Loyal Leadership, Local Decision Making
and Superior Service

Pinnacle Bancshares
2011 Annual Report

PINNACLE BANCSHARES, INC.
AND SUBSIDIARY

CONSOLIDATED FINANCIAL REPORT

DECEMBER 31, 2011

PINNACLE BANCSHARES, INC
AND SUBSIDIARY

CONSOLIDATED FINANCIAL REPORT
DECEMBER 31, 2011

TABLE OF CONTENTS

	Page
INDEPENDENT AUDITOR'S REPORT	1
CONSOLIDATED FINANCIAL STATEMENTS	
Consolidated statements of condition	2
Consolidated statements of income	3
Consolidated statements of comprehensive income	4
Consolidated statements of stockholders' equity	5
Consolidated statements of cash flows	6
Notes to consolidated financial statements	7-34

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Pinnacle Bancshares, Inc.
Jasper, Alabama

We have audited the accompanying consolidated statements of condition of **Pinnacle Bancshares, Inc. and its Subsidiary** as of December 31, 2011 and 2010, and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Pinnacle Bancshares, Inc. and Subsidiary 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.

Mauldin & Jenkins, LLC

Birmingham, Alabama
April 5, 2012

2000 SOUTHBRIDGE PARKWAY, SUITE 501 • BIRMINGHAM, AL 35209 • 205-445-2880 • 888-277-0020 • FAX 205-445-2940 • www.mjcpa.com
MEMBERS OF THE AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

PINNACLE BANCSHARES, INC.
AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CONDITION
December 31, 2011 and 2010

	2011	2010
Assets		
Cash and cash equivalents	**$ 2,510,642**	$ 3,486,659
Interest bearing deposits in banks	**1,613,466**	3,148,883
Securities available for sale	**75,734,778**	63,140,124
Restricted equity securities	**957,800**	1,255,200
Loans held for sale	**-**	251,141
Loans receivable, net of allowance for loan losses of $2,228,644 and $2,443,604, respectively	**102,445,514**	113,157,873
Loans, net	**102,445,514**	113,409,014
Foreclosed assets	**403,881**	587,450
Premises and equipment, net	**6,186,794**	6,488,537
Goodwill	**306,488**	306,488
Bank owned life insurance	**7,117,402**	6,777,100
Accrued interest receivable	**1,018,331**	1,034,539
Other assets	**935,476**	1,249,028
Total assets	**$ 199,230,572**	**$ 200,883,022**
Liabilities and Stockholders' Equity		
Deposits:		
Noninterest-bearing	**$ 31,309,182**	$ 18,339,053
Interest-bearing	**139,267,444**	155,573,414
Total deposits	**170,576,626**	173,912,467
Repurchase agreements	**984,957**	1,461,867
Subordinated debentures	**3,093,000**	3,093,000
Official checks outstanding	**771,362**	423,622
Accrued interest payable	**182,020**	353,564
Other liabilities	**1,288,204**	985,544
Total liabilities	**176,896,169**	180,230,064
Stockholders' equity		
Common stock, $.01 par value, 2,400,000 shares authorized; 1,872,313 shares issued; 1,270,128 shares outstanding	**18,723**	18,723
Additional paid-in capital	**8,923,223**	8,923,223
Treasury stock, at cost (602,185 shares)	**(7,320,909)**	(7,320,909)
Retained earnings	**18,609,374**	17,931,987
Accumulated other comprehensive income, net of tax	**2,103,992**	1,099,934
Total stockholders' equity	**22,334,403**	20,652,958
Total liabilities and stockholders' equity	**$ 199,230,572**	$ 200,883,022

See Notes to Consolidated Financial Statements.

PINNACLE BANCSHARES, INC.
AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME
Years Ended December 31, 2011 and 2010

	2011	2010
Interest income		
Loans	**$ 6,366,734**	$ 7,173,773
Taxable securities	**1,899,623**	2,076,225
Nontaxable securities	**601,355**	471,508
Other interest	**36,875**	30,501
Total interest income	**8,904,587**	9,752,007
Interest expense		
Deposits	**1,174,552**	1,960,362
Borrowings and repurchase agreements	**2,097**	2,000
Subordinated debentures	**99,607**	100,127
Total interest expense	**1,276,256**	2,062,489
Net interest income	**7,628,331**	7,689,518
Provision for loan losses	**1,100,000**	2,415,000
Net interest income after provision for loan losses	**6,528,331**	5,274,518
Other income		
Fees and service charges on deposit accounts	**963,962**	1,215,236
Service fee income, net	**51,440**	66,808
Fees and charges on loans	**188,863**	143,327
Bank owned life insurance	**340,302**	333,386
Net gain on loans held for sale	**40,061**	197,207
Net gain (loss) on sales of securities available for sale	**47,316**	(23,107)
Total other income	**1,631,944**	1,932,857
Other expenses		
Salaries and employee benefits	**3,315,192**	3,243,683
Occupancy expenses	**1,554,028**	1,446,457
Marketing and professional expenses	**202,975**	335,288
Net loss on real estate owned	**136,552**	42,862
Other operating expenses	**1,506,983**	1,468,310
Total other expenses	**6,715,730**	6,536,600
Income before income taxes	**1,444,545**	670,775
Income tax expense	**208,302**	15,940
Net income	**$ 1,236,243**	$ 654,835
Basic and diluted earnings per share	**$ 0.97**	$ 0.52
Cash dividends per share	**$ 0.44**	$ 0.44
Weighted-average basic and diluted shares outstanding	**1,270,128**	1,270,128

See Notes to Consolidated Financial Statements.

PINNACLE BANCSHARES, INC.
AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
Years Ended December 31, 2011 and 2010

	2011	2010
Net income	**$ 1,236,243**	$ 654,835
Other comprehensive income (loss):		
Unrealized holding gains (losses) on securities available for sale arising during the period, net of tax (benefits) of $633,608 and $(61,389), respectively	**1,033,158**	(99,857)
Reclassification adjustment for (gains) losses realized in net income, net of tax (benefits) of $18,216 and $(8,896), respectively	**(29,100)**	14,211
Other comprehensive income (loss)	**1,004,058**	(85,646)
Comprehensive income	**$ 2,240,301**	$ 569,189

See Notes to Consolidated Financial Statements.

PINNACLE BANCSHARES, INC.
AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
Years Ended December 31, 2011 and 2010

	Common Stock		Additional Paid-in	Treasury	Retained	Accumulated Other Comprehensive	Total Stockholders'
	Shares	Par Value	Capital	Stock	Earnings	Income	Equity
Balance, December 31, 2009	1,872,313	$ 18,723	$ 8,923,223	$ (7,320,909)	$ 17,836,009	$ 1,185,580	$ 20,642,626
Net income	-	-	-	-	654,835	-	654,835
Cash dividends declared, $0.44 per share	-	-	-	-	(558,857)	-	(558,857)
Other comprehensive loss	-	-	-	-	-	(85,646)	(85,646)
Balance, December 31, 2010	1,872,313	18,723	8,923,223	(7,320,909)	17,931,987	1,099,934	20,652,958
Net income	-	-	-	-	1,236,243	-	1,236,243
Cash dividends declared, $0.44 per share	-	-	-	-	(558,856)	-	(558,856)
Other comprehensive income	-	-	-	-	-	1,004,057	1,004,057
Balance, December 31, 2011	1,872,313	$ 18,723	$ 8,923,223	$ (7,320,909)	$ 18,609,374	$ 2,103,991	$ 22,334,402

See Notes to Consolidated Financial Statements.

