FIRST CITIZENS BANCSHARES INC /TN/
Form 10-Q
May 09, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark one)

[**X**] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURTIES EXCHANGE ACT OF 1934

For the quarterly period ended **March 31, 2012**

Or

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

For the transition period from _______ to ________.

Commission File Number**: 0-11709**

FIRST CITIZENS BANCSHARES, INC.

(Exact name of registrant as specified in its charter)

Tennessee	**62-1180360**
(State of Incorporation)	(IRS Employer Id. No.)

P. O. Box 370, One First Citizens Place

Dyersburg, TN 38024

(Address of principal executive offices including zip code)

731-285-4410

(Registrant s telephone number including area code)

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

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

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

Large accelerated filer [ ]	Accelerated filer [X]
Non-accelerated filer[ ] (Do not check if a smaller reporting company)	Smaller reporting company [ ]

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

Of the registrant's only class of common stock (no par value), there were 3,607,854 shares outstanding as of May 3, 2012.

PART I-FINANCIAL INFORMATION

Item 1. Financial Statements

FIRST CITIZENS BANCSHARES, INC. & SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

AS OF MARCH 31, 2012 AND DECEMBER 31, 2011

(In Thousands)

	March 31, 2012	December 31, 2011[1]
	(UNAUDITED)	
ASSETS		
Cash and due from banks	$ 13,979	$ 19,460
Federal funds sold	32,260	14,673
Cash and cash equivalents	46,239	34,133
Interest bearing deposits in banks	35,409	40,138
Investment securities:		
Available-for-Sale, stated at market	372,743	365,465
Loans (excluding unearned income of $344 at March 31, 2012 and $352 at December 31, 2011)	533,405	527,699
Less: allowance for loan losses	8,435	8,039
Net loans	524,970	519,660
Loans held-for-sale	3,076	2,616
Federal Home Loan Bank and Federal Reserve Bank stocks, at cost	5,684	5,684
Premises and equipment	29,400	29,553
Accrued interest receivable	4,992	5,306
Goodwill	11,825	11,825
Other intangible assets	14	35

Other real estate owned	10,832	11,073
Bank owned life insurance policies	21,570	21,438
Other assets	6,703	6,623
TOTAL ASSETS	$1,073,457	$1,053,549
LIABILITIES AND EQUITY		
Non-interest bearing demand deposits	$122,390	$119,689
Interest bearing time deposits	339,902	341,141
Interest bearing savings deposits	413,599	394,842
Total deposits	875,891	855,672
Securities sold under agreements to repurchase	33,783	36,471
Other borrowings	47,222	47,328
Other liabilities	10,148	10,610
Total liabilities	967,044	950,081

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FIRST CITIZENS BANCSHARES, INC. & SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS (cont d)

AS OF MARCH 31, 2012 AND DECEMBER 31, 2011

(In Thousands)

	March 31, 2012	December 31, 2011[1]
	(UNAUDITED)	
Equity		
Common stock, no par value - 10,000,000 authorized; 3,717,593 issued and outstanding at March 31, 2012 and December 31, 2011	$ 3,718	$ 3,718
Surplus	15,331	15,331
Retained earnings	79,200	76,586
Accumulated other comprehensive income	9,132	8,801
Total common stock and retained earnings	107,381	104,436
Less-109,739 treasury shares, at cost as of March 31, 2012 and December 31, 2011	3,023	3,023
Total shareholders' equity	104,358	101,413
Noncontrolling (minority) interest in consolidated subsidiary	2,055	2,055
Total equity	106,413	103,468
TOTAL LIABILITITES AND EQUITY	$1,073,457	$1,053,549

[1] Derived from audited financial statements.

See accompanying notes to consolidated financial statements.

FIRST CITIZENS BANCSHARES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

THREE MONTHS ENDED MARCH 31, 2012 AND 2011

(Dollars in Thousands Except for Per Share Amounts)

	Three Months Ended	
	March 31, 2012	March 31, 2011
Interest income:		
Interest and fees on loans	$8,029	$8,506
Interest income on securities:		
Taxable	1,778	1,580
Tax-exempt	1,129	1,073
Dividends	55	56
Other interest income	36	20
Total interest income	11,027	11,235
Interest expense:		
Interest expense on deposits	1,670	2,042
Other interest expense	383	442
Total interest expense	2,053	2,484
Net interest income	8,974	8,751
Provision for loan losses	-	575
Net interest income after provision	8,974	8,176
Non-interest income		
Mortgage banking income	307	163
Income for fiduciary activities	183	187
Service charges on deposits accounts	1,722	1,607
Brokerage fees	293	303
Gain on sale of securities	401	462
Loss on sale of foreclosed property	(151)	(353)
Gain on disposition of property	0	273
Earnings on bank owned life insurance	160	184
Income from insurance activities	250	203
Other non-interest income	179	178

		Total non-interest income		3,344		3,207

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FIRST CITIZENS BANCSHARES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED) (cont d)

THREE MONTHS ENDED MARCH 31, 2012 AND 2011

(Dollars in Thousands Except for Per Share Amounts)

	Three Months Ended	
	March 31, 2012	March 31, 2011
Non-interest expense		
Salaries and employee benefits	$4,380	$4,084
Net occupancy expense	409	419
Depreciation expense	430	425
Data processing expense	403	497
Legal fees	110	70
Stationary and office supplies	62	55
Amortization of intangibles	21	21
Advertising and promotions	182	162
FDIC insurance premium expense	180	218
Other real estate expense	128	209
Other non-interest expense	1,357	1,308
Total non-interest expense	7,662	7,468
Net income before income taxes	4,656	3,915
Income taxes	1,140	919
Net income	$3,516	$2,996
Earnings per share	$0.97	$0.83
Weighted average number of shares outstanding	3,607,854	3,625,826

See accompanying notes to consolidated financial statements.

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FIRST CITIZENS BANCSHARES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY (UNAUDITED)

THREE MONTHS ENDED MARCH 31, 2012 AND 2011

(In Thousands)

	Common Stock			Retained	Accum. Other Compre.	Treasury	Non-Controlling	
	Shares	Amount	Surplus	Earnings	Income	Stock	Interests	Total
	(#)	($)	($)	($)	($)	($)		($)
Balance January 1, 2011	3,718	$3,718	$15,331	$68,696	$1,896	$(2,417)	$2,055	$89,279
Comprehensive income:								
Net income, quarter ended March 31, 2011				2,996				2,996
Adjustment of unrealized gain (loss) on securities available-for-sale, net of tax					1,297			1,297
Total comprehensive income				2,996	1,297			4,293
Cash dividends paid - $0.20 per share				(725)				(725)
Balance March 31, 2011	3,718	$3,718	$15,331	$70,967	$3,193	$(2,417)	$2,055	$97,140
Balance January 1, 2012	3,718	$3,718	$15,331	$76,586	$8,801	$(3,023)	$2,055	$103,468
Comprehensive income:								
Net income, quarter ended March 31, 2012				3,516				3,516
Adjustment of unrealized gain (loss) on securities available-for-sale, net of tax					331			331
Total comprehensive income				3,516	331			3,847
Cash dividends paid - $0.25 per share				(902)				(902)
Balance March 31, 2012	3,718	$3,718	$15,331	$79,200	$9,132	$(3,023)	$2,055	$106,413

See accompanying notes to consolidated financial statements.

