

Independent Alliance Banks, Inc.

Accountants' Report and Consolidated Financial Statements

December 31, 2010 and 2009



Independent Alliance Banks, Inc.

December 31, 2010 and 2009

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Independent Accountants' Report

Board of Directors and Stockholders
Independent Alliance Banks, Inc.
Fort Wayne, Indiana

We have audited the accompanying consolidated balance sheets of Independent Alliance Banks Inc. (Company) as of December 31, 2010 and 2009, and the related consolidated statements of income, stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Independent Alliance Banks, Inc. as of December 31, 2010 and 2009, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

BKD, LLP

March 5, 2011

Independent Alliance Banks, Inc.

Consolidated Balance Sheets

December 31, 2010 and 2009

	2010	2009
Assets		
Cash and due from banks	\$ 7,481,916	\$ 4,080,499
Federal funds sold	3,694,982	6,929,832
Interest-bearing demand deposits in banks	52,654,826	34,215,832
Cash and cash equivalents	63,831,724	45,226,163
Available-for-sale investment securities	164,452,294	147,136,312
Loans held for sale	5,042,422	2,276,414
Loans, net of allowance for loan losses of \$9,646,883 and \$8,507,170 at December 31, 2010 and 2009, respectively	631,186,695	631,010,127
Premises and equipment	11,920,622	11,518,311
Federal Home Loan Bank stock	7,283,000	7,740,000
Interest receivable	4,651,944	4,704,571
Insurance contracts	19,049,749	18,153,240
Goodwill	13,855,664	13,855,664
Core deposits intangible	1,505,936	1,957,712
Other assets	8,983,438	7,683,658
Total assets	\$ 931,763,488	\$ 891,262,172
Liabilities and Stockholders' Equity		
Liabilities		
Deposits		
Noninterest bearing	\$ 114,422,751	\$ 101,039,617
Interest bearing	576,995,801	554,644,520
Total deposits	691,418,552	655,684,137
Short-term borrowings	26,087,594	20,108,206
Long-term debt	100,500,000	110,500,000
Junior subordinated debt	10,310,000	10,310,000
Interest payable	2,707,221	2,755,780
Other liabilities	8,415,811	5,186,600
Total liabilities	839,439,178	804,544,723
Stockholders' Equity		
Common stock and surplus, authorized, 2,000,000 shares; issued, 1,464,079 shares	35,619,709	35,619,709
Retained earnings	61,410,702	55,016,910
Accumulated other comprehensive income	1,438,082	2,187,312
Treasury stock, at cost, 80,024 and 79,287 shares	(6,144,183)	(6,106,482)
Total stockholders' equity	92,324,310	86,717,449
Total liabilities and stockholders' equity	\$ 931,763,488	\$ 891,262,172

Independent Alliance Banks, Inc.
Consolidated Statements of Income
Years Ended December 31, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Interest Income		
Loans receivable	\$ 37,704,236	\$ 38,618,941
Investment securities		
Taxable	3,638,014	4,488,825
Tax exempt	2,073,369	1,662,321
Federal funds sold	10,658	26,242
Deposits with financial institutions	89,442	29,800
Dividends and other	<u>153,602</u>	<u>176,805</u>
Total interest income	<u>43,669,321</u>	<u>45,002,934</u>
Interest Expense		
Deposits	9,970,372	11,548,465
Short-term borrowings	95,387	148,513
Long-term debt	3,697,685	4,724,481
Junior subordinated debt	<u>304,100</u>	<u>376,300</u>
Total interest expense	<u>14,067,544</u>	<u>16,797,759</u>
Net Interest Income	29,601,777	28,205,175
Provision for Loan Losses	<u>3,083,280</u>	<u>2,963,000</u>
Net Interest Income After Provision for Loan Losses	<u>26,518,497</u>	<u>25,242,175</u>
Noninterest Income		
Service charges on deposit accounts	2,253,208	2,550,984
Service charges on loans	401,951	388,770
Net realized gains on sales of available-for-sale securities	94,641	290,341
Income from sale of loans	2,615,831	1,947,911
Fiduciary and other nontraditional activities	1,065,366	542,501
Income from life insurance contracts	855,059	818,440
Other	<u>1,539,411</u>	<u>1,319,870</u>
Total noninterest income	<u>8,825,467</u>	<u>7,858,817</u>
Noninterest Expenses		
Salaries and employee benefits	12,305,400	11,514,011
Net occupancy expense	1,110,766	1,168,982
Equipment expense	1,739,593	1,794,583
Printing and office supplies	726,923	739,973
Legal and professional fees	2,226,055	1,885,510
Advertising expense	589,423	559,634
Deposit insurance expense	971,837	1,434,268
Other	<u>2,759,078</u>	<u>2,351,117</u>
Total noninterest expenses	<u>22,429,075</u>	<u>21,448,078</u>
Income Before Income Taxes	12,914,889	11,652,914
Provision for Income Taxes	<u>3,474,633</u>	<u>3,226,244</u>
Net Income	<u>\$ 9,440,256</u>	<u>\$ 8,426,670</u>

Independent Alliance Banks, Inc.
Consolidated Statements of Stockholders' Equity
Years Ended December 31, 2010 and 2009