PINNACLE BANCSHARES, INC.
AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2011 and 2010

	2011	2010
OPERATING ACTIVITIES		
Net income	**$ 1,236,243**	$ 654,835
Adjustments to reconcile net income to net cash		
Provided by operating activities:		
Depreciation	**484,254**	514,943
Provision for loan losses	**1,100,000**	2,415,000
Deferred tax expense (benefit)	**(86,761)**	138,597
Amortization expense, net	**2,578**	8,215
Bank owned life insurance	**(340,302)**	(333,386)
Gain on sale of loans held for sale	**(40,061)**	(197,207)
(Gain) loss on sale of securities available for sale	**(47,316)**	23,107
Loss on sale or write-down of real estate owned, net	**136,552**	42,862
Proceeds from sales of loans held for sale	**251,141**	16,355,518
Origination of loans held for sale	**-**	(15,730,789)
Decrease in accrued interest receivable	**16,208**	57,638
Decrease in accrued interest payable	**(171,544)**	(4,911)
Net other operating activities	**(102,224)**	700,113
Net cash provided by operating activities	**2,438,768**	4,644,535
INVESTING ACTIVITIES		
Net loan repayments	**9,184,171**	7,910,248
Net decrease in federal funds sold	**-**	1,950,000
Net (increase) decrease in interest-bearing deposits in other banks	**1,535,417**	(2,870,997)
Purchase of securities available for sale	**(29,862,416)**	(20,038,348)
Proceeds from sales of securities available for sale	**4,011,875**	10,033,687
Proceeds from maturing or callable securities available for sale	**14,920,077**	14,233,160
Proceeds from sale of correspondent bank stock	**297,400**	87,300
Purchase of premises and equipment	**(206,339)**	(289,189)
Proceeds from sales of real estate owned	**728,897**	136,396
Net cash provided by investing activities	**609,082**	11,152,257
FINANCING ACTIVITIES		
Net decrease in deposits	**(3,335,841)**	(16,496,010)
Increase (decrease) in official checks outstanding	**347,740**	(493,044)
Increase (decrease) in repurchase agreements	**(476,910)**	978,356
Payments of cash dividends	**(558,856)**	(558,857)
Net cash used in financing activities	**(4,023,867)**	(16,569,555)
Net increase in cash and cash equivalents	**(976,017)**	(772,763)
Cash and cash equivalents at beginning of year	**3,486,659**	4,259,422
Cash and cash equivalents at end of year	**$ 2,510,642**	$ 3,486,659
SUPPLEMENTAL DISCLOSURE		
Cash paid (received) during the year for:		
Interest	**$ 1,447,800**	$ 2,067,400
Taxes	**$ (35,697)**	$ 61,800
OTHER NONCASH TRANSACTIONS		
Real estate acquired through foreclosure	**$ 705,632**	$ 392,394

See Notes to Consolidated Financial Statements.

NOTE 1. SUMMARY OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

Following is a description of the business and the more significant accounting policies followed by Pinnacle Bancshares, Inc. (the "Company") and its wholly-owned subsidiary Pinnacle Bank (the "Bank") in presenting the consolidated financial statements.

Nature of Operations

Pinnacle Bancshares, Inc. is a bank holding company whose principal activity is the ownership and management of its wholly-owned subsidiary, Pinnacle Bank. The Bank is primarily in the business of obtaining funds in the form of various savings and time deposit products and investing those funds in mortgage, consumer, and commercial loans. The Bank operates in seven offices in the central and northwest portions of Alabama and originates its loans in this market area. The Company's principal activities do not constitute separate reportable segments of its business, but encompass traditional banking activities which offer similar products and services within the same primary geographic area and regulatory and economic environment.

Basis of Presentation and Accounting Estimates

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary. Significant intercompany transactions and balances have been eliminated in consolidation.

In preparing the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet, and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of foreclosed assets and deferred taxes, other-than-temporary impairments of securities, and the fair value of financial instruments.

The Company has evaluated all transactions, events, and circumstances for consideration or disclosure through April 5, 2012, the date these financial statements were available to be issued, and has reflected or disclosed those items within the consolidated financial statements and related footnotes as deemed appropriate.

Cash, Cash Equivalents, and Cash Flows

For purposes of reporting consolidated cash flows, cash, and cash equivalents includes cash on hand, cash items in process of collection, and amounts due from banks. Cash flows from loans, federal funds sold, interest-bearing deposits in other banks, deposits, repurchase agreements, and official checks outstanding are reported net.

The Bank is required to maintain average balances in cash or on deposit with the Federal Reserve Bank. The total of those reserve balances was approximately $1,366,000 and $1,195,000 at December 31, 2011 and 2010, respectively.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Securities

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

The Company evaluates investment securities for other-than-temporary impairment using relevant accounting guidance specifying that (a) if the Company does not have the intent to sell a debt security prior to recovery and (b) it is more likely than not that it will not have to sell the debt security prior to recovery, the security would not be considered other-than-temporary impaired unless there is a credit loss that has occurred in the security. If management does not intend to sell the security and it is not more likely than not that they will have to sell the security before recovery of the cost basis, management will recognize the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income.

Securities sold under agreements to repurchase ("repurchase agreements") are treated as collateralized financial transactions. These agreements are recorded at the amount at which the securities were sold plus accrued interest. The market value of these securities is monitored, and additional securities are obtained when deemed appropriate to ensure such transactions are adequately collateralized.

The Bank pledges assets to collateralize repurchase agreements. The carrying value of securities owned by the Bank that have been loaned or pledged to counterparties where those counterparties do not have the right to sell or repledge the securities totaled $2,925,429 and $3,896,829 at December 31, 2011 and 2010, respectively.

Restricted Equity Securities

The Company is required to maintain an investment in capital stock of various entities. Based on redemption provisions of these entities, the stock has no quoted market value and is carried at cost. At their discretion, these entities may declare dividends on the stock. Management reviews for impairment based on the ultimate recoverability of the cost basis in these stocks. Investments in restricted equity securities consisted of the following:

	December 31,	
	2011	2010
Federal Home Loan Bank of Atlanta	**$ 432,800**	$ 730,200
First National Banker's Bankshares, Inc.	**525,000**	525,000
	$ 957,800	$ 1,255,200

Loans Held for Sale

Loans originated and intended for sale in the secondary market are carried at the lower of cost or fair value (LOCOM). For loans carried at LOCOM, gains and losses on loan sales (sales proceeds minus carrying value) are recorded in noninterest income, and direct loan origination costs and fees are deferred at origination of the loan and are recognized in noninterest income upon sale of the loan. The estimated fair value of loans held for sale is based on independent third party quoted prices.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Loans Held for Sale (Continued)

The Company enters into interest rate lock commitments, where customers have locked into mortgages at a set interest rate, and forward sales commitments, which are sales of mortgage loans to third parties at a specified price. These interest rate locks and forward sales commitments qualify as derivatives; however, the change in fair value of these derivatives during the years ended December 31, 2011 and 2010 did not have a material impact on the Company's consolidated financial position or results of operations.

Loans Receivable

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding principal balances less deferred fees and costs on originated loans and the allowance for loan losses. Interest income is accrued on the outstanding principal balance. Loan origination fees, net of certain direct origination costs of consumer and installment loans are recognized at the time the loan is placed on the books. Loan origination fees for all other loans are deferred and recognized as an adjustment of the yield over the life of the loan using the straight-line method without anticipating prepayments.

The accrual of interest on loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due, or at the time the loan is 90 days past due, unless the loan is well-secured and in the process of collection. Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal and interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income or charged to the allowance, unless management believes that the accrual of interest is recoverable through the liquidation of collateral. Interest income on nonaccrual loans is recognized on the cash basis, until the loans are returned to accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and the loan has been performing according to the contractual terms for a period of not less than six months.

Allowance for Loan Losses

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

The allowance is an amount that management believes will be adequate to absorb estimated losses relating to specifically identified loans, as well as probable credit losses inherent in the balance of the loan portfolio. The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the uncollectibility of loans in light of historical experience, the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, current economic conditions that may affect the borrower's ability to pay, 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. This evaluation does not include the effects of expected losses on specific loans or groups of loans that are related to future events or expected changes in economic conditions. While management uses the best information available to make its evaluation, future adjustments to the allowance may be necessary if there are significant changes in economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses, and may require the Company to make additions to the allowance based on their judgment about information available to them at the time of their examinations.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Allowance for Loan Losses (Continued)

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as impaired. For impaired loans, 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 other qualitative factors. Other adjustments may be made to the allowance for pools of loans after an assessment of internal or external influences on credit quality that are not fully reflected in the historical loss or risk rating data. An unallocated component may be maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

A loan is considered impaired when it is probable, based on current information and events, the Company will be unable to collect all principal and interest payments due in accordance with the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest when due. Loans that experience insignificant payment delays and payment shortfalls are not classified as impaired. Impaired loans are measured by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent. Interest on accruing impaired loans is recognized as long as such loans do not meet the criteria for nonaccrual status. Loans, for which the terms have been modified at the borrower's request, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and are also classified as impaired.