FIRST CITIZENS BANCSHARES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (UNAUDITED)

FOR THE THREE MONTHS ENDED MARCH 31, 2012 AND 2011

(Dollars in Thousands)

	Three Months Ended	
	March 31, 2012	March 31, 2011
Net cash provided by operating activities	$ 3,182	$ 3,441
Investing activities:		
Decrease (increase) in interest bearing deposits in banks	4,729	(23,854)
Proceeds of maturities of available-for-sale securities	16,928	14,069
Proceeds of sales of available-for-sale securities	22,246	19,680
Purchase of available-for-sale securities	(45,773)	(44,993)
Decrease (Increase) in loans-net	(6,003)	432
Proceeds from sale of other real estate	551	1,436
Proceeds from disposition of property	-	328
Purchases of premises and equipment	(277)	(134)
Net cash (used) by investing activities	(7,599)	(33,036)
Financing activities:		
Net increase in demand accounts	2,701	9,305
Net increase in savings accounts	18,757	23,862
Net (decrease) in time deposits	(1,239)	(1,271)
Increase (decrease) in other borrowings	(106)	(6,623)
Cash dividends paid	(902)	(725)
Net increase (decrease) in securities sold under agreements to repurchase	(2,688)	(508)
Net cash provided by financing activities	16,523	24,040
Increase (decrease) in cash and cash equivalents	12,106	(5,555)
Cash and cash equivalents at beginning of period	34,133	33,691
Cash and cash equivalents at end of period	$46,239	$28,136

Supplemental cash flow disclosures:		
Interest payments, net	$2,020	$2,579
Income taxes paid, net	-	-
Transfers from loans to foreclosed assets	580	260
Transfers from foreclosed assets to loans	121	-

See accompanying notes to consolidated financial statements.

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FIRST CITIZENS BANCSHARES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2012

Note 1 - Consolidated Financial Statements

The consolidated balance sheet as of March 31, 2012, the consolidated statements of income for the three months ended March 31, 2012 and 2011 and the consolidated statements of cash flows for the three-month periods then ended have been prepared by the company without an audit. The accompanying reviewed condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments necessary to present fairly the financial position, results of operations and cash flows at March 31, 2012 and for all periods presented have been made. Operating results for the reporting periods presented are not necessarily indicative of results that may be expected for the year ending December 31, 2012. For further information, refer to the consolidated financial statements and footnotes thereto included in the company s Annual Report on Form 10-K for the year ended December 31, 2011.

Certain prior year balances have been reclassified to conform to current year presentation. The consolidated financial statements include all accounts of First Citizens Bancshares, Inc. (the Company), and its subsidiary, First Citizens National Bank (the Bank). First Citizens (TN) Statutory Trusts III and IV are reported under the equity method in accordance with generally accepted accounting principles for Variable Interest Entities for all periods presented. These investments are included in other assets and the proportionate share of income (loss) is included in other non-interest income. The Bank also has two wholly owned subsidiaries, First Citizens Financial Plus, Inc. and First Citizens Investments, Inc., which are consolidated into its financial statements.

The principal activity of First Citizens Investments, Inc. is to acquire and sell investment securities and collect income from the securities portfolio. First Citizens Holdings, Inc., a wholly owned subsidiary of First Citizens Investments, Inc., acquires and sells certain investment securities, collects income from its portfolio, and owns First Citizens Properties, Inc., a real estate investment trust. First Citizens Properties, Inc. is a real estate investment trust organized and existing under the laws of the state of Maryland, the principal activity of which is to invest in participation interests in real estate loans made by the Bank and provide the Bank with an alternative vehicle for raising capital. First Citizens Holdings, Inc. owns 100% of the outstanding common stock and 60% of the outstanding preferred stock of First Citizens Properties, Inc. Directors, executive officers and certain employees and affiliates of the Bank own approximately 40% of the preferred stock which is reported as Noncontrolling Interest in Consolidated Subsidiary in the Consolidated Financial Statements of the Company. Net income (loss) attributable to the noncontrolling interest is included in Other Non-Interest Expense on the Consolidated Statements of Income and is not material for any of the periods presented.

The Bank has a 50% ownership interest in two insurance subsidiaries both of which are accounted for using the equity method. One is White and Associates/First Citizens Insurance, LLC, which is a general insurance agency offering a full line of insurance products. The other is First Citizens/White and Associates Insurance Company whose principal activity is credit insurance. The investment in these subsidiaries is included in Other Assets on the Balance Sheets presented in this report and earnings from these subsidiaries are recorded in Other Income on the Income Statements presented in this report.

Note 2 - Organization

First Citizens Bancshares, Inc., is a bank holding company chartered December 14, 1982, under the laws of the State of Tennessee. On September 23, 1983, all outstanding shares of common stock of First Citizens National Bank were exchanged for an equal number of shares in First Citizens Bancshares, Inc.

Note 3 Contingent Liabilities

There is no material pending or threatened litigation as of the current reportable date that would result in a liability.

Note 4 -- Cash Reserves and Interest-Bearing Deposits in Other Banks

The Bank maintains cash reserve balances as required by the Federal Reserve Bank. Average required balances during first quarter ended March 31, 2012 and the year ended December 31, 2011 were approximately $500,000. Amounts above the required minimum balance are reported as Interest-Bearing Deposits in Other Banks on the Consolidated Balance Sheets. Balances in excess of required reserves held at the Federal Reserve Bank as of March 31, 2012 and December 31, 2011 were $33.6 million and $38.3 million, respectively. Interest-bearing deposits in other banks also include short-term certificates of deposit held in increments that are within FDIC insurance limits and totaled $1.8 million and approximately $1.6 million as of March 31, 2012 and December 31, 2011, respectively.

Note 5 Investment Securities

The amortized cost and fair value of securities as of March 31, 2012 and December 31, 2011 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
As of March 31, 2012:				
U.S. Treasury securities and obligations of U.S. government agencies and corporations	$249,056	$7,137	$ (63)	$256,130
Obligations of states and political subdivisions	106,723	9,376	(5)	116,094
All other	2,166	21	(1,668)	519
Total investment securities	$357,945	$16,534	$(1,736)	$372,743
As of December 31, 2011:				
U.S. Treasury securities and obligations of U.S. government agencies and corporations	$242,459	$6,793	$ (12)	$249,240

Obligations of states and political subdivisions	106,554	9,083	(3)	115,634
All other	2,194	15	(1,618)	591
Total investment securities	$351,207	$15,891	$(1,633)	$365,465

There were no securities classified as held-to-maturity or trading as of March 31, 2012 or December 31, 2011.