	Common Stock and Surplus Shares	Surplus Amount	Comprehensive Income	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Total
Balance, January 1, 2009	1,392,270	\$ 35,619,709		\$ 49,644,909	\$ 1,575,972	\$ (5,762,880)	\$ 81,077,710
Comprehensive income							
Net income			\$ 8,426,670	8,426,670			8,426,670
Change in unrealized gain on available-for-sale securities, net of reclassification adjustment and tax effect			<u>611,340</u>		611,340		611,340
Total comprehensive income			<u>\$ 9,038,010</u>				
Cash dividends (\$2.20 per share)				(3,054,669)			(3,054,669)
Purchase of treasury stock	<u>(7,478)</u>					<u>(343,602)</u>	<u>(343,602)</u>
Balance, December 31, 2009	1,384,792	35,619,709		55,016,910	2,187,312	(6,106,482)	86,717,449
Comprehensive income							
Net income			\$ 9,440,256	9,440,256			9,440,256
Change in unrealized loss on available- for-sale securities, net of reclassification adjustment and tax effect			<u>(749,230)</u>		(749,230)		(749,230)
Total comprehensive income			<u>\$ 8,691,026</u>				
Cash dividends (\$2.20 per share)				(3,046,464)			(3,046,464)
Purchase of treasury stock	<u>(737)</u>					<u>(37,701)</u>	<u>(37,701)</u>
Balance, December 31, 2010	<u>1,384,055</u>	<u>\$ 35,619,709</u>		<u>\$ 61,410,702</u>	<u>\$ 1,438,082</u>	<u>\$ (6,144,183)</u>	<u>\$ 92,324,310</u>

Independent Alliance Banks, Inc.
Consolidated Statements of Cash Flows
Years Ended December 31, 2010 and 2009

	2010	2009
Operating Activities		
Net income	\$ 9,440,256	\$ 8,426,670
Items not requiring (providing) cash		
Depreciation and amortization	959,810	986,050
Net accretion of loan origination fees and costs	(10,553)	(44,259)
Provision for loan losses	3,083,280	2,963,000
Deferred income taxes	(250,826)	(855,031)
Net amortization of premiums and discounts on loans, securities, deposits and debt	862,993	670,919
Net gain on sales and disposal of fixed assets	(9,800)	(1,091)
Net realized gains on sale of SBA loans	(10,481)	(90,196)
Net realized gains on available-for-sale securities	(94,641)	(290,341)
Increase in life insurance contracts	(855,059)	(818,440)
Changes in		
Loans held for sale	(2,766,008)	(5,014)
Interest receivable	52,627	192,568
Interest payable	(48,559)	(443,557)
Other assets	(648,959)	(3,318,833)
Other liabilities	3,229,211	549,718
Net cash provided by operating activities	12,933,291	7,922,163
Investing Activities		
Purchases of available-for-sale securities	(72,754,065)	(55,355,470)
Proceeds from maturities of available-for-sale securities	51,122,630	37,365,051
Proceeds from the sales of available-for-sale securities	2,849,652	14,888,540
Net change in loans	(3,238,814)	7,437,079
Proceeds from sale of fixed assets	9,800	2,200
Purchase of premises and equipment	(1,362,121)	(579,016)
Proceeds from redemption of FHLB stock	457,000	—
Purchase of life insurance contracts and contract premiums	(41,450)	(113,672)
Proceeds from life insurance contract	—	75,958
Net cash provided by (used in) investing activities	(22,957,368)	3,720,670
Financing Activities		
Net increase in deposits	35,734,415	18,291,079
Net increase (decrease) in short-term borrowings	5,979,388	(12,859,492)
Proceeds from long-term borrowings	39,000,000	20,000,000
Repayment of long-term borrowings	(49,000,000)	(43,000,000)
Purchase of treasury stock	(37,701)	(343,602)
Cash dividends	(3,046,464)	(3,054,669)
Net cash provided by (used in) financing activities	28,629,638	(20,966,684)
Increase (Decrease) in Cash and Cash Equivalents	18,605,561	(9,323,851)
Cash and Cash Equivalents, Beginning of Year	45,226,163	54,550,014
Cash and Cash Equivalents, End of Year	\$ 63,831,724	\$ 45,226,163
Supplemental Cash Flows Information		
Interest paid	\$ 14,116,103	\$ 17,241,316
Income taxes paid	4,448,000	3,685,000

Independent Alliance Banks, Inc.
Notes to Consolidated Financial Statements
December 31, 2010 and 2009
(Table Dollar Amounts in Thousands)

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

Nature of Operations

Independent Alliance Banks, Inc. (Company) is a bank holding company whose principal activity is the ownership and management of its two wholly owned bank subsidiaries, Grabill Bank (Grabill) and MarkleBank (Markle) (collectively Banks) and one special purpose subsidiary, Grabill Capital Trust I. The Company was formed on May 1, 2005, as a result of the merger of Grabill Bancorp and MarBanc Financial Corporation. The Company is headquartered in Fort Wayne, Indiana, while Grabill and Markle are headquartered in the respective towns of Grabill, Indiana and Markle, Indiana.

