320 and \$910 as of December 31, 2011 and 2010, respectively.

FASB guidance requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates may not be realized in immediate settlement of the instrument. Accounting guidance excludes certain financial instruments and certain nonfinancial instruments from its disclosure requirements. These fair value disclosures may not represent the fair value of the Company.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(18) Fair Value Measurements (continued)

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and cash equivalents: The carrying amounts are reasonable estimates of fair value.

Securities: See previous description in this footnote for securities available-for-sale. The fair values of the Company's securities held-to-maturity are primarily determined by matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities.

Non-marketable equity securities: No ready market exists for the equity securities as they have no quoted market value. The carrying amount of equity securities approximates its fair value.

Loans held for sale: The fair values of loans held for sale are based on commitments on hand from investors or prevailing market prices.

Loans: For variable-rate loans that re-price frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. For fair value estimates for collateral-dependent impaired loans, see previous description in this footnote.

Deposits: The fair values disclosed for demand deposits, savings accounts, and certain money market deposits are, by definition, equal to the amount payable on demand at the reporting date (carrying amounts). Fair values for certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Federal funds purchased and securities sold under agreements to repurchase: The carrying amounts of federal funds and securities sold under agreements to repurchase approximate fair value.

FHLB advances: The fair value of FHLB advances was estimated using discounted cash flow analyses based on the Company's current incremental borrowing rates for similar types of borrowing arrangements.

Other borrowings: The carrying amounts of other borrowings approximate their fair value.

Accrued interest: The carrying amounts of accrued interest approximate their fair value.

Off-balance-sheet financial instruments: No estimated fair value is attributable to unused lines of credit and letters of credit as they are deemed immaterial.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(18) Fair Value Measurements (continued)

The estimated fair values of the Company's financial instruments as of December 31 are as follows:

	December 31, 2011		December 31, 2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and cash equivalents	\$25,517	\$25,517	\$18,493	\$18,493
Securities	223,676	223,744	204,697	204,659
Non-marketable equity securities	2,177	2,177	2,053	2,053
Loans held for sale	2,198	2,198	1,179	1,179
Loans, net of allowance	598,984	601,258	581,105	580,991
Accrued interest receivable	5,341	5,341	5,644	5,644
Financial liabilities:				
Deposits	\$738,068	\$741,822	\$695,439	\$700,045
Federal funds purchased	3,899	3,899	2,084	2,084
Securities sold under agreements to repurchase	27,698	27,716	26,327	26,336
FHLB advances and other borrowings	14,400	14,716	29,700	29,809
Accrued interest payable	1,186	1,186	1,415	1,415

(19) Stock-Compensation Plans

The Company has entered into non-qualified and incentive stock option agreements whereby shares of common stock were made available for purchase by certain executive officers. All incentive and non-qualified options have been issued pursuant to various shareholder approved stock option plans. In May of 2008, the stockholders' approved an additional 100,000 shares of common stock be made available for future purchase by certain officers. Under these agreements, the exercise price of each option equals the market price of the Company's stock on the grant date. The options' maximum terms are ten years. The options vest under a three, five or seven year period after the date of grant. The Company's general practice is to use previously authorized but unissued shares of common stock to satisfy stock option exercises. Currently, the Company has a sufficient number of authorized common shares to satisfy expected stock option exercises, but treasury stock may also be used.

The fair value of each option award is estimated on the date of grant using a closed form option valuation (Black-Scholes) model that uses the assumptions noted in the table below. Expected volatilities are based on historical volatilities of the Company's common stock. The Company uses historical data to estimate option exercise and post-vesting termination behavior. The expected term of options granted is based on historical data and represents the period of time that options granted are expected to be outstanding, which takes into account that the options are not transferable. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield in effect at the time of the grant.

The fair value of each option granted was determined using the following assumptions as of grant date:

	2011	2010	2009
Risk-free interest rate	1.23%-2.23%	1.23%-6.00%	2.72%-6.00%
Expected option life	10	10	10
Expected stock-price volatility	29.4%-36.8%	12.7%-37.0%	12.7%-22.0%
Dividend yield	1.56%-3.20%	0.53%-1.75%	0.53%-1.75%
Intrinsic value of options exercised	\$4	\$3	N/A
Weighted average fair value of options granted	N/A	\$2.90	N/A

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(19) Stock-Compensation Plans (continued)

For the years ended December 31, 2011, 2010 and 2009, the Company recognized \$98, \$81 and \$33 in compensation expense for stock options, respectively. No tax benefits were recognized for the three year period ended December 31, 2011. As of December 31, 2011, stock-based compensation expense not yet recognized totaled \$341, and is expected to be recognized over a weighted-average remaining period of 2.3 years. The total fair value of shares vested during the years ended December 31, 2011, 2010 and 2009 was \$338, \$90 and \$70, respectively.