The following table summarizes contractual maturities of debt securities available-for-sale as of March 31, 2012 (in thousands):

	Amortized Cost	Fair Value
Amounts maturing in:		
One year or less	$3,200	$3,269
After one year through five years	8,415	9,070
After five years through ten years	49,815	55,818
After ten years*	296,492	304,542
Total debt securities	357,922	372,699
Equity securities	23	44
Total securities	$357,945	$372,743

Sales and gains (losses) on sale of available-for-sale securities for the quarter ended March 31, 2012 and 2011 are presented as follows (in thousands):

	Gross Sales	Gross Gains	Gross Losses	Net Gains
2012	$22,246	$401	$ -	$401
2011	19,680	462	-	462

The following table presents information on securities with gross unrealized losses as of March 31, 2012, aggregated by investment category and the length of time that the individual securities have been in a continuous loss position (in thousands):

	Less Than 12 Months		Over 12 Months		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
U.S. Treasury securities and obligations of U.S. Government agencies and corporations	$(63)	$15,296	$ -	$ -	$ (63)	$15,296
Obligations of states and political subdivisions	(5)	475	-	-	(5)	475
Other debt securities	-	-	(1,668)	475	(1,668)	475
Total securities with unrealized losses	$(68)	$15,771	$(1,668)	$475	$(1,736)	$16,246

In reviewing the investment portfolio for other-than-temporary impairment of individual securities, consideration is given but not limited to (1) the length of time in which fair value has been less than cost and the extent of the unrealized loss, (2) the financial condition of the issuer, and (3) the positive intent and ability of the Company to maintain its investment in the issuer for a time that would provide for any anticipated recovery in the fair value.

As of March 31, 2012, the Company had eight debt securities with unrealized losses, with 3 of those securities having been in an unrealized loss position for greater than 12 months. The Company did not intend to sell any such securities in unrealized loss position and it was more likely than not that the Company would not be required to sell the securities prior to recovery of costs. Of the eight securities, three corporate debt securities accounted for approximately 96% of the unrealized gross losses as of March 31, 2012. The remaining bonds had unrealized loss positions for less than 12 months and consisted of two municipal bonds and three agency MBSs or CMOs. Securities in an unrealized loss position as of March 31, 2012 have been evaluated for other-than-temporary impairment. In analyzing reasons for the unrealized losses, management considers various factors including, but not limited to, whether the securities are issued by the federal government or its agencies, whether downgrades of bond ratings have occurred, and also reviews any applicable industry analysts reports. With respect to unrealized losses on municipal and agency and the analysis performed relating to the securities, management believes that declines in market value were not other-than-temporary as of March 31, 2012. The unrealized losses on the agency and municipal securities are considered immaterial on an individual basis and in the aggregate and have not been recognized for other-than-temporary impairment.

Three corporate debt securities accounted for $1.67 million of the $1.74 million unrealized loss as of March 31, 2012 and consist of pooled collateralized debt obligation securities that are backed by trust-preferred securities (TRUP CDOs) issued by banks, thrifts and insurance companies. These three bonds were rated below investment grade (BBB) by Moody s and/or S&P as of March 31, 2012.

The three TRUP CDOs have an aggregate book value of $2.1 million and fair market value of approximately $475,000 and each of the three are the mezzanine or B class tranches. The unrealized loss of $1.7 million as of March 31, 2012 is reflected in accumulated other comprehensive income. The following table provides the book and market values of each security as well as information regarding the levels of excess subordination in the securities as of March 31, 2012 (dollars in thousands):

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Description	Class	Book Value	Market Value	Actual Over Collateral Ratio (2)	Required Over Collateral Ratio (3)	Actual Over (Under)
Pretsl I	Mezzanine	$839(1)	$258	77.78%	103.0%	-30.25%
Pretsl X	B-2	304(1)	6	55.49%	n/a (4)	-80.21%
I-Prestsl IV	B-1	1,000	211	106.4%	106.0%	6.04%

(1) Book values reflect principal only and do not include interest capitalized or payment-in-kind (PIK) to the bond according to contractual terms of the bond if applicable. The Company does not recognize PIK interest for book purposes and has these bonds on non-accrual status.

(2) The Over Collateral (OC) Ratio reflects the ratio of performing collateral to a given class of notes and is calculated by dividing the performing collateral by the sum of the current balance of a given class of notes plus all senior classes.

(3) The Required OC Ratio for a particular class of bonds reflects the required overcollateralization ratio such that cash distributions may be made to lower classes of bonds. If the OC Ratio is less than the Required OC ratio, cash is diverted from the lower classes of bonds to the senior bond classes.

(4) The Required OC Ratio is not applicable in this case, as interest on Pretsl X for B-2 class is capitalized to the bond or PIK.

Security-specific collateral is used in the assumptions to project cash flows each quarter. Issuers in default are assumed at zero recovery. Issuers in deferral are assumed at a 15% recovery beginning two years from deferral date. Forward interest rates are used to project future principal and interest payments allowing the model to indicate impact of over or undercollateralization for each transaction. Higher interest rates generally increase credit stress on undercollateralized transactions by reducing excess interest (calculated as the difference between interest received from underlying collateral and interest paid on the bonds). The discount rate is based on the original discount margin calculated at the time of purchase based on the purchase price. The original discount margin is then added to the three-month LIBOR to determine the discount rate. The discount rate is then used to calculate the present value for the then-current quarter s projected cash flows. If the present value of the then-current quarter s projected cash flows is less than the prior quarter or less than the then-current book value of the security, that difference is recorded against earnings as the credit component of other-than-temporary impairment. No additional credit losses were incurred during the quarter ended March 31, 2012 and therefore no losses were recognized against earnings during first quarter 2012.

See also discussion of valuation techniques and hierarchy for determining fair value of these securities at Note 11.

The Company held no derivative transactions as of March 31, 2012 or December 31, 2011.

Note 6 -- Loans

Performing and non-performing loans by category were as follows as of March 31, 2012 and December 31, 2011 (in thousands):

	Performing	Non- Performing*	Total
March 31, 2012:			
Commercial, financial and agricultural	$73,312	$701	$74,013
Real estate construction	38,449	673	39,122
Real estate mortgage	380,105	8,398	388,503
Installment loans to individuals	26,690	249	26,939
All other loans	4,828	0	4,828
Total	$523,384	$10,021	$533,405
December 31, 2011:			
Commercial, financial and agricultural	$71,465	$709	$ 72,174
Real estate construction	38,946	1,018	39,964
Real estate mortgage	378,006	5,928	383,934
Installment loans to individuals	27,766	261	28,027
All other loans	3,600	-	3,600
Total	$ 519,783	$7,916	$527,699

*Non-Performing loans consist of loans that are on non-accrual status and loans 90 days past due and still accruing interest.