The Company's homogenous loan pools include commercial real estate loans, real estate construction and land development loans, residential real estate loans, real estate other loans, commercial loans, and consumer loans. The general allocations to these loan pools are based on the historical loss rates for specific loan types and the internal risk grade, if applicable, adjusted for both internal and external qualitative risk factors. The qualitative factors considered by management include, among other factors, (1) changes in local and national economic conditions; (2) changes in asset quality; (3) changes in loan portfolio volume; (4) the composition and concentrations of credit and; (5) effectiveness of the Company's loan policies, procedures and internal controls. The total allowance established for each homogenous loan pool represents the product of the historical loss ratio and the total dollar amount of the loans in the pool.

Troubled Debt Restructurings

The Company designates loan modifications as troubled debt restructurings ("TDRs") when for economic and legal reasons related to the borrower's financial difficulties, it grants a concession to the borrower that it would not otherwise consider. TDRs can involve loans remaining on nonaccrual, moving to nonaccrual, or continuing on accrual status, depending on the individual facts and circumstances of the borrower. In circumstances where the TDR involves charging off a portion of the loan balance, the Company typically classifies these restructurings as nonaccrual.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Troubled Debt Restructurings (Continued)

In connection with restructurings, the decision to maintain a loan that has been restructured on accrual status is based on a current, well documented credit evaluation of the borrower's financial condition and prospects for repayment under the modified terms. This evaluation includes consideration of the borrower's current capacity to pay, which among other things may include a review of the borrower's current financial statements, an analysis of global cash flow sufficient to pay all debt obligations, a debt to income analysis, and an evaluation of secondary sources of payment from the borrower and any guarantors. This evaluation also includes an evaluation of the borrower's current willingness to pay, which may include a review of past payment history, an evaluation of the borrower's willingness to provide information on a timely basis, and consideration of offers from the borrower to provide additional collateral or guarantor support. The credit evaluation also reflects consideration of the borrower's future capacity and willingness to pay, which may include evaluation of cash flow projections, consideration of the adequacy of collateral to cover all principal and interest, and trends indicating improving profitability and collectability of receivables.

Restructured nonaccrual loans may be returned to accrual status based on a current, well-documented credit evaluation of the borrower's financial condition and prospects for repayment under the modified terms. This evaluation must include consideration of the borrower's sustained historical repayment for a reasonable period, generally a minimum of six months, prior to the date on which the loan is returned to accrual status.

Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation computed on a straight-line basis over the estimated service lives of the related assets (30 to 50 years for buildings, shorter of lease period or estimated life of 10 to 15 years for leasehold improvements and 3 to 10 years for equipment). Expenditures for maintenance and repairs are charged to operations as incurred; expenditures for renewals and improvements are capitalized and charged to operations through depreciation and amortization charges. Equipment retired or sold is removed from the asset and related accumulated depreciation amounts and any gain or loss resulting therefrom is reflected in the accompanying consolidated statements of operations.

The Company continually evaluates whether events and circumstances have occurred that indicate such long-lived assets have been impaired. Measurement of any impairment of such long-lived assets is based on those assets' fair values and is recognized through a valuation allowance with the resulting charge reflected in the accompanying consolidated statements of operations. There were no impairment losses recorded during any period reported herein.

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 - put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that 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 or the ability to unilaterally cause the holder to return specific assets.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Foreclosed Assets

Foreclosed assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value less selling costs. Any write-down to fair value at the time of transfer to foreclosed assets is charged to the allowance for loan losses. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less costs to sell. Costs of improvements are capitalized, whereas costs relating to holding foreclosed assets and subsequent write-downs to the value are expensed.

Goodwill

Goodwill represents the excess of cost over the fair value of the net assets and liabilities acquired in a business combination. Goodwill is required to be tested annually for impairment, or whenever events occur that may indicate that the recoverability of the carrying amount is not probable. In the event of an impairment, the amount by which the carrying amount exceeds the fair value would be charged to earnings.

Bank Owned Life Insurance

The Company has bank owned life insurance on certain current and former key officers of the Company. The life insurance policies were purchased to reduce costs associated with certain existing employee benefits. Increases in the cash surrender value of the policies, as well as insurance proceeds received, are recorded as a component of non-interest income.

Income Taxes

The Company accounts for income taxes in accordance with income tax accounting guidance (FASB ASC 740, Income Taxes). On January 1, 2009, the Company adopted the recent accounting guidance related to accounting for uncertainty in income taxes, which sets out a consistent framework to determine the appropriate level of tax reserves to maintain for uncertain tax positions.

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

Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are recognized if it is more likely than not, based on the technical merits, that the tax position will be realized or sustained upon examination. The term more likely than not means a likelihood of more than 50 percent; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any. A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances, and information available at the reporting date and is subject to management's judgment. Deferred tax assets may be reduced by deferred tax liabilities and a valuation allowance if, based on the weight of evidence available, it is more likely than not that some portion or all of a deferred tax asset will not be realized.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Earnings Per Share

Basic earnings per share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflects additional potential 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. There were no potential common shares as of December 31, 2011 and 2010.

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although 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.

Fair Value of Financial Instruments

Fair values of financial instruments are estimates using relevant market information and other assumptions, as more fully disclosed in Note 15. Fair value estimates involve uncertainties and matters of significant judgment. Changes in assumptions or in market conditions could significantly affect the estimates.

Recent Accounting Pronouncements

In July 2010, the FASB issued Accounting Standards Update (ASU) No. 2010-20 to Receivables (ASC 310) *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*. This ASU adds new disclosures designed to enhance the transparency of an entity's allowance for loan and lease losses (ALLL), and the credit quality of its financing receivables, and to increase the understanding of an entity's credit risk exposure and adequacy of the ALLL. The required disclosures will include the nature of the credit risk inherent in the loan portfolio, how the risk is analyzed and assessed to determine the ALLL, and the changes and reasons for those changes in the ALLL. These disclosures are effective for annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for annual reporting periods beginning on or after December 15, 2010. This pronouncement had no effect on the Company's financial position or results of operations. The required disclosures are included in Note 3 as of and for the year ended December 31, 2011.

In April 2011, the FASB amended existing guidance for assisting a creditor in determining whether a restructuring is a troubled debt restructuring. The amendments clarify the guidance for a creditor's evaluation of whether it has granted a concession and whether a debtor is experiencing financial difficulties. With regard to determining whether a concession has been granted, the ASU clarifies that creditors are precluded from using the effective interest method to determine whether a concession has been granted. In the absence of using the effective interest method, a creditor must now focus on other considerations such as the value of the underlying collateral, evaluation of other collateral or guarantees, the debtor's ability to access other funds at market rates, interest rate increases and whether the restructuring results in a delay in payment that is insignificant. This guidance is effective for annual reporting periods beginning after June 15, 2011, and should be applied retrospectively to the beginning of the annual period of adoption. For purposes of measuring impairment on newly identified troubled debt restructurings, the amendments should be applied prospectively for the annual period beginning on or after June 15, 2011. The adoption of this guidance is not expected to have a material impact on the Company's financial statements.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Recent Accounting Pronouncements (Continued)

In May, 2011, the FASB issued an amendment to achieve common fair value measurement and disclosure requirements between U.S. and International accounting principles. Overall, the guidance is consistent with existing U.S. accounting principles; however, there are some amendments that change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements. The amendments in this guidance are effective for annual reporting periods beginning after December 15, 2011. The adoption of this guidance is not expected to have a material impact on the Company's financial statements.

In June 2011, the FASB amended existing guidance and eliminated the option to present the components of other comprehensive income as part of the statement of changes in shareholder's equity. The amendment requires that comprehensive income be presented in either a single continuous statement or in two separate consecutive statements. The amendments in this guidance are effective as of the beginning of a fiscal reporting year that begins after December 15, 2011. The adoption of this guidance is not expected to have a material impact on the Company's financial statements.

In September 2011, Financial Accounting Standards Board ("FASB") issued an ASU to amend and simplify the rules related to testing goodwill for impairment. The revised guidance allows an entity to make an initial qualitative evaluation, based on the entity's events and circumstances, to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. The results of this qualitative assessment determine whether it is necessary to perform the currently required two-step impairment test.