During 2010, the Company modified the exercise price on 49,760 fully and partially vested incentive stock options outstanding affecting thirteen employees. The options were originally granted in 2004, 2005 and 2008 and represented a weighted average exercise price of \$19.57 per share. As a result of the modification, the weighted average exercise price on the modified options was reduced to \$10.43 per share. Consistent with generally accepted accounting principles, the Company revaluated the fair value of the modified options resulting in additional compensation expense of \$75 to be recognized over the remaining vesting period. For the modified options already fully vested, the Company recognized the additional compensation expense in 2010. The fair value of the stock options granted in 2008, 2005 and 2004 were revised from \$5.08, \$12.55 and \$9.37 per share, respectively as originally reported to modified fair values of \$7.21, \$14.08, and \$10.74 per share, respectively.

The following tables summarize the activity of options and non-vested shares granted, exercised, or forfeited for the year ended December 31, 2011:

	2011	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Shares under option, beginning of year	193,090	\$10.63	7.07	\$13
Granted during the year	0			
Forfeited and canceled during the year	(26,710)	11.91		
Exercised during the year	(8,850)	12.25		\$4
Shares under option, end of year	157,530	\$10.32	7.4	\$280
Options exercisable, end of year	56,274	\$10.43	5.91	\$94
Shares available for grant, end of year	0			

	Number of Options	Weighted Average Fair Value at Grant
Non-vested options, December 31, 2010	130,480	\$10.26
Granted during the year	0	
Vested during the year	(27,964)	10.24
Forfeited or expired during the year	(1,260)	11.91
Non-vested options, December 31, 2011	101,256	\$10.26

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(19) Stock-Compensation Plans (continued)

The exercise of 8,850 and 2,117 stock options in 2011 and 2010, respectively, involved a like-kind exchange of 8,515 and 1,860 shares, respectively, of the Company's common stock valued at the current market value on the date of exercise plus additional cash. This like-kind exchange resulted in the issuance of 335 and 257 additional shares of common stock, respectively.

The following table summarizes information about fixed stock options outstanding at December 31, 2011:

Exercise Price	Number Outstanding at 12/31/11	Remaining Contractual Life (Years)	Number Exercisable at 12/31/11
\$10.00	26,500	6.0	15,900
\$10.25	93,320	8.5	18,664
\$10.50	20,000	8.5	4,000
\$11.00	8,030	3.5	8,030
\$11.00	9,680	2.5	9,680
	157,530		56,274

(20) Earnings Per Common Share

For the years ended December 31, earnings per common share have been computed based on the following:

	2011	2010	2009
Net income	\$6,568	\$5,815	\$5,483
Less - preferred stock dividends	(818)	(818)	(409)
Less - accretion of preferred stock warrants	(150)	(150)	(94)
Net income available to common stockholders	\$5,600	\$4,847	\$4,980
Average number of common shares outstanding	3,659,306	3,659,058	3,658,880
Effect of dilutive options	26,162	1,216	0
Average number of common shares outstanding used to calculate diluted earnings per common share	3,685,468	3,660,274	3,658,880

The total outstanding options of common stock which were excluded in the computation of diluted earnings per common share for the years ended 2011, 2010 and 2009 were 0, 71,170 and 99,530, respectively because they were considered anti-dilutive.

(21) Regulatory Matters

The Company and Banks are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital-adequacy guidelines and the regulatory framework for prompt corrective action, the Company and Banks must meet specific capital guidelines that involve quantitative measures of the assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(000s omitted except share data)

(21) Regulatory Matters (continued)

Quantitative measures established by regulation to ensure capital adequacy require the Company and its subsidiaries to maintain minimum amounts and ratios (set forth in the following table) of total and Tier-I capital (as defined in the regulations) to risk-weighted assets, and of Tier-I capital to average assets. Management believes that as of December 31, 2011, that the Company and the Banks meet all capital-adequacy requirements to which they are subject.

As of December 31, 2011, the most recent notifications from the Federal Deposit Insurance Corporation (FDIC) categorized all five Banks as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, minimum total risk-based, Tier-I risk-based, and Tier-I leverage ratios as set forth in the table must be maintained. There are no conditions or events occurring since the FDIC notified each Bank which management believes have changed the categories of the Banks.