An aging analysis of loans outstanding by category as of March 31, 2012 and December 31, 2011 was as follows (in thousands):

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Recorded Investment > 90 Days and Accruing
As of March 31, 2012:							
Commercial, financial and agricultural	$ 175	$ 65	$ 534	$ 774	$ 73,239	$ 74,013	$ 35
Real estate construction	234	0	0	234	38,888	39,122	0
Real estate mortgage	3,830	151	4,780	8,761	379,742	388,503	2,717
Installment loans to individuals	180	5	12	197	26,742	26,939	9
All other loans	0	0	0	0	4,828	4,828	0
Total	$4,419	$221	$5,326	$9,966	$523,439	$533,405	$2,761
As of December 31, 2011:							
Commercial, financial and agricultural	$ 72	$ 72	$ 538	$ 682	$ 71,492	$ 72,174	$ 34
Real estate construction	539	47	345	931	39,033	39,964	-
Real estate mortgage	1,481	2,727	2,353	6,561	377,373	383,934	570
Installment loans to individuals	81	30	41	152	27,875	28,027	2
All other loans	-	-	-	-	3,600	3,600	-
Total	$2,173	$2,876	$3,277	$8,326	$519,373	$527,699	$606

Loans on non-accrual status as of March 31, 2012 and December 31, 2011 by category were as follows (in thousands):

	March 31, 2012	December 31, 2011
Commercial, financial and agricultural	$ 667	$ 675
Real estate construction	673	1,018
Real estate mortgage	5,680	5,358
Installment loans to individuals	240	259
All other loans	-	-
Total	$7,260	$7,310

Note 5 Investment Securities

Credit risk management procedures include assessment of loan quality through use of an internal loan rating system. Each loan is assigned a rating upon origination and the rating may be revised over the life of the loan as circumstances warrant. The rating system utilizes eight major classification types based on risk of loss with Grade 1 being the lowest level of risk and Grade 8 being the highest level of risk. Loans internally rated Grade 1 to Grade 4 are considered Pass grade loans with low to average level of risk of credit losses. Loans rated Grade 5 are considered Special Mention and generally have one or more circumstances that require additional monitoring but do not necessarily indicate a higher level of probable credit losses. Loans rated Grade 6 or higher are loans with circumstances that generally indicate an above average level of risk for credit losses. Loans by internal risk rating by category as of March 31, 2012 and December 31, 2011 were as follows (in thousands):

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	Grades 1-4	Grade 5	Grades 6-8	Total
March 31, 2012:				
Commercial, financial and agricultural	$ 72,295	$ 609	$ 1,109	$ 74,013
Real estate construction	36,161	1,254	1,707	39,122
Real estate mortgage	365,961	4,862	17,680	388,503
Installment loans to individuals	26,594	7	338	26,939
All other loans	4,828	-	-	4,828
Total	$ 505,839	$ 6,732	$20,834	$533,405
December 31, 2011:				
Commercial, financial and agricultural	$ 70,399	$ 423	$ 1,352	$ 72,174
Real estate construction	36,972	1,113	1,879	39,964
Real estate mortgage	362,686	4,715	16,533	383,934
Installment loans to individuals	27,701	9	317	28,027
All other loans	3,600	-	-	3,600
Total	$501,358	$6,260	$20,081	$527,699

Information regarding the Company s impaired loans for the quarter ended March 31, 2012 and 2011 is as follows (in thousands):

	Recorded Investment	Unpaid Principal Balance	Specific Allowance	Average Recorded Investment	Interest Income Recognized
March 31, 2012:					
With no specific allocation recorded:					
Commercial, financial and agricultural	$ -	$ -	N/A	$ 4	$ -
Real estate construction	-	-	N/A	-	-
Real estate mortgage	-	-	N/A	1,109	-
Installment loans to individuals	-	-	N/A	-	-
All other loans	-	-	N/A	-	-
With allocation recorded:					
Commercial, financial and agricultural	$ 648	$ 648	$ 130	$ 568	$ 2
Real estate construction	887	887	330	1,179	-
Real estate mortgage	7,406	7,406	1,497	5,973	3
Installment loans to individuals	160	160	33	174	-
All other loans	-	-	-	-	-
Total:					
Commercial, financial and agricultural	$ 648	$ 648	$ 130	$ 572	$ 2
Real estate construction	887	887	330	1,179	-
Real estate mortgage	7,406	7,406	1,497	7,082	3
Installment loans to individuals	160	160	33	174	-
All other loans	-	-	-	-	-

March 31, 2011:					
With no specific allocation recorded:					
Commercial, financial and agricultural	$ -	$ -	N/A	$ -	$ -
Real estate construction	-	-	N/A	420	-
Real estate mortgage	2,346	2,346	N/A	2,596	38
Installment loans to individuals	-	-	N/A	-	-
All other loans	-	-	N/A	-	-
With allocation recorded:					
Commercial, financial and agricultural	$ 609	$ 609	$160	$ 555	$ 8
Real estate construction	1,834	1,834	460	1,288	16
Real estate mortgage	5,967	5,967	953	5,089	63
Installment loans to individuals	218	218	42	209	-
All other loans	-	-	-	-	-
Total:					
Commercial, financial and agricultural	$ 609	$ 609	$160	$ 555	$ 8
Real estate construction	1,834	1,834	460	1,708	16
Real estate mortgage	8,313	8,313	953	7,685	101
Installment loans to individuals	218	218	42	209	-
All other loans	-	-	-	-	-

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The Company adopted amendments in Accounting Standards Codification Update (ASU) No. 2011-01 Receivables (Topic 310) (ASU 2011-01) as of September 30, 2011. As a result, the Company reviewed loans classified as troubled debt restructurings (TDRs) that had been restructured during the year ended December 31, 2011 and confirmed that TDRs with a balance greater than or equal to $250,000 deemed to be impaired were properly identified as such and reviewed individually for impairment as reported in the impaired loan table above. Loans meeting the criteria to be classified as TDRs with a balance less than $250,000 have historically been reviewed on a collective basis by risk code and loan category. Reassessment of these loans on an individual basis upon adoption of the ASU 2011-01 for impairment did not result in a significant difference in the required allowance, as the aggregate balance of loans reviewed was less than $20,000.

Generally, loans are appropriately risk rated and identified for individual impairment review prior to when the restructure occurs. Thus, in the normal life cycle of a loan, any specific allocations are usually made prior to a formal restructuring or at least at the time of restructuring rather than subsequent to modification. Therefore, adoption of these amendments did not have a material impact on the volume of loans classified as TDRs or the related allowance for loan losses associated with TDRs as of December 31, 2011 or March 31, 2012. Also, TDRs are included in non-accrual loans as reported in the above tables unless the loan has performed according to the modified terms for a length of time sufficient to support placing the loan on accrual status (generally six months).