NOTE 2. SECURITIES

The amortized cost, unrealized gross gains and losses, and estimated fair value of securities available for sale are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities Available for Sale				
December 31, 2011:				
Municipal securities	**$ 28,046,089**	**$ 1,381,599**	**$ (16,578)**	**$ 29,411,110**
U.S. treasury securities	**-**	**-**	**-**	**-**
U.S. Government-sponsored enterprises (GSEs)*	**1,896,039**	**81,381**	**-**	**1,977,420**
Corporate securities	**530,219**	**-**	**(25,530)**	**504,689**
Mortgage-backed securities	**41,854,257**	**1,988,148**	**(846)**	**43,841,559**
Total securities**	**$ 72,326,604**	**$ 3,451,128**	**$ (42,954)**	**$ 75,734,778**
December 31, 2010:				
Municipal securities	$ 23,469,360	$ 544,661	$ (287,448)	$ 23,726,573
U.S. treasury securities	3,961,606	-	(152,927)	3,808,679
U.S. Government-sponsored enterprises (GSEs)*	1,886,860	85,760	-	1,972,620
Other securities	716	-	-	716
Mortgage-backed securities	32,032,857	1,602,014	(3,335)	33,631,536
Total securities**	$ 61,351,399	$ 2,232,435	$ (443,710)	$ 63,140,124

* Such as Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, and Federal Home Loan Banks.

** At December 31, 2011, no securities of any single issuer (excluding the U.S. Government and U.S. Government-sponsored enterprises) with a book value that exceeded 10% of stockholders' equity were held.

NOTE 2. SECURITIES (Continued)

The amortized cost and estimated fair value of securities available for sale at December 31, 2011 by contractual maturity are shown below. Actual maturities may differ from contractual maturities in mortgage-backed securities because the mortgages underlying the securities may be called or repaid with or without penalty. Therefore, these securities are not included in the maturity categories in the following summary:

	Amortized Cost	Fair Value
Due within one year	$ 601,979	$ 602,154
Due from one to five years	11,636,649	11,858,862
Due from five to ten years	6,013,367	6,284,788
Due in more than ten years	12,220,352	13,147,415
Mortgage-backed securities	41,854,257	43,841,559
	$ 72,326,604	$ 75,734,778

Securities of approximately $17 million and $15 million at December 31, 2011 and 2010, respectively, were pledged to secure deposits and for other purposes required or permitted by law.

Gains and losses on sales of securities available for sale consist of the following:

	Years Ended December 31,	
	2011	2010
Gross gains	**$ 47,316**	$ 23,702
Gross losses	**-**	(46,809)
Net realized gains (losses)	**$ 47,316**	$ (23,107)

Temporarily Impaired Securities

The following table shows the gross unrealized losses and fair value of the Company's investments with unrealized losses that are not deemed to be other-than-temporarily impaired, 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.

Available for sale securities that have been in a continuous unrealized loss position are as follows:

	Less Than Twelve Months		Over Twelve Months			
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Total Unrealized Losses	Total Fair Value
December 31, 2011						
Municipal securities	**$ (16,578)**	**$ 2,580,981**	**$ -**	**$ -**	**$ (16,578)**	**$ 2,580,981**
Corporate	**(25,530)**	**504,689**	**-**	**-**	**(25,530)**	**504,689**
Mortgage-backed						
GSE residential	**(846)**	**206,052**	**-**	**-**	**(846)**	**206,052**
Total	**$ (42,954)**	**$ 3,291,722**	**$ -**	**$ -**	**$ (42,954)**	**$ 3,291,722**
December 31, 2010						
Municipal securities	$ (287,448)	$ 7,417,525	$ -	$ -	$ (287,448)	$ 7,417,525
U.S. treasury securities	(152,927)	3,808,680	-	-	(152,927)	3,808,680
Mortgage-backed						
GSE residential	(2,733)	190,409	(602)	51,196	(3,335)	241,605
Total	$ (443,108)	$ 11,416,614	$ (602)	$ 51,196	$ (443,710)	$ 11,467,810

NOTE 2. SECURITIES (Continued)

Temporarily Impaired Securities (Continued)

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

Corporate bonds. The Company's unrealized loss on its investment in one corporate bond relates to an investment in a company within the financial services sector. The unrealized loss is primarily caused by recent decreases in profitability and profit forecasts by industry analysts resulting from the sub-prime mortgage market and a recent sector downgrade by several industry analysts. The contractual terms of this investment do not permit the Company to settle the security at a price less than the par value of the investment. The Company currently does not believe it is probable that it will be unable to collect all amounts due according to the contractual terms of the investment. Because the Company does not intend to sell the investment and it is not more likely than not that the Company will be required to sell the investment before recovery of its par value, which may be maturity, it does not consider this investment to be other-than-temporarily impaired at December 31, 2011.

GSE residential mortgage-backed securities. The unrealized losses associated with the Company's investment in six GSE mortgage-backed securities were caused by interest rate increases. The contractual cash flows of those investments are guaranteed by an agency of the U.S. Government. Accordingly, it is expected that the securities would not be settled at a price less than the amortized cost bases of the Company's investments. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other-than-temporarily impaired at December 31, 2011.

NOTE 3. LOANS

The composition of loans is summarized as follows:

	December 31,	
	2011	2010
Real estate – commercial	**$ 39,460,967**	$ 40,695,750
Real estate – construction	**6,954,321**	7,532,730
Real estate – 1-4 family	**36,080,578**	41,074,659
Real estate – other	**277,972**	533,972
Commercial	**17,769,727**	20,601,070
Consumer	**4,078,806**	5,105,715
	104,622,371	115,543,896
Deferred loan costs	**51,787**	57,581
Allowance for loan losses	**(2,228,644)**	(2,443,604)
Loans, net	**$ 102,445,514**	$ 113,157,873

NOTE 3. LOANS (Continued)

The Company has a credit concentration in residential and commercial real estate mortgage loans. Approximately 79% and 78% at December 31, 2011 and 2010, respectively, of the Company's total gross loan portfolio represented first or second mortgage residential and commercial real estate loans. Substantially all of the Company's loan customers are located in the Company's primary lending areas of Walker, Winston, Jefferson, and Shelby counties in Alabama. Although the Company believes that its underwriting standards are generally conservative, including a policy calling for low loan to collateral values, the ability of its borrowers to meet their mortgage obligations is dependent upon local economic conditions.

Portfolio Segmentation

For purposes of the disclosures required pursuant to the adoption of ASC 310, the loan portfolio was disaggregated into segments and then further disaggregated into classes for certain disclosures. A portfolio segment is defined as the level at which an entity develops and documents a systematic method for determining its allowance for loan losses. There are three loan portfolio segments that include real estate, commercial, and consumer. A class is generally determined based on the initial measurement attribute, risk characteristic of the loan, and an entity's method for monitoring and assessing credit risk. Classes within the real estate portfolio segment include commercial, construction and development, 1-4 family mortgages, and other. The portfolio segments of non-real estate commercial and consumer loans have not been further segregated by class.

The following describe risk characteristics relevant to each of the portfolio segments:

Real Estate - As discussed below, the Company offers various types of real estate loan products. All loans within this portfolio segment are particularly sensitive to the valuation of real estate:

- Commercial real estate mortgage loans include owner-occupied commercial real estate loans, owner-occupied construction loans for commercial businesses, and loans secured by income producing properties. Owner-occupied commercial real estate loans to operating businesses are long-term financing of land and buildings. Owner-occupied construction loans for a commercial business are for the development of land or construction of a building. Both of these loans are repaid by cash flow generated from the business operation. Real estate loans for income-producing properties such as apartment buildings, office and industrial buildings, and retail shopping centers are repaid from rent income derived from the properties.
- Loans for real estate construction and development are repaid through cash flow related to the operations, sale or refinance of the underlying property. This portfolio segment includes extensions of credit to real estate developers or investors where repayment is dependent on the sale of the real estate or income generated from the real estate collateral.
- 1-4 family mortgage loans, including HELOCs, are repaid by various means such as a borrower's income, sale of the property, or rental income derived from the property.
- Other real estate mortgage loans include real estate loans secured by farmland. These are repaid by various means such as a borrower's income, sale of the property, or rental income derived from the property.