Grabill and Markle operate as separately chartered subsidiaries, each governed by its own Board of Directors. Grabill and Markle are primarily engaged in providing a full range of banking and financial services to individual and corporate customers primarily in Allen, Huntington, Wells and Grant Counties in Indiana and in surrounding counties. Grabill and Markle are subject to competition from other financial institutions and regulation by the Department of Financial Institutions, state of Indiana and the Federal Deposit Insurance Corporation (FDIC).

Grabill Capital Trust I (Trust) was formed during 2004 for the purpose of participating in a Pooled Trust Preferred Stock offering. The Trust is not consolidated into the Company. See Note 10 for further discussion regarding this entity.

Grabill has two wholly owned subsidiaries, Grabill Investments, Inc. which is primarily engaged in managing Grabill's investment securities and Grabill Bank Insurance Services, LLC which became inactive during 2006, and previously provided general insurance products to business and retail customers. Grabill Investments, Inc. has one subsidiary, Grabill Reit. Markle has one wholly owned subsidiary, Markle Holdings, Inc. which is primarily engaged in managing Markle's investment securities. Markle Holdings, Inc. has one subsidiary, MarkleReit. Markle Investments, Inc. and Markle Portfolio, LLC were merged into Markle Holdings, Inc. on December 31, 2009. During late 2009, the Company formed IAB Risk Management, Inc. which is primarily engaged in the underwriting of excess bank risk. As of December 31, 2010, this subsidiary was inactive.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

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

Independent Alliance Banks, Inc.
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Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, valuation of real estate acquired in connection with foreclosures or in satisfaction of loans, valuation of deferred tax assets, valuation of goodwill and fair values of financial instruments.

Cash Equivalents

The Company considers all liquid investments with original maturities of three months or less to be cash equivalents. Cash and cash equivalents are defined to include the Company's cash on hand, its demand deposits with other institutions, money market mutual funds and federal funds sold with maturities of 90 days or less.

Effective July 21, 2010, the FDIC's insurance limits were permanently increased to \$250,000. At December 31, 2010, the Company's cash accounts at nonfederal government or agencies thereof did not exceed federally insured limits.

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

Federal funds sold are not subject to FDIC insurance.

Securities

Available-for-sale securities, which include any security for which the Company has no immediate plan to sell but which may be sold in the future, are carried at fair value. Unrealized gains and losses are recorded, net of related income tax effects, in other comprehensive income. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific-identification method.

For debt securities with fair value below amortized cost value when the Company does not intend to sell a debt security, and it is more likely than not the Company will not have to sell the security before recovery of its cost basis, it recognizes the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income.

Loans Held for Sale

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to noninterest income. Gains and losses on loan sales 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.

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Loans

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

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

The accrual of interest on mortgage and commercial loans is generally discontinued at the time the loan is 90 days past due unless the credit is well-secured and in process of collection. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off are reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Loan Losses

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

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of allocated and general components. The allocated component relates to loans that are classified as impaired. For those loans that are classified as impaired, an allowance is established if 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 nonclassified loans and is based on historical charge-off experience and expected loss given default derived from the Company's internal risk rating process. 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.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment

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delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price or the fair value of the collateral if the loan is collateral dependent.

Groups of loans with similar risk characteristics are collectively evaluated for impairment based on the group's historical loss experience adjusted for changes in trends, conditions and other relevant factors that affect repayment of the loans. Accordingly, the Company does not separately identify individual consumer and residential loans for impairment measurements.

Premises and Equipment

Depreciable assets are stated at cost less accumulated depreciation. Depreciation is charged to expense using the straight-line method over the estimated useful lives of the assets. Maintenance and repairs are expensed as incurred while major additions and improvements are capitalized. Gains and losses on disposition are included in current operations.

Federal Home Loan Bank Stock

Federal Home Loan Bank stock is a required investment for institutions that are members of the Federal Home Loan Bank (FHLB). The required investment in the common stock is based on a predetermined formula, carried at cost and evaluated for impairment.

Goodwill

Goodwill is tested annually for impairment. If the implied fair value of goodwill is lower than its carrying amount, a goodwill impairment is indicated and goodwill is written down to its implied fair value. Subsequent increases in goodwill value are not recognized in the consolidated financial statements.

On May 1, 2005, at the time of the acquisition of MarBanc Financial Corporation, goodwill of \$13,855,664 was recorded. There was no impairment of goodwill during 2010 or 2009.

Intangible Assets

Intangible assets consist of core deposit intangibles which are being amortized on the straight-line basis over nine years. The intangible asset is periodically evaluated as to the recoverability of its carrying value.

Treasury Stock

Common stock shares repurchased are recorded at cost. Cost of shares retired or reissued is determined using the first-in, first-out method.

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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.

Income Taxes

The Company accounts for income taxes in accordance with income tax accounting guidance (ASC 740, *Income Taxes*). The income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Company determines deferred income taxes using the liability 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 reduced by a valuation allowance if, based on the weight of evidence available, it is more likely than not that some portion or all of a deferred tax asset will not be realized.

Uncertain tax positions are recognized if it is more likely than not, based on the technical merits, that the tax position will be realized or sustained upon examination. The term more likely than not means a likelihood of more than 50%; 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% likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances and information available at the reporting date and is subject to management's judgment.

The Company recognizes interest and penalties on income taxes, if any, as a component of income tax expense.