The actual capital amounts and ratios for the Company and Banks as of December 31 are presented in the following tables:

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount In \$000s	Ratio	Amount In \$000s	Ratio	Amount In \$000s	Ratio
As of December 31, 2011:						
Total Capital to Risk Weighted Assets:						
Company	\$99,291	15.06%	\$52,727	8.00%	N/A	N/A
Northwest	23,655	12.68%	14,927	8.00%	\$18,659	10.00%
German	18,941	12.50%	12,120	8.00%	15,150	10.00%
Davis	13,271	13.51%	7,857	8.00%	9,822	10.00%
Freeport	21,160	12.88%	13,142	8.00%	16,428	10.00%
Lena	9,008	17.27%	4,173	8.00%	5,216	10.00%
Tier-I Capital to Risk Weighted Assets:						
Company	\$91,018	13.81%	\$26,364	4.00%	N/A	N/A
Northwest	21,316	11.42%	7,463	4.00%	\$11,195	6.00%
German	17,036	11.24%	6,060	4.00%	9,090	6.00%
Davis	12,038	12.26%	3,929	4.00%	5,893	6.00%
Freeport	19,100	11.63%	6,571	4.00%	9,857	6.00%
Lena	8,351	16.01%	2,086	4.00%	3,129	6.00%
Tier-I Capital to Average Assets:						
Company	\$91,018	10.30%	\$35,354	4.00%	N/A	N/A
Northwest	21,316	8.65%	9,852	4.00%	\$12,316	5.00%
German	21,316	8.82%	7,728	4.00%	9,660	5.00%
Davis	12,038	8.62%	5,587	4.00%	6,984	5.00%
Freeport	19,100	8.83%	8,651	4.00%	10,814	5.00%
Lena	8,351	10.30%	3,243	4.00%	4,053	5.00%

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(21) Regulatory Matters (continued)

As of December 31, 2010:

Total Capital to Risk						
Weighted Assets:						
Company	\$93,715	14.81%	\$50,614	8.00%	N/A	N/A
Northwest	22,236	12.49%	14,238	8.00%	\$17,798	10.00%
German	17,539	12.48%	11,245	8.00%	14,057	10.00%
Davis	12,430	13.35%	7,449	8.00%	9,312	10.00%
Freeport	19,027	11.89%	12,798	8.00%	15,998	10.00%
Lena	8,757	16.64%	4,210	8.00%	5,263	10.00%
Tier-I Capital to Risk						
Weighted Assets:						
Company	\$85,756	13.55%	\$25,307	4.00%	N/A	N/A
Northwest	19,983	11.23%	7,119	4.00%	\$10,679	6.00%
German	15,778	11.22%	5,623	4.00%	8,434	6.00%
Davis	11,261	12.09%	3,725	4.00%	5,587	6.00%
Freeport	17,021	10.64%	6,399	4.00%	9,599	6.00%
Lena	8,095	15.38%	2,105	4.00%	3,158	6.00%
Tier-I Capital to						
Average Assets:						
Company	\$85,756	10.14%	\$33,832	4.00%	N/A	N/A
Northwest	19,983	8.39%	9,524	4.00%	\$11,905	5.00%
German	15,778	8.82%	7,157	4.00%	8,946	5.00%
Davis	11,261	8.71%	5,173	4.00%	6,466	5.00%
Freeport	17,021	8.42%	8,087	4.00%	10,108	5.00%
Lena	8,095	10.01%	3,236	4.00%	4,045	5.00%

(22) Other Comprehensive Income (Loss)

Other comprehensive income components and related taxes for the years ended December 31 were as follows:

	2011	2010	2009
Holding gains (losses) on securities available-for-sale	\$7,603	(\$2,459)	\$3,029
Less reclassification adjustments for gains recognized in income	(334)	(180)	(437)
Net unrealized gains (losses)	7,269	(2,639)	2,592
Deferred tax effect	(2,958)	1,014	(999)
Other comprehensive income (loss)	\$4,311	(\$1,625)	\$1,593

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(000s omitted except share data)

(23) TARP Capital Purchase Plan (in actual dollars)