Commercial - The commercial non real estate loan portfolio segment includes commercial, financial, agricultural, and municipal tax free loans. These loans include those loans to commercial customers for use in normal business operations to finance working capital needs, equipment purchases, or expansion projects. Loans are repaid by business cash flows. Collection risk in this portfolio is driven by the creditworthiness of the underlying borrower, particularly cash flows from the customers' business operations.

Consumer - The consumer loan portfolio segment includes direct consumer installment loans, overdrafts, and other revolving credit loans. Loans in this portfolio are sensitive to unemployment and other key consumer economic measures.

NOTE 3. LOANS (Continued)

Credit Risk Management

Credit Risk Management and the Special Assets Division are both involved in the credit risk management process and assess the accuracy of risk ratings, the quality of the portfolio and the estimation of inherent credit losses in the loan portfolio. This comprehensive process also assists in the prompt identification of problem credits. The Company has taken a number of measures to manage the portfolios and reduce risk, particularly in the more problematic portfolios.

The Company employs a credit risk management process with defined policies, accountability and routine reporting to manage credit risk in the loan portfolio segments. Credit risk management is guided by credit policies that provide for a consistent and prudent approach to underwriting and approvals of credits. Within the Credit Policy, procedures exist that elevate the approval requirements as credits become larger and more complex. All loans are individually underwritten, risk-rated, approved, and monitored.

Responsibility and accountability for adherence to underwriting policies and accurate risk ratings lies in each portfolio segment. For the consumer portfolio segment, the risk management process focuses on managing customers who become delinquent in their payments. For the commercial and real estate portfolio segments, the risk management process focuses on underwriting new business and, on an ongoing basis, monitoring the credit of the portfolios.

Credit quality and trends in the loan portfolio segments are measured and monitored regularly and loans are classified according to the following risk grade categories. Detailed reports, by product, collateral, accrual status, etc, are reviewed by management and the Loan Committee.

- **Pass -** includes obligations where the probability of default is considered low.
- **Management Attention -** includes obligation that contain a greater than normal amount of risk and warrant more than the ordinary amount of supervision though they do not yet require frequent monitoring of the situation.
- **Special Mention** - includes obligations that exhibit potential credit weaknesses or downward trends deserving management's close attention. If left uncorrected, these potential weaknesses may result in the deterioration of the repayment prospects or credit position at a future date. These loans are not adversely classified and do not expose the Company to sufficient risk to warrant adverse classification.
- **Substandard** - includes obligations with defined weaknesses that jeopardize the orderly liquidation of debt. A substandard loan is inadequately protected by the current sound worth and paying capacity of the borrower or by the collateral pledged, if any. Normal repayment from the borrower is in jeopardy although no loss of principal is envisioned. There is a distinct possibility that a partial loss of interest and/or principal will occur if the deficiencies are not corrected. Loss potential, while existing in the aggregate amount of substandard loans, does not have to exist in individual loans classified substandard.
- **Doubtful** - includes obligations with all the weaknesses found in substandard loans with the added provision that the weaknesses make collection of debt in full, based on current existing facts, conditions, and values, highly questionable and improbable. Serious problems exist to the point where partial loss of principal is likely. The possibility of loss is extremely high, but because of certain important, reasonably specific pending factors that may work to strengthen the loan, the loans' classification as estimated losses is deferred until a more exact status may be determined. There are no loans with a doubtful rating in the Company's portfolio as of December 31, 2011.
- **Loss** - includes obligations incapable of repayment or unsecured debt. Such loans are considered uncollectible and of such little value, that continuance as an active asset is not warranted. Loans determined to be a loss are charged-off at the date of loss determination. There are no loans with a loss rating in the Company's portfolio as of December 31, 2011.

NOTE 3. LOANS (Continued)

Credit Risk Management (Continued)

The following table summarizes the risk categories of the Company's loan portfolio based upon on the most recent analysis performed as of December 31, 2011:

	Pass	Management Attention	Special Mention	Substandard	Total
Real estate – commercial	$ 35,953,845	$ 1,595,087	$ 1,403,732	$ 508,303	$ 39,460,967
Real estate – construction	3,290,890	669,983	28,181	2,965,267	6,954,321
Real estate – 1-4 family	32,836,003	888,567	673,698	1,682,310	36,080,578
Real estate – other	277,972	-	-	-	277,972
Commercial	11,309,934	5,069,899	793,989	595,905	17,769,727
Consumer	4,048,201	12,129	2,950	15,526	4,078,806
Total:	$ 87,716,845	$ 8,235,665	$ 2,902,550	$ 5,767,311	$ 104,622,371

A loan is considered past due if any required principal and interest payments have not been received as of the date such payments were required to be made under the terms of the loan agreement. Generally, we place loans on non-accrual when there is a clear indication that the borrower's cash flow may not be sufficient to meet payments as they become due, which is generally when a loan is 90 days past due. The following table presents the aging of the recorded investment in loans and leases as of December 31, 2011:

		Past Due Status (Accruing Loans)					
	Current	30-59 Days	60-89 Days	90+ Days	Total Past Due	Non-accrual	Total
Real estate – commercial	$ 39,452,209	$ 8,758	$ -	$ -	$ 8,758	$ -	$ 39,460,967
Real estate – construction	5,908,105	20,405	30,593	-	50,998	995,218	6,954,321
Real estate – 1-4 family	35,337,396	-	685,380	-	685,380	57,802	36,080,578
Real estate – other	277,972	-	-	-	-	-	277,972
Commercial	17,769,727	-	-	-	-	-	17,769,727
Consumer	4,010,915	67,891	-	-	67,891	-	4,078,806
Total:	$ 102,756,324	$ 97,054	$ 715,973	$ -	$ 813,027	$ 1,053,020	$ 104,622,371

NOTE 3. LOANS (Continued)

Allowance for Loan Losses

The following table details activity in the allowance for loan losses by portfolio segment for the year ended December 31, 2011. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

	Real Estate	Commercial	Consumer	Unallocated	Total
Allowance for loan losses:					
Beginning balance	$ 1,692,414	$ 599,905	$ 137,751	$ 13,534	$ 2,443,604
Provision for loan losses	964,248	(111,434)	10,465	236,721	1,100,000
Loans charged off	(1,331,246)	(64,653)	(162,009)	-	(1,557,908)
Recoveries	131,994	7,217	103,737	-	242,948
Ending balance	$ 1,457,410	$ 431,035	$ 89,944	$ 250,255	$ 2,228,644
Ending balance – individually evaluated for impairment	$ 531,639	$ 294,131	$ -	$ -	$ 825,770
Ending balance – collectively evaluated for impairment	$ 925,771	$ 136,904	$ 89,944	$ 250,255	$ 1,402,874
	1,457,410	431,035	89,944	250,255	2,228,644
Loans:					
Ending balance - individual evaluated for impairment	$ 4,365,800	$ 639,868	$ -	$ -	$ 5,005,668
Ending balance – collectively evaluated for impairment	$ 78,408,038	$ 17,129,859	$ 4,078,806	$ -	$ 99,616,703
Ending balance	$ 82,773,838	$ 17,769,727	$ 4,078,806	$ -	$ 104,622,371

Activity in the allowance for loan losses for the year ended December 2010 is summarized below:

Balance, beginning of year	$ 3,573,643
Provision for loan losses	2,415,000
Loans charged off	(3,740,093)
Recoveries	195,054
Balance, end of year	$ 2,443,604

NOTE 3. LOANS (Continued)

Impaired Loans

A loan held for investment is considered impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due (both principal and interest) according to the terms of the loan agreement. The following table details our impaired loans, by portfolio class as of December 31, 2011:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Real estate – commercial	$ -	$ -	$ -	$ -	$ -
Real estate – construction	1,782,596	2,768,968		1,547,954	61,214
Real estate – 1-4 family	-	-	-	-	-
Real estate – other	-	-	-	-	-
Commercial	-	-	-	-	-
Consumer	-	-	-	-	-
Total with no related allowance recorded	1,782,596	2,768,968	-	1,547,954	61,214
With an allowance recorded:					
Real estate – commercial	737,352	737,352	193,402	1,116,670	58,314
Real estate – construction	166,688	239,819	32,323	703,554	8,493
Real estate – 1-4 family	1,679,164	1,687,164	305,915	2,095,131	109,884
Real estate – other	-	-	-	-	-
Commercial	639,868	639,868	294,130	678,297	42,105
Consumer	-	-	-	-	-
Total with an allowance recorded	3,223,072	3,304,203	825,770	4,593,652	218,796
Total impaired loans:	$ 5,005,668	$ 6,073,171	$ 825,770	$ 6,141,606	$ 280,010

The following is a summary of information pertaining to impaired loans as of December 31, 2010.