The Company files consolidated income tax returns with its subsidiaries.

Comprehensive Income

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

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Stock Options

At December 31, 2010 and 2009, the Company has a share-based employee compensation plan, which is described more fully in Note 15.

Subsequent Events

Subsequent events have been evaluated through March 5, 2011, which is the date the consolidated financial statements were available to be issued.

Note 2: Restriction on Cash and Due From Banks

The Banks are required to maintain reserve funds in cash and/or on deposit with the Federal Reserve Bank. The reserve required at December 31, 2010, was \$300,000 for Grabill and \$25,000 for Markle.

Note 3: Securities

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

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-Sale Securities				
December 31, 2010				
U.S. Government agencies	\$ 36,725	\$ 363	\$ 92	\$ 36,996
Mortgage-backed GSE residential	54,253	2,184	95	56,342
State and political subdivision	<u>71,286</u>	<u>930</u>	<u>1,102</u>	<u>71,114</u>
	<u>\$ 162,264</u>	<u>\$ 3,477</u>	<u>\$ 1,289</u>	<u>\$ 164,452</u>

Independent Alliance Banks, Inc.
Notes to Consolidated Financial Statements
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	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-Sale Securities				
December 31, 2009				
U.S. Government agencies	\$ 28,245	\$ 168	\$ 135	\$ 28,278
Mortgage-backed GSE residential	71,399	2,505	37	73,867
State and political subdivision	<u>44,155</u>	<u>1,020</u>	<u>184</u>	<u>44,991</u>
	<u>\$ 143,799</u>	<u>\$ 3,693</u>	<u>\$ 356</u>	<u>\$ 147,136</u>

The amortized cost and fair value of securities available for sale at December 31, 2010, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Within one year	\$ 175	\$ 175
One to five years	35,731	36,100
Five to ten years	53,441	53,451
After ten years	<u>18,664</u>	<u>18,384</u>
	108,011	108,110
Mortgage-backed GSE residential	<u>54,253</u>	<u>56,342</u>
Totals	<u>\$ 162,264</u>	<u>\$ 164,452</u>

The carrying value of securities pledged as collateral was \$65,090,000 at December 31, 2010 and \$63,954,000 at December 31, 2009.

Gross gains of \$112,898 and \$313,337 and gross losses of \$18,257 and \$22,996 resulting from sales of available-for-sale securities were realized in 2010 and 2009, respectively.

There were no other than temporary impairment losses recognized in 2010 or 2009.

Certain investments in debt securities are reported in the consolidated financial statements at an amount less than their historical cost. Total fair value of these investments at December 31, 2010 and 2009, was \$48,180,000 and \$25,772,000, respectively, which is approximately 29% and 18% of the Company's available-for-sale investment portfolio. These declines primarily resulted from changes in market interest rates since the securities were purchased.

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Based on evaluation of available evidence, management believes the declines in fair value for these securities are temporary.

The following table shows the Company's investments' 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 class and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2010 and 2009:

	December 31, 2010					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-Sale Securities						
U.S. Government agencies	\$ 6,686	\$ 71	\$ 1,099	\$ 21	\$ 7,785	\$ 92
Mortgage-backed GSE residential	5,582	95	—	—	5,582	95
State and political subdivision	<u>34,294</u>	<u>1,065</u>	<u>519</u>	<u>37</u>	<u>34,813</u>	<u>1,102</u>
Total temporarily impaired securities	<u>\$ 46,562</u>	<u>\$ 1,231</u>	<u>\$ 1,618</u>	<u>\$ 58</u>	<u>\$ 48,180</u>	<u>\$ 1,289</u>

	December 31, 2009					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-Sale Securities						
U.S. Government agencies	\$ 11,746	\$ 135	\$ —	\$ —	\$ 11,746	\$ 135
Mortgage-backed GSE residential	4,687	37	—	—	4,687	37
State and political subdivision	<u>8,830</u>	<u>136</u>	<u>509</u>	<u>48</u>	<u>9,339</u>	<u>184</u>
Total temporarily impaired securities	<u>\$ 25,263</u>	<u>\$ 308</u>	<u>\$ 509</u>	<u>\$ 48</u>	<u>\$ 25,772</u>	<u>\$ 356</u>

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Note 4: Loans and Allowance for Loan Losses

Categories of loans at December 31 include:

	2010	2009
Commercial and industrial loans	\$ 103,483	\$ 97,749
Real estate loans (includes \$63,231 and \$59,573 secured by farmland)	442,380	459,765
Construction loans	42,270	36,758
Agricultural production financing and other loans to farmers	28,871	25,470
Individuals' loans for household and other personal expenditures	9,238	11,827
Tax-exempt loans	10,531	4,359
Other	<u>3,989</u>	<u>3,506</u>
 Total loans	 640,762	 639,434
Net deferred loan costs	72	83
Allowance for loan losses	<u>(9,647)</u>	<u>(8,507)</u>
 Net loans	 <u>\$ 631,187</u>	 <u>\$ 631,010</u>

Activity in the allowance for loan losses was as follows:

	2010	2009
Balance, beginning of year	\$ 8,507	\$ 7,658
Provision for losses	3,083	2,963
Recoveries on loans	240	148
Loans charged off	<u>(2,183)</u>	<u>(2,262)</u>
 Balance, end of year	 <u>\$ 9,647</u>	 <u>\$ 8,507</u>

A loan is considered impaired, in accordance with the impairment accounting guidance (ASC 310-10-35-16), when based on current information and events, it is probable the Company will be unable to collect all amounts due from the borrower in accordance with the contractual terms of the loan. Impaired loans include nonperforming commercial loans but also include loans modified in troubled debt restructurings where concessions have been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in the interest rate on the loan, payment extensions, forgiveness of principal, forbearance or other actions intended to maximize collection.