Loans that were restructured as of March 31, 2012 consisted of the following (dollars in thousands):

	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled debt restructurings:			
Commercial, financial and agricultural	6	$372	$330
Real estate construction	9	1,604	1,591
Real estate mortgage	13	3,648	3,614
Installment loans to individuals	18	205	194
All other loans	0	0	0
Total	46	$5,829	$5,729

Note 5 Investment Securities

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Modification of the terms of the TDRs reported in the above table did not have a material impact on the consolidated financial statements or to the overall risk profile of the loan portfolio. There were no TDRs that were modified during the year ended December 31, 2011 that re-defaulted in the quarter ended March 31, 2012. The allowance for loan losses associated with the TDRs totaled approximately $1.1 million as of March 31, 2012.

Note 7 Allowance for Loan Losses

The following table presents the breakdown of the allowance for loan losses by category and the percentage of each category in the loan portfolio to total loans as of March 31, 2012 and December 31, 2011 (dollars in thousands):

	March 31, 2012		December 31, 2011	
	Amount	% to Total Loans	Amount	% to Total Loans
Commercial, financial and agricultural	$1,585	13.88%	$1,469	13.68%
Real estate construction	1,973	7.33%	1,614	7.57%
Real estate mortgage	4,485	72.83%	4,534	72.76%
Installment loans to individuals	351	5.05%	381	5.31%
All other loans	41	0.91%	41	0.68%
Total	$8,435	100.00%	$8,039	100.00%

An analysis of the allowance for loan losses by loan category for the quarter ended March 31, 2012 is as follows (in thousands):

-	Beginning Balance	Charge-offs	Recoveries	Provision	Ending Balance
Allowance for loan losses:					
Commercial, financial and agricultural	$1,469	($28)	$144	$-	$1,585
Real estate construction	1,614	(120)	479	-	1,973
Real estate mortgage	4,534	(53)	4	-	4,485
Installment loans to individuals	381	(33)	3	-	351
All other loans	41	-	-	-	41
Total	$8,039	($234)	$630	$-	$8,435

The allowance for loan losses is comprised of allocations for loans evaluated individually and loans evaluated collectively for impairment. The allocations of the allowance for loan losses for outstanding loans by category evaluated individually and collectively were as follows as of March 31, 2012 and December 31, 2011 (in thousands):

Note 5   Investment Securities

	Evaluated Individually	Evaluated Collectively	Total
As of March 31, 2012:			
Allowance for loan losses			
Commercial, financial and agricultural	$ 130	$1,455	$1,585
Real estate construction	330	1,643	1,973
Real estate mortgage	1,497	2,988	4,485
Installment loans to individuals	33	318	351
All other loans	0	41	41
Total	$1,990	$6,445	$8,435
Loans			
Commercial, financial and agricultural	$ 648	$73,365	$74,013
Real estate construction	887	38,235	39,122
Real estate mortgage	7,405	381,097	388,503
Installment loans to individuals	160	26,779	26,939
All other loans	-	4,828	4,828
Total	$9,101	$524,304	$533,405
As of December 31, 2011:			
Allowance for loan losses			
Commercial, financial and agricultural	$ 50	$ 1,419	$ 1,469
Real estate construction	350	1,264	1,614
Real estate mortgage	427	4,107	4,534
Installment loans to individuals	33	348	381
All other loans	-	41	41
Total	$860	$7,179	$8,039
Loans			
Commercial, financial and agricultural	$ 500	$71,674	$72,174
Real estate construction	1,007	38,957	39,964
Real estate mortgage	5,132	378,802	383,934
Installment loans to individuals	158	27,869	28,027
All other loans	-	3,600	3,600
Total	$6,797	$520,902	$527,699

Note 8 Goodwill and Intangible Assets

Goodwill is not amortized and is tested for impairment annually or more frequently if events and circumstances indicate that the asset might be impaired. The goodwill impairment test is conducted in first quarter annually and is a two-step test. The first step, used to identify potential impairment, involves comparing each reporting unit s estimated fair value to its carrying value, including goodwill. Currently the Company has one reporting unit and does not meet the tests to segment under generally accepted accounting standards. If the estimated fair value of the reporting unit exceeds its carrying value, goodwill is considered not to be impaired. If the carrying value exceeds estimated fair value, there is an indication of potential impairment and the second step is performed to measure the amount of impairment.

If required, the second step involves calculating an implied fair value of goodwill which is determined in a manner similar to the amount of goodwill calculated in a business combination, by measuring the excess of the estimated fair value of the reporting unit, as determined in the first step, over the aggregate estimated fair values of the individual assets, liabilities and identifiable intangibles as if the reporting unit was being acquired in a business combination. If the implied fair value of goodwill exceeds the carrying value of goodwill assigned to the reporting unit, there is no impairment. If the carrying value of goodwill exceeds the implied fair value of the goodwill, an impairment charge is recorded for the excess. An impairment loss cannot exceed the carrying value of goodwill.

The Company s stock price has historically traded above its book value per common share and tangible book value per common share and was trading above its book value per common share and tangible book value per common share as of March 31, 2012. In the event the stock price were to trade below its book value per common share and tangible book value per common share, an evaluation of the carrying value of goodwill would be performed as of the reporting date. Such a circumstance would be one factor in an evaluation that could result in an eventual goodwill impairment charge. Additionally, should future earnings and cash flows decline and/or discount rates increase, an impairment charge to goodwill and other intangible assets may also be required.

No impairment of goodwill is recorded in the current or prior reportable periods. Total goodwill as of the reportable date is $11.8 million or 1.10% of total assets or 11.33% of total capital.

Amortization expense of the other identifiable intangibles was approximately $21,000 for each of first quarters in 2012 and 2011.

Note 9 Borrowings

In March 2005, the Company formed a wholly owned subsidiary -- First Citizens (TN) Statutory Trust III. The trust was created as a Delaware statutory trust for the sole purpose of issuing and selling trust preferred securities and using proceeds from the sale to acquire long-term subordinated debentures issued by the Company. The debentures are the sole assets of the trust. The Company owns 100% of the common stock of the trust.

On March 17, 2005, the Company, through First Citizens (TN) Statutory Trust III, sold 5,000 of its floating rate trust preferred securities at a liquidation amount of $1,000 per security for an aggregate amount of $5.0 million. For the period beginning on (and including) the date of original issuance and ending on (but excluding) June 17, 2005, the rate per annum was 4.84%. For each successive period beginning on (and including) June 17, 2005, and each succeeding interest payment date, interest accrues at a rate per annum equal to the three-month LIBOR plus 1.80%. Interest payment dates are March 17, June 17, September 17, and December 17 during the 30-year term. The entire $5.0 million in proceeds was used to reduce other debt at the Company. The Company s obligation under the debentures and related documents constitute a full and unconditional guarantee by the Company of the trust issuer s obligations under the trust preferred securities.