Impaired loans with a valuation allowance	$ 4,851,028
Impaired loans without a valuation allowance	1,839,566
Total impaired loans	$ 6,690,594
Valuation allowance related to impaired loans	$ 1,163,445
Total nonaccrual loans	1,336,405
Total loans past due ninety days or more and still accruing	390,994
Average investment in impaired loans	6,116,845
Interest income recognized on impaired loans	371,728

Troubled Debt Restructurings

At December 31, 2011, impaired loans included loans that were classified as Troubled Debt Restructurings “TDRs”. The restructuring of a loan is considered a TDR if both (i) the borrower is experiencing financial difficulties and (ii) the creditor has granted a concession.

NOTE 3. LOANS (Continued)

Troubled Debt Restructurings (Continued)

The following table summarizes the loans that were modified as a TDR during the year-ended December 31, 2011 and were in compliance with the modified terms:

	Troubled-Debt Restructurings			
	Number of Loans	Recorded Investment Prior to Modification	Recorded Investment After Modification	Impact on the Allowance for Loan Losses
Real estate – commercial	1	$ 381,642	$ 381,642	$ -
Real estate – construction	1	828,530	828,530	-
Real estate – 1-4 family	-	-	-	-
Real estate – other	-	-	-	-
Commercial	-	-	-	-
Consumer	-	-	-	-
Total	2	$ 1,210,172	$ 1,210,172	$ -

At December 31, 2011, there were no loans classified as a TDR that had defaulted under their modified terms.

At December 31, 2010 the Company had $1,342,000 in loans that were modified in troubled debt restructuring and impaired. Of these amounts, all were performing in accordance with their modified terms as of December 31, 2010.

The Company has no additional commitments to lend additional funds to any of the related debtors whose terms have been modified in a TDR.

Related Party Transactions

In the ordinary course of business, the Company has granted loans to certain related parties, including directors, executive officers, and their affiliates. The interest rates on these loans were substantially the same as rates prevailing at the time of the transaction and repayment terms are customary for the type of loan. Changes in related party loans for the year ended December 31, 2011 and 2010 are as follows:

	December 31,	
	2011	2010
Balance, beginning of year	**$ 683,327**	$ 723,128
Change in directors	**80,000**	231,391
Advances	**852,635**	38,472
Repayments	**(679,171)**	(309,664)
Balance, end of year	$ **936,791**	$ 683,327

NOTE 4. FORECLOSED ASSETS

A summary of foreclosed assets is presented as follows:

	Years Ended December 31,	
	2011	2010
Balance, beginning of year	**$ 587,450**	$ 374,314
Additions, including capitalized expenses	**708,183**	392,394
Disposals	**(755,200)**	(136,396)
Net loss on sale, writedowns and provisions for losses	**(136,552)**	(42,862)
Balance, end of year	**$ 403,881**	$ 587,450

NOTE 5. PREMISES AND EQUIPMENT

Premises and equipment are summarized as follows:

	December 31,	
	2011	2010
Land	**$ 1,219,463**	$ 1,219,463
Buildings and leasehold improvements	**8,504,560**	8,488,535
Furniture, fixtures, and equipment	**3,287,549**	3,365,128
Construction in process	**174,428**	-
Automobiles	**74,657**	74,657
	13,260,657	13,147,783
Less accumulated depreciation	**(7,073,863)**	(6,659,246)
	$ 6,186,794	$ 6,488,537

The Company had noncancelable operating leases for the main and branch office sites. Occupancy expenses for the fiscal years ended December 31, 2011 and 2010 include rental expense under these leases of $110,404 and $121,628, respectively. Future rental payments subject to periodic renegotiations required under these leases are as follows:

2012	$ 114,786
2013	115,968
2014	117,178
2015	118,658
2016	119,806
Thereafter	1,076,939
	$ 1,663,335

The Company has a sublease agreement for the building in which the main office branch is located that generated income of $106,404 and $105,636 for the fiscal years ended December 31, 2011 and 2010, respectively.

NOTE 6. DEPOSITS

The aggregate amount of time deposits in denominations of $100,000 or more at December 31, 2011 and 2010 was $29,497,246 and $39,268,297, respectively. The scheduled maturities of time deposits at December 31, 2011 are as follows:

2012	$ 53,464,817
2013	9,973,543
2014	2,059,537
2015	414,587
2016	3,126,928
Thereafter	95,978
	$ 69,135,390

At December 31, 2011 and 2010, overdraft demand and savings deposits reclassified to loans totaled $41,530 and $77,099, respectively. Deposits from one customer held by the Bank at December 31, 2011 amounted to $9,227,893.

NOTE 7. SUBORDINATED DEBENTURES

On December 22, 2003, the Company established Pinnacle Capital Trust I (“Trust”), a wholly-owned statutory business trust. The Company is the sole sponsor of the Trust and acquired the Trust’s common securities for $93,000. The Trust was created for the exclusive purpose of issuing 30-year capital trust securities (“Trust Preferred Securities”) in the aggregate amount of $3,000,000 and using proceeds to purchase $3,093,000 of junior subordinated debentures (“Subordinated Debentures”) issued by the Company. The sole assets of the Trust are the Subordinated Debentures. The Company’s $93,000 investment in the Trust is included in other assets in the accompanying consolidated balance sheet and the $3,093,000 obligation of the Company is included in subordinated debentures.

The Trust Preferred Securities bear a floating interest rate of 2.85% over 3-month LIBOR (3.41% at December 31, 2011) which is set each quarter and matures on December 22, 2033. Distributions are payable quarterly. The Trust Preferred Securities are subject to mandatory redemption upon repayment of the Subordinated Debentures at their stated maturity date or their earlier redemption in an amount equal to their liquidation amount plus accumulated and unpaid distributions to the date of redemption. The Company guarantees the payment of distributions and payments for redemption or liquidation of the Trust Preferred Securities to the extent of funds held by the Trust. Pinnacle Bancshares, Inc.’s obligation under the subordinated debentures together with the guarantee and other back-up obligation, in aggregate, constitute a full and unconditional guarantee by the Company of the obligations of the Trust under the Trust Preferred Securities.

The subordinated debentures are unsecured, bear an interest rate equal to the spread paid by the Trust on the Trust Preferred Securities which is set each quarter and matures on December 30, 2033. Interest is payable quarterly. The Company may defer the payment of interest at any time for a period not exceeding 20 consecutive quarters provided that deferral period does not extend past the stated maturity. During any such deferral period, distributions on the Trust Preferred Securities will also be deferred and the Company’s ability to pay dividends on the common shares will be restricted.

Subject to approval by the Federal Reserve Bank of Atlanta, the Trust Preferred Securities may be redeemed prior to maturity at the Company’s option on or after January 7, 2009. The Trust Preferred Securities may also be redeemed at any time in whole (but not in part) in the event of unfavorable changes in laws or regulations that result in (1) the Trust becoming subject to federal income tax on income received on the Subordinated Debentures, (2) interest payable by the Company on the subordinated debentures becoming non-deductible for federal tax purposes, or (3) the requirement for Trust Preferred Securities as “Tier I Capital” under the Federal Reserve capital adequacy guidelines.

NOTE 8. BORROWED FUNDS

The Company has an available unused line of credit with First National Banker's Bank totaling $7,300,000 at December 31, 2011. There were no advances outstanding at December 31, 2011 or 2010.

In addition to the federal funds line of credit mentioned above, the Company has an available unused line of credit with the Federal Reserve Bank. Under the agreement with the Federal Reserve, the Company is allowed to borrow up to the fair market value of the available for sale securities pledged to the Federal Reserve Bank. There were no outstanding advances at December 31, 2011 and 2010, and thus no securities were required to be pledged to the Federal Reserve Bank.