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The following table presents the Company's impaired and nonaccrual loans at December 31, 2010 and 2009.

	<u>2010</u>	<u>2009</u>
Impaired loans without a valuation allowance	\$ 10,291	\$ 2,615
Impaired loans with a valuation allowance	<u>10,351</u>	<u>7,440</u>
Total impaired loans	<u>\$ 20,642</u>	<u>\$ 10,055</u>
Valuation allowance related to impaired loans	<u>\$ 2,457</u>	<u>\$ 1,144</u>
Average investment in impaired loans	<u>\$ 18,364</u>	<u>\$ 11,691</u>
Interest income recognized on impaired loans	<u>\$ 684</u>	<u>\$ 628</u>
Interest income recognized on a cash basis on impaired loans	<u>\$ 712</u>	<u>\$ 613</u>
Total nonaccrual loans	<u>\$ 6,725</u>	<u>\$ 7,874</u>
Total loans past due 90 days or more and still accruing	<u>\$ 1,162</u>	<u>\$ 879</u>

Note 5: Premises and Equipment

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

	<u>2010</u>	<u>2009</u>
Land	\$ 2,513	\$ 2,513
Buildings	10,181	10,131
Equipment	<u>10,036</u>	<u>8,935</u>
	22,730	21,579
Less accumulated depreciation	<u>(10,809)</u>	<u>(10,061)</u>
Net premises and equipment	<u>\$ 11,921</u>	<u>\$ 11,518</u>

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Note 6: Core Deposit Intangible

The carrying basis and accumulated amortization of recognized intangible assets at December 31, 2010 and 2009, were:

	2010		2009	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Core deposits	\$ <u>4,066</u>	\$ <u>2,560</u>	\$ <u>4,066</u>	\$ <u>2,108</u>

Amortization expense for both of the years ended December 31, 2010 and 2009, was approximately \$452,000.

Estimated amortization expense for each of the following four years is:

2011	\$ 452
2012	452
2013	452
2014	150

Note 7: Deposits

	2010	2009
Demand deposits	\$ 114,423	\$ 101,040
Savings deposits	52,519	47,409
Interest-bearing demand deposits	147,597	116,797
Certificates of \$100,000 or more	211,652	214,909
Other certificates and time deposits	<u>165,228</u>	<u>175,529</u>
	<u>\$ 691,419</u>	<u>\$ 655,684</u>

Certificates maturing in years ending December 31:

2011	\$ 194,888
2012	116,263
2013	27,950
2014	23,677
2015	14,099
Thereafter	<u>3</u>
	<u>\$ 376,880</u>

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Note 8: Short-Term Borrowings

Short-term borrowings included the following:

	2010	2009
Securities sold under repurchase agreements	\$ <u>26,088</u>	\$ <u>20,108</u>

Securities sold under agreements to repurchase consist of obligations of the Banks to other parties. The obligations are secured by investment securities and such collateral is held by a safekeeping agent. The maximum amount of outstanding agreements at any month end during 2010 and 2009 totaled \$28,784,000 and \$34,652,000, and the daily average of such agreements totaled \$22,284,000 and \$27,180,000, respectively. The agreements at December 31, 2010, mature within 12 months.

The Company had available unused Federal Funds commitments of \$46,000,000 at December 31, 2010 with three institutions.

Note 9: Long-Term Debt

	2010	2009
Federal Home Loan Bank Advances, fixed rates ranging from 1.88% to 4.70%, due at various dates through June 6, 2017	\$ <u>100,500</u>	\$ <u>110,500</u>

The Federal Home Loan Bank advances, including both short term and long term, are secured by mortgage loans and investment securities totaling approximately \$286,748,000 and \$318,680,000 at December 31, 2010 and 2009, respectively. Advances are subject to restrictions or penalties in the event of prepayment.

Aggregate annual maturities of long-term debt at December 31, 2010, are:

2011	\$ 13,500
2012	18,000
2013	15,000
2014	17,000
2015	17,000
Thereafter	20,000
	\$ 100,500

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Note 10: Guaranteed Preferred Beneficial Interests in Independent Alliance Banks, Inc. Subordinated Debentures

In June 2004, Grabill Bancorp formed Grabill Capital Trust I (Trust), a statutory business trust. As a result of the completed merger, the rights and obligations to the Trust were assumed by the Company. The Trust issued \$10,310,000 of Trust Preferred Capital Securities (TPS) as a participant in a pooled trust preferred securities offering. Grabill Bancorp issued junior subordinated debentures aggregating \$10,310,000 to the Trust. The junior subordinated debentures are the sole assets of the Trust. The junior subordinated debentures and the trust preferred securities pay interest and dividends, respectively, on a quarterly basis. The junior subordinated debentures and the securities bear interest at a rate of LIBOR plus 2.60% and mature on July 23, 2034, and are noncallable for five years. After that period, the securities may be called at any quarterly interest payment date at par. The Trust Preferred Capital Securities, subject to certain limitations, are included in Tier 1 Capital for regulatory purposes.