On May 15, 2009, as part of the United States Treasury Department's (UST) Troubled Asset Relief Program (TARP) Capital Purchase Program, the Company issued 15,000 shares of fixed rate cumulative perpetual preferred stock (Series A preferred stock) to the UST for total proceeds of \$15,000,000. The Series A preferred stock has no par value and a redemption value of \$1,000 per share. The UST also received warrants to purchase 750 shares of fixed rate cumulative preferred stock (Series B preferred stock) for an exercise price of \$.01 per share. The UST immediately exercised the warrants. The Series B preferred stock has no par value and a redemption value of \$1,000 per share. The Series A and Series B preferred stock are redeemable by the Company at any time. The dividend rate on the Series A preferred stock is 5% for the first five years and 9% thereafter. The dividend rate on the Series B preferred stock is 9%. Dividends on the preferred stock are cumulative and are payable quarterly in arrears on the 15th of February, May, August and November. The redemption value of the 750 shares of Series B preferred stock is being accreted as an increase to preferred stock over five years which is the Company's expected redemption period. The Series A and Series B preferred stock is included as Tier-1 capital for regulatory purposes.

Under the terms of the TARP agreement, the Company is subject to certain dividend limitations. Generally, without the UST's consent, the Company is limited to a maximum quarterly dividend of \$.08 per common share until May 14, 2012. Additionally, without the UST's consent, the Company is limited to a maximum dividend of 103% of the aggregate per share dividends of the prior fiscal year for the period from May 15, 2012 to May 14, 2019. Subsequent to May 14, 2019, without the UST's consent, the Company may not pay a dividend until the Series A and Series B preferred stock is redeemed.

Additionally under the terms of the TARP agreement, without the consent of the UST, the Company generally may not acquire additional shares of treasury stock, except in connection with the administration of any employee benefit plan in the ordinary course of business and consistent with past practice. The TARP agreement also places certain restrictions on executive compensation, the effect of which has not had a material effect on the consolidated financial statements.

CONSOLIDATING SCHEDULE 1 - BALANCE SHEET
(000s omitted except share data)

December 31, 2011

ASSETS	German-American State Bank	State Bank of Davis
Cash and due from banks	\$3,063	\$1,818
Interest-bearing deposits in banks	263	2,030
Federal funds sold		0
Securities:		
Securities held-to-maturity		1,976
Securities available-for-sale	45,312	37,354
Non-marketable equity securities, at cost	534	306
Loans held for sale		
Loans, net	141,577	90,938
Foreclosed assets, net	70	312
Premises and equipment	1,237	929
Other assets	3,871	1,293
Investment in subsidiary banks		
Total assets	\$195,927	\$136,956
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Deposits:		
Noninterest bearing	\$15,606	\$12,195
Interest-bearing	154,484	102,148
Total deposits	170,090	114,343
Federal funds purchased	3,303	596
Securities sold under agreements to repurchase		7,870
Federal Home Loan Bank borrowings and other	3,500	750
Accrued interest payable and other liabilities	1,028	377
Total liabilities	177,921	123,936
Stockholders' equity:		
Preferred stock		
Common stock	400	100
Additional paid-in capital	2,737	1,547
Retained earnings	13,899	10,391
Treasury stock		
Accumulated other comprehensive income	970	982
Total stockholders' equity	18,006	13,020
Total liabilities and stockholders' equity	\$195,927	\$136,956

Northwest Bank	State Bank	Lena State Bank	Foresight Financial Group, Inc.	Eliminations	Consolidated Total
\$6,829	\$4,126	\$1,285	\$6,940	(\$6,940)	\$17,121
2,242	2,605	1,256			8,396
0	0	0			0
66					2,042
48,847	58,186	31,935			221,634
636	448	253			2,177
2,198					2,198
173,353	148,210	44,621	285		598,984
1,453		156	4,006		5,997
4,783	1,944	486	736		10,115
5,566	1,863	2,598	1,550		16,741
			83,279	(83,279)	
\$245,973	\$217,382	\$82,590	\$96,796	(\$90,219)	\$885,405
\$32,442	\$19,148	\$6,382		(\$3,737)	\$82,036
179,222	156,979	66,402		(3,203)	656,032
211,664	176,127	72,784		(6,940)	738,068
	0				3,899
5,760	14,068				27,698
4,000	6,150	0			14,400
1,904	615	620	\$198		4,742
223,328	196,960	73,404	198	(6,940)	788,807
			15,394		15,394
1,450	1,000	500	966	(3,450)	966
5,120	4,550	3,670	7,666	(17,624)	7,666
14,745	13,550	4,181	71,193	(56,766)	71,193
			(4,060)		(4,060)
1,330	1,322	835	5,439	(5,439)	5,439
22,645	20,422	9,186	96,598	(83,279)	96,598
\$245,973	\$217,382	\$82,590	\$96,796	(\$90,219)	\$885,405