The Company also has an available unused line of credit with the Federal Home Loan Bank of Atlanta, Georgia. Any advances from this line of credit will be secured by pledged securities available for sale and certain real estate loans owned by the Company. At December 31, 2011 the total borrowing capacity available through the FHLB was approximately $10,739,000. There were no outstanding advances at December 31, 2011 and 2010.

NOTE 9. REPURCHASE AGREEMENTS

Securities sold under repurchase agreements, which are secured borrowings, generally mature within one to four days from the transaction date. Securities sold under repurchase agreements are reflected at the amount of cash received in connection with the transaction. The Company may be required to provide additional collateral based on the fair value of the underlying securities. The Company monitors the fair value of the underlying securities on a daily basis. Securities sold under repurchase agreements at December 31, 2011 and 2010 were $984,957 and $1,461,867, respectively.

NOTE 10. INCOME TAXES

The allocation of income tax expense between current and deferred income taxes is as follows:

	Years Ended December 31,	
	2011	2010
Current	**$ 295,063**	$ (122,657)
Deferred	**(86,761)**	138,597
Income tax expense	**$ 208,302**	$ 15,940

The Company's income tax expense differs from the amounts computed by applying the federal income tax statutory rates to income before income taxes. A reconciliation of the differences is as follows:

	Years Ended December 31,	
	2011	2010
Tax provision at federal statutory rate	**$ 491,147**	$ 228,065
Tax-exempt interest	**(201,240)**	(152,222)
Cash surrender value income	**(115,703)**	(113,351)
State income taxes	**29,252**	30,465
Other items, net	**4,846**	22,983
Income tax expense	**$ 208,302**	$ 15,940

NOTE 10. INCOME TAXES (Continued)

The components of the net deferred tax liabilities, included in other liabilities, are as follows:

	December 31,	
	2011	2010
Deferred tax assets:		
Alternative minimum tax credit	**$ 328,045**	$ 245,408
Loan loss reserves	**853,348**	935,656
Other real estate losses	**58,668**	23,311
Other	**10,260**	21,308
	1,250,321	1,225,683
Deferred tax liabilities:		
Depreciation	**(611,343)**	(665,774)
Unrealized gain on securities available for sale	**(1,304,181)**	(688,791)
Other	**(28,402)**	(36,094)
	(1,943,926)	(1,390,659)
Net deferred tax liabilities	**$ (693,605)**	$ (164,976)

NOTE 11. COMPENSATION AND BENEFITS

The Company maintains a noncontributory profit sharing plan and a contributory 401(k) plan. The Company's contributions to these plans were $73,295 and $83,564 in fiscal years ended December 31, 2011 and 2010, respectively.

The Company has an employment agreement with the chief executive officer which provides for compensation and benefits in the event the chief executive officer is terminated. The maximum aggregate liability at December 31, 2011 for termination is approximately $495,232.

NOTE 12. LOAN COMMITMENTS

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Such commitments involve, to varying degrees, elements of credit risk and interest rate risk in excess of the amount recognized in the balance sheets. The majority of all commitments to extend credit and standby letters of credit are variable rate instruments.

The Company's exposure to credit loss is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments as it does for on-balance sheet instruments. A summary of the Company's commitments is as follows:

	December 31,	
	2011	2010
Commitments to extend credit	**$ 17,170,162**	$ 21,173,175
Financial standby letters of credit	**10,000**	470,400
	$ 17,180,162	$ 21,643,575

NOTE 12. LOAN COMMITMENTS (Continued)

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

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those letters of credit are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. Collateral held varies and is required in instances which the Company deems necessary.

At December 31, 2011 and 2010, the carrying amount of liabilities related to the Company's obligation to perform under standby letters of credit was insignificant. The Company has not been required to perform on any standby letters of credit, and the Company has not incurred any losses on financial standby letters of credit for the years ended December 31, 2011 and 2010.

NOTE 13. CONTINGENCIES

In the normal course of business, the Company is involved in various legal proceedings. In the opinion of management, any liability resulting from such proceedings would not have a material effect on the Company's financial statements.

NOTE 14. REGULATORY MATTERS

Dividends are paid by the Company from funds provided by dividends from the Bank. However, certain regulatory restrictions exist regarding the ability of the Bank to transfer funds to the Company in the form of cash dividends, loans, or advances. As of December 31, 2011, approximately $520,000 of retained earnings was available for dividend declaration without regulatory approval.

The Company and the Bank are subject to various regulatory capital requirements that prescribe quantitative measures of the Company's and Bank's assets, liabilities, and certain off-balance sheet items. The regulators have also imposed qualitative guidelines for capital amounts and classifications such as risk weightings, capital components, and other details. The quantitative measures to ensure capital adequacy require that the Company and the Bank maintain amounts and ratios, as set forth in the schedule below, of Total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier I capital to average total assets (as defined). Failure to meet minimum capital requirements can initiate certain actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Management believes, as of December 31, 2011 and 2010, that the Company and the Bank meet all capital adequacy requirements imposed by its regulators.

As of December 31, 2011 and 2010, the most recent notification from the Federal Deposit Insurance Corporation categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum Total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the table. There have been no conditions or events since that notification that management believes have changed the institution's category.

NOTE 14. REGULATORY MATTERS (Continued)

Actual capital amounts as well as required and well capitalized Tier I, Total, and Tier I leverage ratios as of December 31, 2011 and 2010 for the Company and Bank are as follows:

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in Thousands)			
As of December 31, 2011:						
Total Capital to Risk Weighted Assets:						
Consolidated	**$ 24,165**	**19.0%**	**$ 10,164**	**8.0%**	**N/A**	**N/A**
Bank	**$ 23,081**	**18.2%**	**$ 10,070**	**8.0%**	**$ 12,588**	**10.0%**
Tier 1 Capital to Risk Weighted Assets:						
Consolidated	**$ 23,017**	**18.1%**	**$ 5,082**	**4.0%**	**N/A**	**N/A**
Bank	**$ 21,933**	**17.4%**	**$ 5,035**	**4.0%**	**$ 7,533**	**6.0%**
Tier 1 Capital to Average Assets:						
Consolidated	**$ 23,017**	**11.3%**	**$ 8,163**	**4.0%**	**N/A**	**N/A**
Bank	**$ 21,933**	**10.8%**	**$ 8,160**	**4.0%**	**$ 10,200**	**5.0%**
As of December 31, 2010:						
Total Capital to Risk Weighted Assets:						
Consolidated	$ 24,011	18.1%	$ 10,631	8.0%	N/A	N/A
Bank	$ 22,439	16.9%	$ 10,636	8.0%	$ 13,295	10.0%
Tier 1 Capital to Risk Weighted Assets:						
Consolidated	$ 22,340	16.8%	$ 5,316	4.0%	N/A	N/A
Bank	$ 20,768	15.6%	$ 5,318	4.0%	$ 7,977	6.0%
Tier 1 Capital to Average Assets:						
Consolidated	$ 22,340	10.7%	$ 8,338	4.0%	N/A	N/A
Bank	$ 20,768	10.0%	$ 8,334	4.0%	$ 10,418	5.0%

NOTE 15. FAIR VALUE OF ASSETS AND LIABILITIES

Determination of Fair Value

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. In accordance with the Fair Value Measurements and Disclosures topic (FASB ASC 820), the fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. 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. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

NOTE 15. FAIR VALUE OF ASSETS AND LIABILITIES (Continued)

Determination of Fair Value (Continued)

The fair value guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions.

Fair Value Hierarchy

In accordance with this guidance, the Company groups its financial assets and financial liabilities generally measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

Level 1 - Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include debt and equity securities that are traded in an active exchange market, as well as certain U.S. treasury and U.S. Government-sponsored enterprise debt securities that are highly liquid and are actively traded in over-the-counter markets.

Level 2 - Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include debt securities with quoted prices that are traded less frequently than exchange-traded instruments and derivative contracts whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data.

Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

NOTE 15. FAIR VALUE OF ASSETS AND LIABILITIES (Continued)

The following methods and assumptions were used by the Company in estimating fair value disclosures for financial instruments:

Cash and Cash Equivalents and Interest-Bearing Deposits: The carrying amounts of cash and short-term instruments approximate fair values based on the short-term nature of the assets.