The Trust is not consolidated into the Company and as a result, the Company accounts for the investment in the Trust as an asset, the subordinated debentures as debt, and the interest paid thereon as interest expense.

Note 11: Income Taxes

The Company files income tax returns in the U.S. federal jurisdiction and various state jurisdictions. With a few exceptions, the Company is no longer subject to U.S. federal, state and local income tax examinations by tax authorities for years before 2007.

The provision for income taxes includes these components:

	2010	2009
Taxes currently payable	\$ 3,726	\$ 4,081
Deferred income taxes	<u>(251)</u>	<u>(855)</u>
Income tax expense	<u>\$ 3,475</u>	<u>\$ 3,226</u>

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

	2010	2009
Computed at the statutory rate (34%)	\$ 4,391	\$ 3,962
Increase (decrease) resulting from		
Tax-exempt interest	(855)	(629)
Effect of state income taxes	180	111
Other nontaxable income, net	(291)	(245)
Other	<u>50</u>	<u>27</u>
Actual tax expense	<u>\$ 3,475</u>	<u>\$ 3,226</u>

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The tax effects of temporary differences related to deferred taxes shown on the consolidated balance sheets were:

	2010	2009
Deferred tax assets		
Differences in accounting for loan losses	\$ 4,068	\$ 2,892
State income tax	—	279
Deferred compensation	1,259	753
Differences in the basis of assets	—	176
Differences in accounting for employee benefits	110	37
Nonaccrual interest	230	51
Differences in depreciation methods	—	97
State net operating loss carryforwards	—	445
Other real estate owned	38	—
Capital loss carryover	117	—
	<u>5,822</u>	<u>4,730</u>
Deferred tax liabilities		
Differences in expense recognition	(121)	(32)
State income tax	(172)	—
Accretion of investment discounts	(38)	(45)
Differences in depreciation methods	(650)	—
Federal Home Loan Bank stock dividends	(152)	(130)
Differences in basis of intangible assets	(635)	(666)
Differences in income recognition	(254)	(308)
Unrealized gain on securities available for sale	(750)	(836)
	<u>(2,772)</u>	<u>(2,017)</u>
Net deferred tax asset	<u>\$ 3,050</u>	<u>\$ 2,713</u>

At December 31, 2010, the Company had approximately \$277,000 of capital loss carryovers that are being carried forward to off-set future capital gains. The carryovers expire in 2015.

Note 12: Other Comprehensive Income (Loss)

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

	2010	2009
Unrealized gains (losses) on securities available for sale	\$ (1,050)	\$ 1,224
Less reclassification for realized gains included in income	95	290
Other comprehensive income (loss), before tax effect	(1,145)	934
Tax expense (benefit)	(396)	323
Other comprehensive income (loss)	<u>\$ (749)</u>	<u>\$ 611</u>

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Note 13: Regulatory Matters

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

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

As of December 31, 2010, the most recent notification from Federal Reserve Bank and FDIC categorized the subsidiary banks as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well-capitalized, the subsidiary banks must maintain capital ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the Company or subsidiary bank's categories.

The Company and subsidiary bank's actual capital amounts and ratios are also presented in the following table.

	Actual		Minimum Capital Requirement		Minimum to Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2010						
Total capital (to risk-weighted assets)						
Consolidated	\$ 94,699	13.9%	\$ 54,509	8.0%	\$ —	N/A
Grabill	63,124	14.2	35,677	8.0	44,596	10.0%
Markle	28,816	12.4	18,649	8.0	23,311	10.0
Tier I capital (to risk-weighted assets)						
Consolidated	\$ 86,168	12.6%	\$ 27,254	4.0%	\$ —	N/A
Grabill	57,530	12.9	17,838	4.0	26,758	6.0%
Markle	26,328	11.3	9,325	4.0	13,987	6.0

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	Actual		Minimum Capital Requirement		Minimum to Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Tier I capital (to average assets)						
Consolidated	\$ 86,168	9.3%	\$ 36,967	4.0%	\$ —	N/A
Grabill	57,530	9.5	24,143	4.0	30,179	5.0%
Markle	26,328	8.2	12,780	4.0	15,975	5.0
As of December 31, 2009						
Total capital (to risk-weighted assets)						
Consolidated	\$ 87,896	13.1%	\$ 53,615	8.0%	\$ —	N/A
Grabill	58,757	13.1	35,818	8.0	44,772	10.0%
Markle	26,827	12.2	17,654	8.0	22,068	10.0
Tier I capital (to risk-weighted assets)						
Consolidated	\$ 79,517	11.9%	\$ 26,808	4.0%	\$ —	N/A
Grabill	53,156	11.9	17,909	4.0	26,863	6.0%
Markle	24,254	11.0	8,827	4.0	13,241	6.0
Tier I capital (to average assets)						
Consolidated	\$ 79,517	9.1%	\$ 35,004	4.0%	\$ —	N/A
Grabill	53,156	9.1	23,269	4.0	29,087	5.0%
Markle	24,254	8.3	11,661	4.0	14,577	5.0

Grabill is subject to certain restrictions on the amount of dividends that it may declare without prior regulatory approval. At December 31, 2010 and 2009, approximately \$8,429,000 and \$7,310,000, respectively, of retained earnings were available for dividend declaration without prior regulatory approval.