For the year ended December 31, 2011

	German-American State Bank	State Bank of Davis
Interest and dividend income:		
Loans, including fees	\$7,883	\$5,002
Securities:		
Taxable	834	643
Tax-exempt	687	784
Dividends	1	
Interest-bearing deposits in banks	8	4
Federal funds sold	2	4
Total interest and dividend income	9,415	6,437
Interest expense:		
Deposits	2,249	1,706
Federal funds purchased	1	1
Securities sold under agreements to repurchase		73
Federal Home Loan Bank advances and other borrowings	91	19
Total interest expense	2,341	1,799
Net interest and dividend income	7,074	4,638
Provision for loan losses	1,100	879
Net interest and dividend income, after provision for loan losses	5,974	3,759
Noninterest income:		
Customer service fees	370	129
Equity in earnings of subsidiaries		
Gain on sales and calls of AFS securities, net	2	(7)
Gain on sales of loans, net		
Loan-servicing fees		
Other	666	173
Total noninterest income	1,038	295
Noninterest expenses:		
Salaries and employee benefits	2,079	918
Occupancy expense of premises, net	402	159
Outside services	186	147
Data processing	262	108
Foreclosed assets, net	78	67
Other	1,044	570
Total noninterest expenses	4,051	1,969
Income before income taxes	2,961	2,085
Income tax expense (benefit)	957	556
Net income	\$2,004	\$1,529

CONSOLIDATING SCHEDULE 2 - STATEMENT OF INCOME
(000s omitted except share data)

Northwest Bank	State Bank	Lena State Bank	Foresight Financial Group, Inc.	Eliminations	Consolidated Total
\$10,131	\$8,197	\$2,617			\$33,830
896	970	572			3,915
847	989	593			3,900
					1
1		2	11	(\$11)	15
1	3	1			11
11,876	10,159	3,785	11	(11)	41,672
2,160	2,100	1,109		(\$11)	9,313
2	2	1			7
21	73		0		167
84	147	0			341
2,267	2,322	1,110	0	(11)	9,828
9,609	7,837	2,675	11	0	31,844
3,255	1,270	591	100		7,195
6,354	6,567	2,084	(89)	0	24,649
473	240	157			1,369
			\$8,377	(\$8,377)	0
295	40	4			334
705					705
579					579
719	603	178	28		2,367
2,771	883	339	8,405	(8,377)	5,354
4,515	1,888	813	327		10,540
866	292	175	10		1,904
56	149	144	41		723
250	275	64			959
223			2,400		2,768
1,697	651	394	179		4,535
7,607	3,255	1,590	2,957	0	21,429
1,518	4,195	833	5,359	(8,377)	8,574
215	1,366	121	(1,209)		2,006
\$1,303	\$2,829	\$712	\$6,568	(\$8,377)	\$6,568

GENERAL INFORMATION

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E-mail: dcooke@ffgbank.net

Registrar, Transfer Agent and
Change of Address:

Foresight Financial Group, Inc. at its
Corporate Address

Foresight common stock is listed
on the NASDAQ Bulletin Board
under the symbol FGFH

For more information,
contact Foresight
Financial Group, Inc. at its
Corporate Address
or visit our
website at
www.foresightfg.com

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**WE ARE A MARKET DRIVEN, PEOPLE ORIENTED
COMMUNITY BANKING ORGANIZATION DEDICATED TO
ENHANCING SHAREHOLDER VALUE BY
PROVIDING OUR CUSTOMERS WITH
DIVERSIFIED FINANCIAL SERVICES THAT
HELP THEM ACHIEVE ECONOMIC SUCCESS
AND FINANCIAL SECURITY.**

**WE WILL PURSUE THESE GOALS WHILE
BALANCING SHAREHOLDER AND CUSTOMER INTERESTS
WITH THE ONGOING WELFARE OF OUR
EMPLOYEES AND LOCAL COMMUNITIES.**

**THE MEMBER BANKS OF OUR GROUP
MAINTAIN A HIGH DEGREE OF INDEPENDENCE
AND SENSITIVITY TO THE CONCERNS OF THE
LOCAL COMMUNITIES AND MARKETS
THAT WE CHOOSE TO SERVE.**

**WE WILL SEEK TO EXPAND SENSIBLY
INTO NEW MARKETS WHEN WE BELIEVE
THAT OUR BUSINESS MODEL AND
COMMUNITY BANKING PHILOSOPHY
CAN BE SUCCESSFULLY EXTENDED.**

IN SUMMARY:

“Community Building through Community Banking”



COMMUNITY BUILDING THROUGH COMMUNITY BANKING