In March 2007, the Company formed a wholly owned subsidiary -- First Citizens (TN) Statutory Trust IV. The trust was created as a Delaware statutory trust for the sole purpose of issuing and selling trust preferred securities and using proceeds from the sale to acquire long-term subordinated debentures issued by the Company. The debentures are the sole assets of the trust. The Company owns 100% of the common stock of the trust.

In March 2007, the Company, through First Citizens (TN) Statutory Trust IV, sold 5,000 of its floating rate trust preferred securities at a liquidation amount of $1,000 per security for an aggregate amount of $5.0 million. For the period beginning on (and including) the date of original issuance and ending on (but excluding) June 15, 2007, the rate per annum was 7.10%. For each successive period beginning on (and including) June 15, 2007, and each succeeding interest payment date, interest accrues at a rate per annum equal to the three-month LIBOR plus 1.75%. Interest payment dates are March 15, June 15, September 15, and December 15 during the 30-year term. The purpose of proceeds was to refinance the debt issued through First Citizens (TN) Statutory Trust II at a lower spread to LIBOR and results in savings of approximately $92,500 annually. First Citizens (TN) Statutory Trust II was dissolved as a result of this transaction. The Company s obligation under the debentures and related documents constitute a full and unconditional guarantee by the Company of the trust issuer s obligations under the trust preferred securities.

Although for accounting presentation the trust preferred securities are presented as debt, the outstanding balance qualifies as Tier I capital subject to the limitation that the amount of the securities included in Tier I Capital cannot exceed 25% of total Tier I capital.

The Company is dependent on the profitability of its subsidiaries and their ability to pay dividends in order to service its long-term debt.

The Bank had secured advances from the FHLB totaling $36.9 million as of March 31, 2012 and $37.1 million as of December 31, 2011. FHLB borrowings are comprised primarily of advances with principal due at call date or maturity date with fixed interest rates ranging from 0.62% to 7.05%. Some of these FHLB borrowings have quarterly call features and maturities ranging from 2012 to 2019. Advances totaling $16 million require repayment if the call feature is exercised. Under the existing and forecasted rate environments, borrowings with call features in place are not likely to be called in the next 12 months. The Bank had one London Interbank Offered Rate (LIBOR) based variable rate advance totaling $2.5 million with a rate of 0.34% as of March 31, 2012 and December 31, 2011. Also included in the FHLB borrowings total reported above is a pool of smaller balance amortizing advances that totaled approximately $912,000 as of March 31, 2012 and $1.0 million as of year-end 2011. These smaller balance advances have rates ranging from 3.34% to 7.05% and maturities range from 2012 to 2019. Obligations are secured by loans totaling $368 million consisting of the Bank s entire portfolio of fully disbursed, one-to-four family residential mortgages, commercial mortgages, farm mortgages, second mortgages and multi-family residential mortgages. The Bank had additional borrowing capacity of $119.8 million as of March 31, 2012.

Note 10 Bank Owned Life Insurance and Imputed Income Tax Reimbursement Agreements

The Bank has a significant investment in bank-owned life insurance policies (BOLI) and provides the associated fringe benefit to certain employees in the position of Vice President and higher after one year of service. The cash surrender values of BOLI were $21.6 million and $21.4 million as of March 31, 2012 and December 31, 2011, respectively. BOLI are initially recorded at the amount of premiums paid and are adjusted to current cash surrender values. Changes in cash surrender values are recorded in other non-interest income and are based on premiums paid less expenses plus accreted interest income. Earnings on BOLI resulted in non-interest income of approximately $160,000 and $184,000 for first quarters ended March 31, 2012 and 2011, respectively.

Expense related to these post-retirement death benefit accruals is reflected in Salaries and Employee Benefits on the Consolidated Income Statements and was approximately $42,000 for the quarter ended March 31, 2012 and approximately $49,000 for the quarter ended March 31, 2011. The accrual for the post-retirement death benefits is included in Other Liabilities on the Consolidated Balance Sheet and totaled $2.5 million as of March 31, 2012 and $2.4 million as of December 31, 2011.

Executive Management Life Insurance Death Benefit Only Salary Continuation Plans provided for in the employment agreements for certain officers of the Bank were replaced in December 2007 with Endorsement Split Dollar Life Insurance Plans and Amended and Restated Split Dollar Agreements. The new agreements combine the death benefits from the Bank s larger group plan with the death benefits established in the Executive Management Life Insurance Death Benefit Only Salary Continuation Plans. The new agreements did not change the total after-tax death benefit provided to each participant. Imputed Income Tax Reimbursement Agreements for each participant became effective January 1, 2008 and were entered into in order to keep the participants at the same after-tax benefit under the Amended and Restated Split Dollar Agreements. These Imputed Income Tax Reimbursement Agreements provide for annual cash payments to the participants until death beginning in March 2009 for the 2008 tax year in amounts equal to the portion of the amount of federal and state income taxes attributable to the income imputed to the participant on the benefit under the Amended and Restated Split Dollar Agreement.

Because the Endorsement Split Dollar Life Insurance Plans created imputed income to each participant without generating cash to pay the tax expense associated with the imputed income, and in order to provide participants the same after-tax benefit provided under the previous plans, effective January 1, 2008 the Bank entered into Imputed Income Tax Reimbursement Agreements with the applicable officers under the Amended and Restated Split Dollar Agreements. The Imputed Income Tax Reimbursement Agreements provide for annual cash payments to the participants until death beginning in March 2009 for the previous tax year in amounts equal to a portion of federal income taxes attributable to (i) the income imputed to the participant on the benefit under the Amended and Restated Split Dollar Agreement and (ii) the additional cash payments under the Imputed Income Tax Reimbursement Agreement.

Each participant was 100% vested in benefits provided under Imputed Income Tax Reimbursement Agreements as of January 1, 2008. Therefore, 100% of the principal (or service) cost of the plan was accrued for as of January 1, 2008 and expensed through earnings in the year ended December 31, 2008. Service costs are based on the net present value of the sum of payments in accordance with each participant s agreement. Interest accrues monthly at a rate of 7.0%.

Net other post-retirement benefits expense for Imputed Income Tax Reimbursement Agreements is included in Salaries and Employee Benefits on the Consolidated Statements of Income and totaled approximately $7,000 per quarter for the quarters ended March 31, 2012 and 2011. Benefit payments are made annually in March and totaled approximately $18,000 and $17,000 for the three months ended March 31, 2012 and 2011, respectively.

The accumulated post-retirement defined benefit obligation for Imputed Income Tax Reimbursement Agreements is included in Other Liabilities on the Consolidated Balance Sheet totaled approximately $390,000 as of March 31, 2012 and approximately $403,000 as of December 31, 2011. The accumulated post-retirement benefit obligation was equal to the funded status of the plan as of each applicable period-end as there were no related assets recognized on the Consolidated Balance Sheets for the Imputed Income Tax Reimbursement Agreements.