Securities Available for Sale: Where quoted prices are available in an active market, we classify the securities within level 1 of the valuation hierarchy. Securities are defined as both long and short positions. Level 1 securities include highly liquid government bonds and exchange-traded equities.

If quoted market prices are not available, we estimate fair values using pricing models and discounted cash flows that consider standard input factors such as observable market data, benchmark yields, interest rate volatilities, broker/dealer quotes, and credit spreads. Examples of such instruments, which would generally be classified within level 2 of the valuation hierarchy, include GSE obligations, corporate bonds, municipal securities, and other securities. Mortgage-backed securities are included in level 2 if observable inputs are available. In certain cases where there is limited activity or less transparency around inputs to the valuation, we classify those securities in level 3.

Restricted Equity Securities: The carrying amount of restricted equity securities is its cost basis.

Loans Held for Sale: Substantially all of the Company's loans held for sale, primarily to third-party investors, have a readily determinable fair value. Fair values for these loans are based on quoted market prices, where available. If not available, fair values are based on market prices of comparable instruments. The carrying amount of accrued interest on these instruments approximates its fair value.

Loans Receivable: For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair value for fixed rate loans are estimated using discounted cash flow analyses, using market interest rates for comparable loans. Fair values for nonperforming loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

Deposit Liabilities: The fair values disclosed for demand deposits (for example, interest and noninterest checking, passbook savings, and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). The carrying amounts of variable-rate, fixed-term money market accounts and certificates of deposit approximate their fair values at the reporting date. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates on comparable instruments to a schedule of aggregated expected monthly maturities on time deposits.

Subordinated Debt: The carrying amount of subordinated debt approximates its fair value.

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

Off-Balance Sheet Credit-Related Instruments: Fair values for off-balance sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing.

NOTE 15. FAIR VALUE OF ASSETS AND LIABILITIES (Continued)

Assets Measured at Fair Value on a Recurring Basis

Following is a description of the valuation methodologies used for instruments measured at fair value on a recurring basis and recognized in the accompanying balance sheet, as well as the general classification of such instruments pursuant to the valuation hierarchy.

The following table presents financial assets measured at fair value on a recurring basis:

		Fair Value Measurements at December 31, 2011 Using		
	Assets/Liabilities Measured at Fair Value December 31, 2011	**Quoted Prices In Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservabl Inputs (Level 3)**
		(Dollars in Thousands)		
Available for sale securities	**$ 75,734,778**	**$ -**	**$ 75,734,778**	**$ -**

		Fair Value Measurements at December 31, 2010 Using		
	Assets/Liabilities Measured at Fair Value December 31, 2010	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(Dollars in Thousands)		
Available for sale securities	$ 63,140,124	$ -	$ 63,140,124	$ -

Assets Measured at Fair Value on a Nonrecurring Basis

Following is a description of the valuation methodologies used for instruments measured at fair value on a nonrecurring basis and recognized in the accompanying balance sheet, as well as the general classification of such instruments pursuant to the valuation hierarchy.

Impaired Loans

Loan impairment is reported when full payment under the loan terms is not expected. Impaired loans are carried at the present value of estimated future cash flows using the loan's existing rate, or the fair value of collateral if the loan is collateral dependent. A portion of the allowance for loan losses is allocated to impaired loans if the value of such loans is deemed to be less than the unpaid balance. If these allocations cause the allowance for loan losses to require increase, such increase is reported as a component of the provision for loan losses. Loan losses are charged against the allowance when management believes the uncollectibility of a loan is confirmed. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the loan impairment as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the loan impairment as nonrecurring Level 3.

NOTE 15. FAIR VALUE OF ASSETS AND LIABILITIES (Continued)

Assets Measured at Fair Value on a Nonrecurring Basis (Continued)

Foreclosed Assets

Foreclosed assets are adjusted to fair value upon transfer of the loans to foreclosed assets. Subsequently, foreclosed assets are carried at the lower of carrying value or fair value. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the foreclosed assets as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the foreclosed asset as nonrecurring Level 3.

The following table presents the assets and liabilities carried on the balance sheet by caption and by level within the FASB ASC 820 valuation hierarchy (as described above) as of December 31, 2011 and 2010, for which a nonrecurring change in fair value has been recorded during the years ended December 31, 2011 and 2010.

	Fair Value Measurements at December 31, 2011 Using				
	Total	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Year Ended December 31, 2011 Total Losses**
Impaired loans	**$ 4,182,051**	**$ -**	**$ -**	**$ 4,182,051**	**$ (122,972)**
Foreclosed	**403,881**	**-**	**-**	**403,881**	**(136,552)**
					$ (259,524)

	Fair Value Measurements at December 31, 2010 Using				
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Year Ended December 31, 2010 Total Losses
Impaired loans	$ 4,638,267	$ -	$ -	$ 4,638,267	$ (1,134,470)
Foreclosed assets	587,450	-	-	587,450	(42,862)
					$ (1,177,332)

NOTE 15. FAIR VALUE OF ASSETS AND LIABILITIES (Continued)

The carrying amount and estimated fair value of the Company's financial instruments were as follows:

	December 31,			
	2011		2010	
	Carrying Amount	**Fair Value**	Carrying Amount	Fair Value
	(Dollars in Thousands)			
Financial assets:				
Cash and cash equivalents	**$ 2,511**	**$ 2,511**	$ 3,487	$ 3,487
Interest-bearing deposits in banks	**1,613**	**1,613**	3,149	3,149
Securities available for sale	**72,735**	**75,735**	63,140	63,140
Restricted equity securities	**958**	**958**	1,255	1,255
Loans held for sale	**-**	**-**	251	251
Loans receivable, net	**102,446**	**102,145**	113,158	114,178
Accrued interest receivable	**1,018**	**1,018**	1,035	1,035
Financial liabilities:				
Deposits	**171,562**	**172,944**	175,374	175,975
Subordinated debentures	**3,093**	**3,093**	3,093	3,093
Accrued interest payable	**182**	**182**	354	354

NOTE 16. PARENT COMPANY FINANCIAL INFORMATION

The following information presents the condensed statements of condition of Pinnacle Bancshares, Inc. as of December 31, 2011 and 2010 and the condensed statements of income and cash flows for the years then ended.

CONDENSED STATEMENTS OF CONDITION

	2011	2010
	(Dollars in Thousands)	
Assets		
Cash and cash equivalents	**$ 937**	$ 1,421
Investment in unconsolidated subsidiary	**93**	93
Investment in Pinnacle Bank	**24,343**	22,175
Other assets	**84**	85
Total assets	**$ 25,457**	$ 23,774
Liabilities and stockholders' equity		
Subordinated debentures	**$ 3,093**	$ 3,093
Other liabilities	**30**	28
Total liabilities	**3,123**	3,121
Stockholders' equity	**22,334**	20,653
Total liabilities and stockholders' equity	**$ 25,457**	$ 23,774

NOTE 16. PARENT COMPANY FINANCIAL INFORMATION (Continued)

CONDENSED STATEMENTS OF INCOME

	2011	2010
	(Dollars in Thousands)	
Income		
Dividend income from Pinnacle Bank	**$ 140**	$ 942
Interest income	**7**	9
	147	951
Expense, other	**76**	75
Income before undistributed earnings (distributions in excess) of subsidiary	**71**	876
Equity in undistributed earnings (distributions in excess) of subsidiary	**1,165**	(221)
Net income	**$ 1,236**	$ 655

CONDENSED STATEMENTS OF CASH FLOWS

	2011	2010
	(Dollars in Thousands)	
OPERATING ACTIVITIES		
Net income	**$ 1,236**	$ 655
Adjustments to reconcile net income to net cash provided by operating activities:		
(Equity in) distributions in excess of undistributed earnings of subsidiary	**(1,165)**	221
Decrease in other assets	**1**	367
Increase (decrease) in other liabilities	**3**	(2)
Net cash provided by operating activities	**75**	1,241
FINANCING ACTIVITIES		
Dividends paid	**(559)**	(559)
Net cash used in financing activities	**(559)**	(559)
Net increase (decrease) in cash and cash equivalents	**(484)**	682
Cash and cash equivalents at beginning of year	**1,421**	739
Cash and cash equivalents at end of year	**$ 937**	$ 1,421

1811 SECOND AVENUE • JASPER, AL 35501
(205) 221-4111