Markle is subject to certain restrictions on the amount of dividends that it may declare without prior regulatory approval. At December 31, 2010 and 2009, approximately \$2,702,000 and \$946,000, respectively, of retained earnings were available for dividend declaration without prior regulatory approval.

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Note 14: Related Party Transactions

At December 31, 2010 and 2009, the Banks had loans outstanding to executive officers, directors, significant stockholders and their affiliates (related parties), of approximately \$6,241,000 and \$4,926,000, respectively.

At December 31, 2010 and 2009, the Banks had deposits from executive officers, directors, significant stockholders and their affiliates (related parties), of approximately \$6,929,000 and \$8,111,000, respectively.

In management's opinion, such loans and other extensions of credit and deposits were made in the ordinary course of business and were made on substantially the same terms (including interest rates and collateral) as those prevailing at the time for comparable transactions with other persons. Further, in management's opinion, these loans did not involve more than normal risk of collectibility or present other unfavorable features.

Note 15: Employee Benefits

Defined Contribution Plan

The Company sponsors a retirement plan titled IAB 401(k) Profit Sharing Plan (Plan) which includes a 401(k) component and an employee stock ownership plan (ESOP) component. The Plan covers substantially all of the Company's employees. Employer contributions charged to expense for 2010 and 2009 was approximately \$609,000 and \$544,000, respectively.

The cost of the ESOP is borne by the Company through contributions to an employee stock ownership trust in amounts determined by the Board of Directors. The Plan provides for the purchase of any stock distributed to a participant at its fair value within 60 days of its distribution. If the participant does not exercise the put option within the 60-day period, the option will temporarily lapse. After the next succeeding appraisal of the Company's stock has been completed, all those who did not exercise the put option during the first option period will have an additional 60-day option period.

The total number of shares held by the ESOP, all of which have been allocated to participant accounts were 47,463 and 42,273 at December 31, 2010 and 2009, respectively. At December 31, 2010 and 2009, the fair value of the allocated shares, as determined by an independent appraiser, was approximately \$3,275,000 and \$2,832,000, respectively. At December 31, 2010 and 2009, there were no shares subject to a put option.

Deferred Compensation

The Company has deferred compensation agreements with certain officers and directors. The Company's expense for the agreements was \$307,280 and \$304,409 for 2010 and 2009, respectively.

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Stock Incentive Plan

The Company has adopted a stock incentive plan that allows for awards of incentive stock options, nonqualified stock options and stock appreciation rights to key employees, subject to vesting requirements and exercise periods determined by the Board of Directors. The maximum number of designated shares for award is 11,400 shares. The stock incentive plan is currently set to expire March 21, 2011.

All stock options expire five years after the date of grant. Since inception of the plan, 5,350 stock options have been granted.

The Company has a policy of issuing authorized shares to satisfy share option exercises.

During the year ended December 31, 2010, there were no stock options granted; there were no shares forfeited and no shares were exercised. At December 31, 2010, there were no stock options outstanding.

During the year ended December 31, 2009, there were no stock options granted; 700 shares were forfeited and no shares were exercised. At December 31, 2009, there were no stock options outstanding.

The Company accounts for this plan under the recognition and measurement principles of Accounting Standards Codification (ASC) Topic 718, *Compensation—Stock Compensation* (Topic 718). All stock options issued under the plan are fully vested and had an exercise price equal to the market value of the underlying common stock at the grant date.

The Company is required to expense the fair value of stock options granted, modified, repurchased or cancelled. Since all of the Company's stock options were fully vested prior to the adoption of Topic 718 and no options have been granted, modified, repurchased or cancelled, no compensation expense has been recorded for 2010 or 2009. Due to the immaterial amounts associated with stock options, disclosure of all items specified in ASC Topic 718 has not been included.

Note 16: Disclosures About Fair Value of Assets and Liabilities

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

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

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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

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a recurring basis and recognized in the accompanying balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy. The Company has no liabilities measured at fair value on a recurring basis.

Cash Equivalents and Available-for-Sale Securities

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include money market mutual funds. If quoted market prices are not available, then fair values are estimated by a third-party pricing service using pricing models, quoted market prices of securities with similar characteristics or discounted cash flows. The inputs used by the pricing service to determine fair value may include one, or a combination of, observable inputs such as benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data market research publications and are classified within Level 2 of the valuation hierarchy. These Level 2 securities include U.S. Government agencies, state and political subdivision, and mortgage-backed GSE residential securities. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. The Company has no securities classified as Level 3.

	2010			
	Fair Value Measurements Using			
Fair Value	Quoted Prices			
	in Active	Significant	Significant	
	Markets for	Other	Unobservable	
	Identical	Observable	Inputs	
	Assets	Inputs	(Level 3)	
	(Level 1)	(Level 2)		
Cash Equivalents				
Money market mutual funds	\$ 4,235	\$ 4,235	\$ —	\$ —
Available-for-Sale Securities				
U.S. Government agencies	36,996	—	36,996	—
Mortgage-backed GSE residential	56,342	—	56,342	—
State and political subdivision	71,114	—	71,114	—

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	2009 Fair Value Measurements Using			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash Equivalents				
Money market mutual funds	\$ 5,172	\$ 5,172	\$ —	\$ —
Available-for-Sale Securities				
U.S. Government agencies	28,278	—	28,278	—
Mortgage-backed GSE residential	73,867	—	73,867	—
State and political subdivision	44,991	—	44,991	—

Following is a description of the valuation methodologies used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy. The Company has no liabilities measured at fair value on a nonrecurring basis.

Impaired Loans (Collateral Dependent)

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

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

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

Impaired loans are classified within Level 3 of the fair value hierarchy.

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The following table presents the fair value measurement of assets measured at fair value on a nonrecurring basis and the level within the fair value hierarchy in which the fair value measurements fall at December 31, 2010 and 2009:

	2010			
	Fair Value Measurements Using			
Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Impaired loans (collateral dependent)	\$ <u>7,894</u>	\$ <u>0</u>	\$ <u>0</u>	\$ <u>7,894</u>

	2009			
	Fair Value Measurements Using			
Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Impaired loans (collateral dependent)	\$ <u>6,296</u>	\$ <u>0</u>	\$ <u>0</u>	\$ <u>6,296</u>

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying consolidated balance sheets at amounts other than fair value.

Cash and Cash Equivalents, Federal Home Loan Bank Stock and Interest Receivable

The carrying amount approximates fair value.

Loans Held for Sale

Fair value of loans held for sale are based on quoted market prices, where available, or are determined by discounting estimated cash flows using interest rates approximating the Company's current origination rates for similar loans and adjusted to reflect the inherent credit risk.

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Loans

The fair value of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. Loans with similar characteristics were aggregated for purposes of the calculations. The carrying amount of accrued interest approximates its fair value.

Deposits

Deposits include demand deposits, savings accounts, NOW accounts and certain money market deposits. The carrying amount approximates fair value. The fair value of fixed-maturity time deposits is estimated using a discounted cash flow calculation that applies the rates currently offered for deposits of similar remaining maturities.

Short-Term Borrowings and Interest Payable

The carrying amount approximates fair value.

Long-Term Debt and Junior Subordinated Debt

Rates currently available to the Company for debt with similar terms and remaining maturities are used to estimate the fair value of existing debt.

The following table presents estimated fair values of the Company's financial instruments at December 31, 2010 and 2009.

	2010		2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets				
Cash and cash equivalents	\$ 63,832	\$ 63,832	\$ 45,226	\$ 45,226
Available-for-sale securities	164,452	164,452	147,136	147,136
Loans held for sale	5,042	5,140	2,276	2,319
Loans, net of allowance for loan losses	631,187	628,669	631,010	632,636
Federal Home Loan Bank stock	7,283	7,283	7,740	7,740
Interest receivable	4,652	4,652	4,705	4,705

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	2010		2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial liabilities				
Deposits	\$ 691,419	\$ 699,264	\$ 655,684	\$ 661,512
Short-term borrowings	26,088	26,088	20,108	20,108
Long-term debt	100,500	104,534	110,500	114,261
Junior subordinated debt	10,310	7,964	10,310	8,376
Interest payable	2,707	2,707	2,756	2,756

Note 17: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Estimates related to the allowance for loan losses are reflected in the footnote regarding loans. Current vulnerabilities due to certain concentrations of credit risk are discussed in the footnote on commitments and credit risk.

Investments

The Company invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the accompanying consolidated balance sheets.

Current Economic Conditions

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

At December 31, 2010, the Company held approximately \$103,483,000 in commercial and industrial loans and approximately \$235,614,000 in loans collateralized by commercial real estate primarily in northeastern Indiana. Due to national, state and local economic conditions, values for commercial real estate have declined, and the market for these properties is depressed.

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

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Given the volatility of current economic conditions, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments in asset values, the allowance for loan losses and capital that could negatively impact the Company's ability to meet regulatory capital requirements and maintain sufficient liquidity.

Goodwill

As discussed in Note 1, the Company annually tests its goodwill for impairment. At the most recent testing date, the fair value of the bank reporting unit exceeded its carrying value by approximately 3%. Estimated fair value of the bank reporting unit was based principally on forecasts of future income. Due to the volatility of the current economic environment, management's forecasts of future income are subject to significantly more uncertainty than during more stable environments. Management believes it has applied reasonable judgment in developing its estimates; however, unforeseen negative changes in the national, state or local economic environment may negatively impact those estimates in the near term.

Note 18: Commitments and Credit Risk

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

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

	<u>2010</u>	<u>2009</u>
Commitments to extend credit	\$ 114,999	\$ 109,896
Standby letters of credit	1,154	2,338

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 Banks evaluate each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Banks upon extension of credit, is based on management's credit evaluation. Collateral held varies, but may include accounts receivable, inventory, property and equipment and income-producing commercial properties.

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

The Company and subsidiaries are also subject to claims and lawsuits which arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the consolidated financial position of the Company.