Note 11 Fair Value Measurements

Fair value measurements are used to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. The Company measures fair value under guidance provided by the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 820, Fair Value Measurements and Disclosures (AS

820). ASC 820 defines fair value, establishes a framework for measuring fair value and expands disclosure requirements regarding fair value measurements. ASC 820 does not expand the use of fair value in any new circumstances but clarifies the principle that fair value should be based on assumptions that market participants would use when pricing the asset or liability. ASC 820 outlines the following three acceptable valuation techniques may be used to measure fair value:

a. Market approach The market approach uses prices and other relevant information generated by market transactions involving identical or similar assets or liabilities. This technique includes matrix pricing that is a mathematical technique used principally to value debt securities without relying solely on quoted prices for specific securities but rather by relying on securities relationship to other benchmark quoted securities.

b. Income approach The income approach uses valuation techniques to convert future amounts such as earnings or cash flows to a single present discounted amount. The measurement is based on the value indicated by current market expectations about those future amounts. Such valuation techniques include present value techniques, option-pricing models (such as the Black-Scholes-Merton formula or a binomial model), and multi-period excess earnings method (used to measure fair value of certain intangible assets).

c. Cost approach The cost approach is based on current replacement cost which is the amount that would currently be required to replace the service capacity of an asset.

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Valuation techniques are selected as appropriate for the circumstances and for which sufficient data is available. Valuation techniques are to be consistently applied, but a change in valuation technique or its application may be made if the change results in a measurement that is equally or more representative of fair value under the circumstances. Revisions resulting from a change in valuation technique or its application are accounted for as a change in accounting estimate which does not require the change in accounting estimate to be accounted for by restating or retrospectively adjusting amounts reported in financial statements of prior periods or by reporting pro forma amounts for prior periods.

ASC 820 also establishes a hierarchy that prioritizes information used to develop those assumptions. The level in the hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company considers an input to be significant if it drives more than 10% of the total fair value of a particular asset or liability. The hierarchy is as follows:

- Level 1 Inputs (Highest ranking): Unadjusted quoted prices in active markets for identical assets or liabilities that the entity has the ability to access at the measurement date.

- Level 2 Inputs: Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Such inputs may include quoted prices for similar assets or liabilities in active markets, and inputs other than quoted market prices that are observable for the assets and liabilities such as interest rates and yield curves that are observable at commonly quoted intervals.

- Level 3 Inputs (Lowest ranking): Unobservable inputs for determining fair values of assets and liabilities that reflect an entity s own assumptions about the assumptions that market participants would use in pricing the assets and liabilities.

Assets and liabilities may be measured for fair value on a recurring basis (daily, weekly, monthly or quarterly) or on a non-recurring basis in periods subsequent to initial recognition. Recurring valuations are measured regularly for investment securities and the cash flow hedge. Loans held for sale, other real estate and impaired loans are measured at fair value on a non-recurring basis and do not necessarily result in a change in the amount recorded on the Consolidated Balance Sheets. Generally, these assets have non-recurring valuations that are the result of application of other accounting pronouncements that require the assets be assessed for impairment or at the lower of cost or fair value. Fair values of loans held for sale are considered Level 2. Fair values for other real estate and impaired loans are considered Level 3.

The Company obtains fair value measurements for securities and the cash flow hedge from a third party vendor. The cash flow hedge and the majority of the available-for-sale securities are valued using Level 2 inputs. Collateralized debt obligation securities that are backed by trust preferred securities and account for less than 1% of the available-for-sale securities portfolio are valued using Level 3 inputs. The fair value measurements reported in Level 2 are primarily matrix pricing that considers observable data (such as dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and terms and conditions of bonds, and other factors). Fair value measurements for pooled trust-preferred securities are obtained through the use of valuation models that include unobservable inputs which are considered Level 3.

Certain non-financial assets and non-financial liabilities measured at fair value on a recurring basis include reporting units measured at fair value in the first step of a goodwill impairment test. Certain non-financial assets measured at fair value on a non-recurring basis include non-financial assets and non-financial liabilities measured at fair value in the second step of a goodwill impairment test, as well as intangible assets and other non-financial long-lived assets measured at fair value for impairment assessment.

Recurring Basis

The following are descriptions of valuation methodologies used for assets and liabilities measured at fair value on a recurring basis.

Available for Sale Securities

Fair values for available-for-sale securities are obtained from a third party vendor and are valued using Level 2 inputs, except for TRUP CDOs which are accounted for using Level 3 inputs. TRUP CDOs accounted for less than 1% of the portfolio at March 31, 2012 and December 31, 2011.

The markets for TRUP CDOs and other similar securities were not active at March 31, 2012 or December 31, 2011. The inactivity was evidenced first by a significant widening of the bid-ask spread in the brokered markets in which these securities trade and then by a significant decrease in the volume of trades relative to historical levels. The new issue market has also been relatively inactive.

The market values for TRUP CDOs and other securities except for those issued or guaranteed by the U.S. Treasury have been very depressed relative to historical levels. For example, the yield spreads for the broad market of investment grade and high yield corporate bonds reached all-time levels versus Treasuries at the end of November 2008 and remained close to those levels at March 31, 2012. Therefore, low market prices for a particular bond may only have provided evidence of stress in credit markets in general rather than being an indicator of credit problems with a particular issuer over the past three years.

Given conditions in debt markets for this type of security at March 31, 2012 and December 31, 2011 and the relative inactivity in the secondary and new issue markets, the Company determined:

- Few observable transactions existed and market quotations that were available were not reliable for purposes of determining fair value as of March 31, 2012 or December 31, 2011;

- An income valuation approach technique (present value technique) that maximized the use of relevant observable inputs and minimized the use of unobservable inputs were equally or more representative of fair value than the market approach valuation technique used at prior measurement dates; and

- The Company s TRUP CDOs should be classified within Level 3 of the fair value hierarchy because significant adjustments were required to determine fair value at the measurement date.

The Company s TRUP CDO valuations were prepared by an independent third party. The third party s approach to determining fair value involved these steps as of March 31, 2012 and December 31, 2011:

- ♦ The credit quality of the collateral was calibrated by assigning default probabilities to each issuer;
- ♦ Asset defaults were generated taking into account both the probability of default of the asset and an assumed level of correlation among the assets;
- ♦ A 50% level of correlation was assumed among assets from the same industry (e.g., banks with other banks) while a lower (30%) correlation level is assumed among those from different industries;
- ♦ The loss given default was assumed to be 100% (i.e., no recovery);
- ♦ The cash flows were forecast for the underlying collateral and applied to each TRUP CDO tranche to determine the resulting distribution among the securities;
- ♦ The calculations were modeled in 10,000 scenarios using a Monte Carlo engine;

- The expected cash flows for each scenario were discounted using a discount rate that the third party calculates for each bond that represents an estimate of the yield that would be required in today s market for a bond with a similar credit profile as the bond in question; and
- The prices were aggregated and the average price was used for valuation purposes.

The Company recalculated the overall effective discount rates for these valuations. The overall discount rates ranged from .5% to 16% and were highly dependent upon the credit quality of the collateral, the relative position of the tranche in the capital structure of the TRUP CDO and the prepayment assumptions.

A summary of assets and liabilities as of March 31, 2012 and December 31, 2011 measured at estimated fair value on a recurring basis is as follows (in thousands):

	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
March 31, 2012:				
Financial assets:				
Securities available-for-sale	$ -	$372,268	$475	$372,743
December 31, 2011:				
Financial assets:				
Securities available-for-sale	$ -	$364,912	$553	$365,465

The following table presents a reconciliation and income statement classification of gains and losses for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the quarters ended March 31, 2012 and 2011 (in thousands):

	2012	2011
Available-for-sale securities		
Beginning balance	$553	$439
Total unrealized gains (losses) included in:		
Net income	-	-
Other comprehensive income	(55)	(73)
Purchases, sales, issuances and settlements, net	(23)	-
Transfers in and (out) of Level 3	-	-

Ending balance	$475	$366

Non-Recurring Basis

Certain assets are measured at fair value on a non-recurring basis as described below.

Impaired Loans

Impaired loans are evaluated and valued at the time the loan is identified as impaired at the lower of cost or fair value. Fair value is measured based on the value of the collateral securing these loans. Collateral may be real estate and/or business assets including equipment, inventory and/or accounts receivable. Independent appraisals for collateral are obtained and may be discounted by management based on historical experience, changes in market conditions from time of valuation and/or management s knowledge of the borrower and the borrower s business. As such discounts may be significant, these inputs are considered Level 3 in the hierarchy for determining fair value. Values of impaired loans are reviewed on at least a quarterly basis to determine if specific allocations in the allowance for loan losses are adequate.

Loans Held for Sale

Loans held for sale are recorded at the lower of cost or fair value. Fair value of loans held for sale are based upon binding contracts and quotes from third party investors that qualify as Level 2 inputs for determining fair value. Loans held for sale did not have an impairment charge for first quarters ended March 31, 2012 or 2011.

Other Real Estate

Other real estate is recorded at the lower of cost or fair value. Fair value is measured based on independent appraisals and may be discounted by management based on historical experience and knowledge and changes in market conditions from time of valuation. As such discounts may be significant, these inputs are considered Level 3 in the hierarchy for determining fair value. Values of other real estate are reviewed at least annually or more often if circumstances require more frequent evaluations.

A summary of assets as of March 31, 2012 and December 31, 2011 measured at estimated fair value on a non-recurring basis were as follows:

	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
March 31, 2012:				
Assets:				
Impaired loans	$ -	$ -	$ 9,101	$ 9,101
Loans held for sale	-	3,076	-	3,076
Other real estate owned	-	-	10,831	10,831
December 31, 2011:				
Assets:				
Impaired loans	$ -	$ -	$ 6,797	$ 6,797
Loans held for sale	-	2,616	-	2,616
Other real estate owned	-	-	11,073	11,073

Fair Value Estimates

ASC 820 requires disclosure of the estimated fair value of financial instruments for interim and annual periods. The following assumptions were made and methods applied to estimate the fair value of each class of financial instruments not measured at fair value on the Consolidated Balance Sheets:

Cash and Cash Equivalents

For instruments that qualify as cash equivalents, as described in Note 1, the carrying amount is assumed to be fair value.

Loans

Fair value of variable-rate loans with no significant change in credit risk subsequent to loan origination is based on carrying amounts. For other loans, such as fixed rate loans, fair values are estimated utilizing discounted cash flow analyses, applying interest rates currently offered for new loans with similar terms to borrowers of similar credit quality. Fair values of loans that have experienced significant changes in credit risk have been adjusted to reflect such changes.

Accrued Interest Receivable

The fair values of accrued interest receivable and other assets are assumed to be the carrying value.

Federal Home Loan Bank and Federal Reserve Bank Stock

Carrying amounts of capital stock of the FHLB of Cincinnati and Federal Reserve Bank of St. Louis approximate fair value.

Bank-Owned Life Insurance

Carrying amount of bank-owned life insurance is the cash surrender value as of the end of the periods presented and approximates fair value.

Deposit Liabilities

Demand Deposits

The fair values of deposits which are payable on demand, such as interest-bearing and non-interest-bearing checking accounts, passbook savings, and certain money market accounts are equal to the carrying amount of the deposits.

Variable-Rate Deposits

The fair value of variable-rate money market accounts and certificates of deposit approximate their carrying value at the balance sheet date.

Fixed-Rate Deposits

For fixed-rate certificates of deposit, fair values are estimated utilizing discounted cash flow analyses, which apply interest rates currently being offered on certificates of deposits to a schedule of aggregated monthly maturities on time deposits.

Short Term and Other Borrowings

For securities sold under repurchase agreements payable upon demand, the carrying amount is a reasonable estimate of fair value. For securities sold under repurchase agreements for a fixed term, fair values are estimated using the same methodology as fixed rate time deposits discussed above. The fair value of the advances from the FHLB and other long-term borrowings are estimated by discounting the future cash outflows using the current market rates.

Other Liabilities

Fair value of other liabilities is assumed to be the carrying values.

The carrying amount and fair value of assets and liabilities as of March 31, 2012 and December 31, 2011 were as follows (in thousands):

	March 31, 2012		December 31, 2011	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets				
Cash and cash equivalents	$ 46,239	$ 46,239	$ 34,133	$ 34,133
Interest bearing deposits in other banks	35,409	35,409	40,138	40,138
Investment securities	372,743	372,743	365,465	365,465
Loans	533,405		527,699	
Less: allowance for loan losses	(8,435)		(8,039)	
Loans, net of allowance	524,970	523,588	519,660	519,269
Loans held for sale	3,076	3,076	2,616	2,616
Accrued interest receivable	4,992	4,992	5,306	5,306
Federal Reserve Bank and Federal Home Loan Bank Stock	5,684	5,684	5,684	5,684
Other real estate owned	10,832	10,832	11,073	11,073
Bank owned life insurance	21,570	21,570	21,438	21,438
Financial liabilities				
Deposits	875,891	877,279	855,672	857,299
Short-term borrowings	33,783	33,858	36,471	36,550
Other borrowings	47,222	48,969	47,328	49,230
Other liabilities	10,148	10,148	10,610	10,610
Off-balance sheet arrangements				
Commitments to extend credit	$ 64,675	$ 64,675	$ 77,861	$ 77,861
Standby letters of credit	2,184	2,184	2,410	2,410

Note 12 Comprehensive Income

The components of comprehensive income for the quarters ended March 31, 2012 and 2011 are as follows: