WEST BANCORPORATION INC
Form 10-Q
April 26, 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 SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2012

or

o 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: 0-49677

WEST BANCORPORATION, INC.
(Exact Name of Registrant as Specified in its Charter)

IOWA	42-1230603
(State of Incorporation)	(I.R.S. Employer Identification No.)

1601 22nd Street, West Des Moines, Iowa 50266

Telephone Number: (515) 222-2300

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

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 (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes x No o

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 definition of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer o Accelerated filer x

Non-accelerated filer o Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

As of April 25, 2012, there were 17,403,882 shares of common stock, no par value, outstanding.

WEST BANCORPORATION, INC.

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PART I - FINANCIAL INFORMATION
Item 1. Financial Statements

West Bancorporation, Inc. and Subsidiary
Consolidated Balance Sheets
(unaudited)

(in thousands)	March 31, 2012	December 31, 2011
ASSETS		
Cash and due from banks	$32,803	$35,772
Federal funds sold	75,703	51,332
Cash and cash equivalents	108,506	87,104
Securities available for sale	306,188	283,145
Federal Home Loan Bank stock, at cost	11,475	11,352
Loans held for sale	901	4,089
Loans	849,041	838,959
Allowance for loan losses	(16,651)	(16,778)
Loans, net	832,390	822,181
Premises and equipment, net	5,871	5,396
Accrued interest receivable	4,735	4,183
Bank-owned life insurance	25,923	25,724
Other real estate owned	9,963	10,967
Deferred tax assets	7,849	8,409
Other assets	7,403	6,974
Total assets	$1,321,204	$1,269,524
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Deposits:		
Noninterest-bearing demand	$272,018	$268,887
Interest-bearing demand	163,553	158,141
Savings	374,530	343,312
Time of $100,000 or more	73,756	98,743
Other time	85,173	88,290
Total deposits	969,030	957,373
Federal funds purchased and securities sold under agreements to repurchase	93,496	55,841
Subordinated notes	20,619	20,619
Federal Home Loan Bank advances	105,000	105,000
Accrued expenses and other liabilities	6,790	7,240
Total liabilities	1,194,935	1,146,073
STOCKHOLDERS' EQUITY		
Preferred stock, $0.01 par value; authorized 50,000,000 shares; no shares issued		
and outstanding at March 31, 2012, and December 31, 2011	—	—
Common stock, no par value; authorized 50,000,000 shares; 17,403,882		
shares issued and outstanding at March 31, 2012, and December 31, 2011	3,000	3,000
Additional paid-in capital	33,687	33,687
Retained earnings	88,696	86,110
Accumulated other comprehensive income	886	654

Total stockholders' equity	126,269	123,451
Total liabilities and stockholders' equity	$1,321,204	$1,269,524

See accompanying Notes to Consolidated Financial Statements.

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West Bancorporation, Inc. and Subsidiary
Consolidated Income Statements
(unaudited)

(in thousands, except per share data)	Three Months Ended March 31, 2012	2011
Interest income:		
Loans, including fees	$11,190	$11,793
Securities:		
Taxable securities	971	1,114
Tax-exempt securities	503	604
Federal funds sold and other short-term investments	42	61
Total interest income	12,706	13,572
Interest expense:		
Demand deposits	294	420
Savings deposits	266	284
Time deposits	719	1,161
Federal funds purchased and securities sold under agreements to repurchase	37	46
Subordinated notes	193	176
Long-term borrowings	1,019	1,008
Total interest expense	2,528	3,095
Net interest income	10,178	10,477
Provision for loan losses	—	500
Net interest income after provision for loan losses	10,178	9,977
Noninterest income:		
Service charges on deposit accounts	730	750
Debit card usage fees	378	347
Trust services	204	219
Gains and fees on sales of residential mortgages	747	184
Increase in cash value of bank-owned life insurance	199	221
Gain from bank-owned life insurance	—	637
Net impairment losses	(46)	—
Realized securities (losses), net	(33)	—
Other income	222	313
Total noninterest income	2,401	2,671
Noninterest expense:		
Salaries and employee benefits	3,636	3,055
Occupancy	857	816
Data processing	501	451
FDIC insurance expense	166	549
Other real estate owned expense	82	187
Professional fees	292	222
Other expenses	1,331	1,196
Total noninterest expense	6,865	6,476
Income before income taxes	5,714	6,172
Income taxes	1,737	1,642
Net income	3,977	4,530
Preferred stock dividends and accretion of discount	—	(571)
Net income available to common stockholders	$3,977	$3,959

Basic and diluted earnings per common share	$0.23	$0.23
Cash dividends per common share	$0.08	$—

See accompanying Notes to Consolidated Financial Statements.

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West Bancorporation, Inc. and Subsidiary
Consolidated Statements of Comprehensive Income
(unaudited)

(in thousands)	Three Months Ended March 31, 2012	2011
Net income	$3,977	$4,530
Other comprehensive income, before tax:		
Unrealized gains (losses) on securities for which a portion of an other than temporary impairment has been recorded in earnings before tax:		
Unrealized holding gains (losses) arising during the period	(56)	88
Less: reclassification adjustment for impairment losses realized in net income	46	—
Net unrealized gains (losses) on securities with other than temporary impairment before tax expense	(10)	88
Unrealized gains on securities without other than temporary impairment before tax:		
Unrealized holding gains arising during the period	352	1,289
Plus: reclassification adjustment for net losses realized in net income	33	—
Net unrealized gains on other securities before tax expense	385	1,289
Other comprehensive income before tax	375	1,377
Tax expense related to other comprehensive income	(143)	(524)
Other comprehensive income, net of tax:	232	853
Comprehensive income	$4,209	$5,383

See accompanying Notes to Consolidated Financial Statements.

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West Bancorporation, Inc. and Subsidiary
Consolidated Statements of Stockholders' Equity
(unaudited)

(in thousands, except per share data)	Preferred Stock	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 2010	$34,508	$3,000	$34,387	$76,188	$ (2,647)	$145,436
Net income	—	—	—	4,530	—	4,530
Other comprehensive income	—	—	—	—	853	853
Preferred stock discount accretion	121	—	—	(121)	—	—
Preferred stock dividends declared	—	—	—	(450)	—	(450)
Balance, March 31, 2011	$34,629	$3,000	$34,387	$80,147	$ (1,794)	$150,369
Balance, December 31, 2011	$—	$3,000	$33,687	$86,110	$ 654	$123,451
Net income	—	—	—	3,977	—	3,977
Other comprehensive income	—	—	—	—	232	232
Cash dividends declared, $0.08 per common share	—	—	—	(1,391)	—	(1,391)
Balance, March 31, 2012	$—	$3,000	$33,687	$88,696	$ 886	$126,269

See accompanying Notes to Consolidated Financial Statements.

West Bancorporation, Inc. and Subsidiary
Consolidated Statements of Cash Flows
(unaudited)

(in thousands)	Three Months Ended March 31, 2012	2011
Cash Flows from Operating Activities:		
Net income	$3,977	$4,530
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	—	500
Net amortization and accretion	1,160	733
(Gain) loss on disposition of premises and equipment	4	(9)
Securities losses, net	33	—
Investment securities impairment losses	46	—
Gain on sale of loans	(635)	(158)
Proceeds from sales of loans held for sale	27,292	12,703
Originations of loans held for sale	(23,469)	(9,090)
Gain on sale of other real estate owned	(86)	(245)
Write-down of other real estate owned	123	352
Gain from bank-owned life insurance	—	(637)
Increase in value of bank-owned life insurance	(199)	(221)
Depreciation	166	143
Deferred income taxes	417	759
Change in assets and liabilities:		
(Increase) decrease in accrued interest receivable	(552)	248
(Increase) decrease in other assets	(433)	1,076
Decrease in accrued expenses and other liabilities	(450)	(276)
Net cash provided by operating activities	7,394	10,408
Cash Flows from Investing Activities:		
Proceeds from sales, calls, and maturities of securities available for sale	22,021	13,265
Purchases of securities available for sale	(45,925)	(17,208)
Purchases of Federal Home Loan Bank stock	(586)	(209)
Proceeds from redemption of Federal Home Loan Bank stock	463	78
Net change in loans	(9,497)	55,287
Net proceeds from sales of other real estate owned	256	3,599
Proceeds from sales of premises and equipment	—	36
Purchases of premises and equipment	(645)	(97)
Net cash provided by (used in) investing activities	(33,913)	54,751
Cash Flows from Financing Activities:		
Net increase (decrease) in deposits	11,657	(21,998)
Net increase in federal funds purchased and securities sold under agreements to repurchase	37,655	4,640
Net decrease in other short-term borrowings	—	(1,175)
Common stock dividends paid	(1,391)	—
Preferred stock dividends paid	—	(450)
Net cash provided by (used in) financing activities	47,921	(18,983)
Net increase in cash and cash equivalents	21,402	46,176
Cash and Cash Equivalents:		
Beginning	87,104	87,954

Ending	$108,506	$134,130
Supplemental Disclosures of Cash Flow Information:		
Cash payments for:		
Interest	$2,625	$3,508
Income taxes	286	451
Supplemental Disclosure of Noncash Investing and Financing Activities:		
Transfer of loans to other real estate owned	$114	$780
Sale of OREO financed by issuance of a loan	800	—

See accompanying Notes to Consolidated Financial Statements.

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West Bancorporation, Inc. and Subsidiary
Notes to Consolidated Financial Statements
(unaudited)
(in thousands, except per share information)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared by West Bancorporation, Inc. (the Company) pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements have been condensed or omitted pursuant to such rules and regulations. Although management believes that the disclosures are adequate to make the information presented understandable, it is suggested that these interim consolidated financial statements be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2011. In the opinion of management, the accompanying consolidated financial statements contain all adjustments necessary to present fairly the financial position as of March 31, 2012, and December 31, 2011, and the results of operations, comprehensive income, and cash flows for the three months ended March 31, 2012 and 2011. The results for these interim periods may not be indicative of results for the entire year or for any other period.

The consolidated financial statements have been prepared in conformity with generally accepted accounting principles (GAAP) established by the Financial Accounting Standards Board (FASB). References to GAAP issued by the FASB in these footnotes are to the FASB Accounting Standards Codification™, sometimes referred to as the Codification or ASC. In preparing the financial statements, management is required 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 for the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term are the fair value of financial instruments and other than temporary impairment (OTTI), the valuation of other real estate owned, and the allowance for loan losses.

The accompanying consolidated financial statements include the accounts of the Company, West Bank, West Bank's wholly-owned subsidiary WB Funding Corporation (which owns an interest in a partnership), and West Bank's 99.99 percent owned subsidiary ICD IV, LLC (a community development entity). All significant intercompany transactions and balances have been eliminated in consolidation. In accordance with GAAP, West Bancorporation Capital Trust I is recorded on the books of the Company using the equity method of accounting and is not consolidated.

Certain items in the financial statements as of March 31, 2011, were reclassified to be consistent with the classifications used in the March 31, 2012, financial statements. The reclassification had no effect on net income or stockholders' equity.

Current accounting developments: In April 2011, the FASB issued guidance to improve the accounting for repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. This guidance removes from the assessment of effective control in the accounting for repurchase agreements (a) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee, and (b) the collateral maintenance implementation guidance related to that criterion. The guidance is effective for the first interim and annual periods beginning after December 15, 2011. The adoption of this guidance did not have a material impact on the Company's consolidated financial statements.

In May 2011, the FASB issued amended guidance to improve the comparability of fair value measurements presented and disclosed in financial statements made in accordance with GAAP and International Financial Reporting

Standards. The guidance does not extend the use of fair value accounting, but provides guidance on how it should be applied in situations where it is already required or permitted. The guidance is included in the Codification as part of ASC 820. The guidance is effective for public companies during interim and annual periods beginning after December 15, 2011. The adoption of this guidance did not have a material impact on the Company's consolidated financial statements.

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In June 2011, the FASB issued amended guidance for improving the comparability of financial reporting and to increase the prominence of items reported in other comprehensive income. The guidance eliminated the option to present components of other comprehensive income as part of the changes in stockholders' equity and requires all nonowner changes in stockholders' equity to be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The guidance also requires entities to present all reclassification adjustments from other comprehensive income to net income on the face of the financial statements. The guidance did not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This guidance is included in the Codification as part of ASC 220. The guidance is effective for public companies during interim and annual periods beginning after December 15, 2011 and early adoption was permitted. The Company adopted this guidance effective June 30, 2011. The adoption did not have a material impact on the Company's consolidated financial statements.

2. Critical Accounting Policies

Management has identified its most critical accounting policies to be those related to asset impairment judgments, including fair value and OTTI of available for sale investment securities, the valuation of other real estate owned, and the allowance for loan losses.

Securities available for sale are reported at fair value, with unrealized gains and losses reported as a separate component of accumulated other comprehensive income, net of deferred income taxes. The Company evaluates each of its investment securities whose value has declined below amortized cost to determine whether the decline in fair value is OTTI. The investment portfolio is evaluated for OTTI by segregating the portfolio into two segments and applying the appropriate OTTI model. Investment securities classified as available for sale are generally evaluated for OTTI under FASB ASC 320, Investments - Debt and Equity Securities. However, certain purchased beneficial interests in securitized financial assets, including asset-backed securities and collateralized debt obligations that had credit ratings below AA at the time of purchase, are evaluated using the model outlined in FASB ASC 325, Beneficial Interests in Securitized Financial Assets.

In determining OTTI under the FASB ASC 320 model, the review takes into consideration the severity and duration of the decline in fair value, the length of time expected for recovery, the financial condition of the issuer, and other qualitative factors, as well as whether the Company intends to sell the security or whether it is more likely than not the Company will be required to sell the debt security before its anticipated recovery.

Under the FASB ASC 325 model for the second segment of the portfolio, the Company compares the present value of the remaining cash flows as estimated at the preceding evaluation date to the current expected remaining cash flows. An OTTI is deemed to have occurred if there has been an adverse change in the remaining expected future cash flows.

When OTTI occurs under either model, the amount of the OTTI recognized in earnings depends on whether the Company intends to sell the security or whether it is more likely than not it will be required to sell the security before recovery of its amortized cost basis. If the Company intends to sell or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, the OTTI is recognized in earnings equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. If the Company does not intend to sell the security and it is not more likely than not that the entity will be required to sell before recovery of its amortized cost basis, the OTTI is separated into the amount representing the credit loss and the amount related to all other factors. The amount of the total OTTI related to the credit loss is determined based on the present value of cash flows expected to be collected, using the original yield as the discount rate, and is recognized in earnings. The amount of the total OTTI related to other factors is recognized in other comprehensive income, net of applicable taxes. The previous amortized cost basis less the OTTI recognized in earnings becomes the new amortized cost basis of the investment. The assessment of whether an OTTI exists involves a high degree of subjectivity and

judgment and is based on the information available to management at the time.

Other real estate owned includes real estate properties acquired through or in lieu of foreclosure. They are initially recorded at fair value less estimated selling costs. After foreclosure, valuations are performed by management at least annually by obtaining updated appraisals or other market information. Any subsequent write-downs are recorded as a charge to operations.

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The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that collectibility of the principal is unlikely. The Company has policies and procedures for evaluating the overall credit quality of its loan portfolio, including timely identification of potential problem loans. On a quarterly basis, management reviews the appropriate level for the allowance for loan losses, incorporating a variety of risk considerations, both quantitative and qualitative. Quantitative factors include the Company's historical loss experience, delinquency and charge-off trends, collateral values, known information about individual loans, and other factors. Qualitative factors include the general economic environment in the Company's market areas and the expected trend of those economic conditions. While management uses the best information available to make its evaluations, future adjustments to the allowance may be necessary if there are significant changes in economic conditions or the other factors relied upon. To the extent actual results differ from forecasts and management's judgment, the allowance for loan losses may be greater or less than future charge-offs.

3. Securities Available for Sale

For securities available for sale, the following tables show the amortized cost, unrealized gains and losses (pre-tax) included in accumulated other comprehensive income, and estimated fair value by security type as of March 31, 2012, and December 31, 2011.

	March 31, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
U.S. government agencies and corporations	$17,629	$304	$(118)	$17,815
State and political subdivisions	51,808	2,270	(223)	53,855
Collateralized mortgage obligations [1]	189,880	3,028	(458)	192,450
Mortgage-backed securities [1]	38,645	773	(31)	39,387
Trust preferred securities	6,061	—	(4,115)	1,946
Corporate notes and other investments	735	—	—	735
	$304,758	$6,375	$(4,945)	$306,188

	December 31, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
U.S. government agencies and corporations	$12,644	$371	$(12)	$13,003
State and political subdivisions	50,172	2,398	(53)	52,517
Collateralized mortgage obligations [1]	173,438	2,301	(241)	175,498
Mortgage-backed securities [1]	34,967	706	(37)	35,636
Trust preferred securities	6,105	—	(4,094)	2,011
Corporate notes and other investments	4,764	—	(284)	4,480
	$282,090	$5,776	$(4,721)	$283,145

(1) All collateralized mortgage obligations and mortgage-backed securities consist of residential mortgage pass-through securities guaranteed by GNMA or issued by FNMA, and real estate mortgage investment conduits guaranteed by FHLMC or GNMA.

Securities with an amortized cost of $88,902 and $96,062 as of March 31, 2012, and December 31, 2011, respectively, were pledged as collateral on securities sold under agreements to repurchase and for other purposes as required or permitted by law or regulation. Securities sold under agreements to repurchase are held in safekeeping at a correspondent bank on behalf of the Company.

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The amortized cost and fair value of securities available for sale as of March 31, 2012, by contractual maturity are shown below. Certain securities have call features that allow the issuer to call the securities prior to maturity. Expected maturities may differ from contractual maturities in collateralized mortgage obligations and mortgage-backed securities because principal payments are typically collected sooner than scheduled due to prepayments by the underlying borrowers. Therefore, collateralized mortgage obligations and mortgage-backed securities are not included in the maturity categories within the summary.

	March 31, 2012	
	Amortized Cost	Fair Value
Due in one year or less	$1,154	$1,162
Due after one year through five years	22,213	22,213
Due after five years through ten years	21,186	22,275
Due after ten years	31,680	28,701
	76,233	74,351
Collateralized mortgage obligations and mortgage-backed securities	228,525	231,837
	$304,758	$306,188

The details of the sales of securities for the three months ended March 31, 2012 and 2011, are summarized in the following table.

	Three Months Ended March 31,	
	2012	2011
Proceeds from sales	$3,960	$—
Gross gains on sales	—	—
Gross losses on sales	33	—

The following tables show the fair value and gross unrealized losses, aggregated by investment category and length of time that individual securities have been in a continuous loss position, as of March 31, 2012, and December 31, 2011.

	March 31, 2012					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Gross Unrealized (Losses)	Fair Value	Gross Unrealized (Losses)	Fair Value	Gross Unrealized (Losses)
U.S. government agencies and corporations	$14,867	$(118)	$—	$—	$14,867	$(118)
State and political subdivisions	4,051	(185)	3,105	(38)	7,156	(223)
Collateralized mortgage obligations	41,707	(458)	—	—	41,707	(458)
Mortgage-backed securities	5,193	(31)	—	—	5,193	(31)
Trust preferred securities	—	—	1,946	(4,115)	1,946	(4,115)
	$65,818	$(792)	$5,051	$(4,153)	$70,869	$(4,945)

	December 31, 2011					
	Less than 12 months		12 months or longer		Total	
	Fair Value	Gross Unrealized (Losses)	Fair Value	Gross Unrealized (Losses)	Fair Value	Gross Unrealized (Losses)
U.S. government agencies and corporations	$4,988	$(12)	$—	$—	$4,988	$(12)
State and political subdivisions	—	—	3,090	(53)	3,090	(53)
Collateralized mortgage obligations	38,175	(241)	—	—	38,175	(241)
Mortgage-backed securities	17,898	(37)	—	—	17,898	(37)

Trust preferred securities	—	—	2,011	(4,094)	2,011	(4,094)
Corporate notes and other investments	—	—	3,708	(284)	3,708	(284)
	$61,061	$(290)	$8,809	$(4,431)	$69,870	$(4,721)

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See Note 2 for a discussion of financial reporting for securities with unrealized losses. As of March 31, 2012, the available for sale investment portfolio included two municipal securities and two trust preferred securities (TPS) with unrealized losses that have existed for longer than one year.

The Company believes the unrealized losses on investments in U.S. government agency securities, municipal obligations, collateralized mortgage obligations and mortgage-backed securities are due to market conditions, not reduced estimated cash flows. The Company does not have the intent to sell these securities, does not anticipate that these securities will be required to be sold before anticipated recovery, and expects full principal and interest to be collected. Therefore, the Company does not consider these investments to have OTTI at March 31, 2012.

The Company believes the unrealized loss of $976 on an investment in one single-issuer TPS issued by Heartland Financial, USA, Inc. is due to market conditions, not reduced estimated cash flows. The Company does not have the intent to sell this security, does not anticipate that this security will be required to be sold before anticipated recovery, and expects full principal and interest will be collected. Therefore, the Company does not consider this investment to have OTTI at March 31, 2012.

As of March 31, 2012, the Company had one pooled TPS, ALESCO Preferred Funding X, Ltd., it considered to be OTTI. The Company engaged an independent consulting firm to assist in the valuation of this security. Based on that valuation, management determined the security had an estimated fair value of $1,189 at March 31, 2012. The consulting firm first evaluated the credit quality of each of the 77 underlying issuers within the pool by reviewing a comprehensive database of financial information and/or publicly-filed financial statements. On the basis of this information and a review of historical industry default data and current and near-term operating conditions, default and recovery probabilities for each underlying issuer within the asset were estimated. For issuers who had already defaulted, no recovery was assumed. For deferring issuers, an assumption was made that the majority of deferring issuers will continue to defer and will eventually default. Each deferring issuer is reviewed on a case-by-case basis and, in some instances, a probability is assigned that the deferral will ultimately be cured. The issuer-specific assumptions are then aggregated into cumulative weighted-average default, recovery, and prepayment probabilities. The collateral prepayment assumptions were affected by the view that the terms and pricing of TPSs and subordinated debt issued by banks and insurance companies were so aggressive that it is unlikely that such financing will become available in the foreseeable future. Therefore, the assumption was made that no issuer will prepay over the life of the TPS. In light of generally weak collateral credit performance and a challenging U.S. credit and real estate environment, the assumptions generally imply more issuer defaults during the next two to three years than those that had been experienced historically, and a gradual leveling off of defaults thereafter.

In accordance with ASC 325, a discounted cash flow model was used to determine the estimated fair value of this security. The methodology for determining the appropriate discount rate for a TPS for purposes of determining fair value combines an evaluation of current market yields for comparable corporate and structured credit products with an evaluation of the risks associated with the TPS cash flows. As a result of this analysis and due to the fixed-rate nature of the instrument's contractual interest cash flows, a discount rate of the three-month LIBOR plus 14 percent (a lifetime average all-in discount rate of approximately 17 percent) was used for determination of fair value as of March 31, 2012, and an all-in discount rate of approximately 18 percent was used as of December 31, 2011. For purposes of determining any credit loss, projected cash flows were discounted at the original rate of three-month LIBOR plus 1.25 percent. Future fair value estimates for this security may vary due to changes in market interest rates and credit performance of the underlying collateral. Any additional deferrals or defaults of the underlying issuers will have a negative impact on the value of the pooled TPS, because there is no excess collateral to absorb any future defaults.

Based on the valuation work performed, an additional credit loss of $46 was recognized in first quarter 2012 earnings and none was recognized in the first quarter of 2011. The remaining unrealized loss of $3,139 is reflected in

accumulated other comprehensive income, net of taxes of $1,193. The Company will continue to periodically estimate the present value of cash flows expected to be collected over the life of the security.

The following table provides a roll forward of the amount of credit-related losses recognized in earnings for the three months ended March 31, 2012 and 2011.

	Three Months Ended March 31,	
	2012	2011
Balance at beginning of period	$526	$427
Current period credit loss recognized in earnings	46	—
Reductions for securities sold during the period	—	—
Reductions for securities where there is an intent to sell or requirement to sell	—	—
Reductions for increases in cash flows expected to be collected	—	—
Balance at end of period	$572	$427

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4. Loans and Allowance for Loan Losses

Loans consist of the following segments as of March 31, 2012, and December 31, 2011.

	March 31, 2012	December 31, 2011
Commercial	$256,854	$255,702
Real estate:		
Construction, land, and land development	104,006	101,607
1-4 family residential first mortgages	62,703	63,218
Home equity	23,080	26,423
Commercial	397,047	386,137
Consumer and other loans	5,516	6,155
	849,206	839,242
Net unamortized fees and costs	165	283
	$849,041	$838,959

Real estate loans of approximately $350,000 and $337,000 were pledged as security for FHLB advances as of March 31, 2012 and December 31, 2011, respectively.

Loans are stated at the principal amounts outstanding, net of unamortized loan fees and costs, with interest income recognized on the interest method based upon those outstanding loan balances. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method. Loans are reported by the portfolio segments identified above and are analyzed by management on this basis. All loan policies identified below apply to all segments of the loan portfolio.

Delinquencies are determined based on the payment terms of the individual loan agreements. The accrual of interest on past due and other impaired loans is generally discontinued at 90 days or when, in the opinion of management, the borrower may be unable to make all contractual payments pursuant to contractual terms. Unless considered collectible, all interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income, if accrued in the current year, or charged to the allowance for loan losses, if accrued in the prior year. Generally, all payments received while a loan is on nonaccrual status are applied to the principal balance of the loan. Loans are returned to accrual status when all principal and interest amounts contractually due are brought current and future payments are reasonably assured.

A loan is classified as a troubled debt restructured (TDR) loan when the Company concludes that a borrower is experiencing financial difficulties and a concession was granted that would not otherwise be considered. Concessions may include a restructuring of the terms of a loan to alleviate the burden on the borrower's cash requirements, such as an extension of the payment terms beyond the original maturity date or a change in the interest rate charged. TDR loans with extended payment terms are accounted for as impaired until performance is established. A change to the interest rate would change the classification of a loan to a TDR loan if the restructured loan yields a rate which is below a market rate for that of a new loan with comparable risk. TDR loans with below market rates are considered impaired until fully collected. TDR loans may be reported as nonaccrual rather than TDR, if they are not performing per the restructured terms.

Based upon its ongoing assessment of credit quality within the loan portfolio, the Company maintains a Watch List, which includes classified loans. These loans involve the anticipated potential for payment defaults or collateral inadequacies. A loan on the Watch List is considered impaired when management believes it is probable the Company will be unable to collect all contractual principal and interest payments due in accordance with the terms of the loan agreement. Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. The amount of impairment, if any, and any subsequent changes are

included in the allowance for loan losses.

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The following table sets forth the recorded investment in nonperforming loans, disaggregated by segment, held by the Company as of March 31, 2012, and December 31, 2011. The recorded investment represents principal balances net of any partial charge-offs. Related accrued interest and net unamortized fees and costs are immaterial and are excluded from the table.

	March 31, 2012	December 31, 2011
Nonaccrual loans:		
Commercial	$800	$800
Real estate:		
Construction, land, and land development	4,220	4,220
1-4 family residential first mortgages	907	923
Home equity	—	—
Commercial	2,629	2,629
Consumer and other loans	—	—
Total nonaccrual loans	8,556	8,572
Loans past due 90 days and still accruing interest:		
Commercial	—	—
Real estate:		
Construction, land, and land development	—	—
1-4 family residential first mortgages	—	—
Home equity	—	—
Commercial	—	—
Consumer and other loans	—	—
Total loans past due 90 days and still accruing interest	—	—
Troubled debt restructured loans(1):		
Commercial	28	—
Real estate:		
Construction, land, and land development	1,089	1,094
1-4 family residential first mortgages	170	171
Home equity	—	—
Commercial	848	856
Consumer and other loans	—	—
Total troubled debt restructured loans	2,135	2,121
Total nonperforming loans	$10,691	$10,693

(1) While TDR loans are commonly reported by the industry as nonperforming, those not classified in the nonaccrual category are accruing interest due to payment performance. TDR loans on nonaccrual status would be included in the nonaccrual category if there were any, however, there were none at these dates.

The following table shows the pre- and post-modification recorded investment in TDR loans by type of modification and loan segment that have occurred during the three months ended March 31, 2012.

	Three Months Ended March 31, 2012		
	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Lengthened amortization:			
Commercial	1	$28	$28
Real estate:			
Construction, land, and land development	—	—	—
1-4 family residential first mortgages	—	—	—
Home equity	—	—	—

Commercial	—	—	—
Consumer and other loans	—	—	—
	1	$28	$28

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There was no financial impact for specific reserves or from charge-offs for the modified loan included in the previous table. There were no TDR loans that have been modified within the previous twelve months and have subsequently had a payment default during the three months ended March 31, 2012.

The following tables summarize the recorded investment in impaired loans by segment, broken down by loans with no related allowance and loans with a related allowance and the amount of that allowance as of March 31, 2012, and December 31, 2011, and the average recorded investment and interest income recognized on these loans for the three months ended March 31, 2012 and March 31, 2011.

	March 31, 2012			December 31, 2011		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:						
Commercial	$827	$827	N/A	$800	$800	N/A
Real Estate:						
Construction, land, and land development	—	—	N/A	—	—	N/A
1-4 family residential	1,077	1,092	N/A	1,094	1,094	N/A
Home equity	—	—	N/A	—	—	N/A
Commercial	3,478	4,671	N/A	3,484	4,678	N/A
Consumer and other	—	—	N/A	—	—	N/A
	5,382	6,590	N/A	5,378	6,572	N/A
With an allowance recorded:						
Commercial	7	7	$—	4,577	4,577	$100
Real Estate:						
Construction, land, and land development	16,466	16,466	2,630	17,359	17,359	2,630
1-4 family residential	743	743	113	283	283	84
Home equity	—	—	—	156	156	156
Commercial	1,269	1,269	200	1,278	1,278	200
Consumer and other	32	32	11	42	42	12
	18,517	18,517	2,954	23,695	23,695	3,182
Total:						
Commercial	834	834	—	5,377	5,377	100
Real Estate:						
Construction, land, and land development	16,466	16,466	2,630	17,359	17,359	2,630
1-4 family residential	1,820	1,835	113	1,377	1,377	84
Home equity	—	—	—	156	156	156
Commercial	4,747	5,940	200	4,762	5,956	200
Consumer and other	32	32	11	42	42	12
	$23,899	$25,107	$2,954	$29,073	$30,267	$3,182

N/A - Not applicable.

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	Three months ended March 31, 2012		Three months ended March 31, 2011	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:				
Commercial	$807	$—	$2,261	$—
Real Estate:				
Construction, land, and land development	2,110	—	138	2
1-4 family residential	1,089	1	989	1
Home equity	—	—	24	—
Commercial	3,510	20	5,688	40
Consumer and other	—	—	13	—
	7,516	21	9,113	43
With an allowance recorded:				
Commercial	2,290	24	6,997	65
Real Estate:				
Construction, land, and land development	15,023	161	14,004	173
1-4 family residential	390	7	124	—
Home equity	78	—	—	—
Commercial	1,273	24	—	—
Consumer and other	37	1	44	1
	19,091	217	21,169	239
Total:				
Commercial	3,097	24	9,258	65
Real Estate:				
Construction, land, and land development	17,133	161	14,142	175
1-4 family residential	1,479	8	1,113	1
Home equity	78	—	24	—
Commercial	4,783	44	5,688	40
Consumer and other	37	1	57	1
	$26,607	$238	$30,282	$282

The following table reconciles the balance of nonaccrual loans with impaired loans as of March 31, 2012, and December 31, 2011.

	March 31, 2012	December 31, 2011
Nonaccrual loans	$8,556	$8,572
Troubled debt restructured loans	2,135	2,121
Other impaired loans still accruing interest	13,208	18,380
Total impaired loans	$23,899	$29,073

The balance of impaired loans at March 31, 2012 and December 31, 2011, was comprised of 16 different borrowers. The Company has no commitments to advance additional funds on any of the impaired loans.

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The following tables provide an analysis of the payment status of the recorded investment in loans as of March 31, 2012, and December 31, 2011.

	March 31, 2012						
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Current	Total Loans	90 Days and Still Accruing
Commercial	$291	$—	$—	$291	$256,563	$256,854	$—
Real estate:							
Construction, land, and land development	—	—	4,220	4,220	99,786	104,006	—
1-4 family residential first mortgages	924	—	809	1,733	60,970	62,703	—
Home equity	5	—	—	5	23,075	23,080	—
Commercial	246	—	2,519	2,765	394,282	397,047	—
Consumer and other	5	—	—	5	5,511	5,516	—
Total	$1,471	$—	$7,548	$9,019	$840,187	$849,206	$—
Nonaccrual loans included above	$—	$—	$7,548	$7,548	$1,008	$8,556	N/A

	December 31, 2011						
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Current	Total Loans	90 Days and Still Accruing
Commercial	$179	$1	$—	$180	$255,522	$255,702	$—
Real estate:							
Construction, land, and land development	4,220	—	—	4,220	97,387	101,607	—
1-4 family residential first mortgages	703	6	809	1,518	61,700	63,218	—
Home equity	47	75	—	122	26,301	26,423	—
Commercial	—	60	2,434	2,494	383,643	386,137	—
Consumer and other	1	—	—	1	6,154	6,155	—
Total	$5,150	$142	$3,243	$8,535	$830,707	$839,242	$—
Nonaccrual loans included above	$4,235	$60	$3,243	$7,538	$1,034	$8,572	N/A

N/A - Not applicable

The following tables show the recorded investment in loans by credit quality indicator and loan segment as of March 31, 2012, and December 31, 2011.

	March 31, 2012				
	Pass	Watch	Substandard	Doubtful	Total
Commercial	$233,311	$5,777	$17,766	$—	$256,854
Real estate:					
Construction, land, and land development	83,326	454	20,226	—	104,006
1-4 family residential first mortgages	59,883	724	2,096	—	62,703
Home equity	22,644	348	88	—	23,080
Commercial	377,738	6,167	13,142	—	397,047

Consumer and other	5,427	57	32	—	5,516
Total	$782,329	$13,527	$53,350	$—	$849,206

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	December 31, 2011				
	Pass	Watch	Substandard	Doubtful	Total
Commercial	$227,088	$10,458	$18,156	$—	$255,702
Real estate:					
Construction, land, and land development	78,402	2,087	21,118	—	101,607
1-4 family residential first mortgages	60,474	664	2,080	—	63,218
Home equity	25,987	280	156	—	26,423
Commercial	367,094	6,209	12,834	—	386,137
Consumer and other	6,029	72	54	—	6,155
Total	$765,074	$19,770	$54,398	$—	$839,242

All loans are subject to the assessment of a credit quality indicator. Risk ratings are assigned for each loan at the time of approval and change as circumstances dictate during the term of the loan. The Company utilizes a 9-point risk rating scale as shown below, with ratings 1 - 5 included in the Pass column, rating 6 included in the Watch column, ratings 7 - 8 included in the Substandard column, and rating 9 included in the Doubtful column. The Substandard column includes all loans classified as impaired as well as loans with ratings 7 and 8, which are included in the general evaluation of the allowance for loan losses.

Risk rating 1: The loan is secured by cash equivalent collateral.

Risk rating 2: The loan is secured by properly margined marketable securities, bonds, or cash surrender value of life insurance.

Risk rating 3: The borrower is in strong financial condition and has strong debt service capacity. The loan is performing as agreed and the financial characteristics and trends of the borrower exceed industry statistics.

Risk rating 4: The borrower is in satisfactory financial condition and has satisfactory debt service capacity. The loan is performing as agreed and the financial characteristics and trends of the borrower fall in line with industry statistics.

Risk rating 5: The borrower's financial condition is less than satisfactory. The loan is still generally paying as agreed, but strained cash flow may cause some slowness in payments. Collateral values adequately preclude loss. Financial characteristics and trends lag industry statistics. There may be noncompliance with loan covenants.

Risk rating 6: The borrower's financial condition is deficient. Payment delinquencies may be more common. Collateral values still protect from loss, but margins are narrow. Loan may be reliant on secondary sources of repayment, including liquidation of collateral and guarantor support.

Risk rating 7: The loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Well-defined weaknesses exist that jeopardize the liquidation of the debt. The Company is inadequately protected by the valuation or paying capacity of the collateral pledged. If deficiencies are not corrected, there is a distinct possibility that a loss will be sustained.

Risk rating 8: All the characteristics of rating 7 exist with the added condition that the loan is past due more than 90 days or there is reason to believe the Company will not receive its principal and interest according to the terms of the loan agreement.

Risk rating 9: All of the weaknesses inherent in risk ratings 7 and 8 exist with the added condition that collection or liquidation, on the basis of currently known facts, conditions, and values is highly questionable and improbable. A loan reaching this category would most likely be charged off.

Credit quality indicators for all loans and the Company's risk rating process are dynamic and updated on a continuous basis. Risk ratings are updated as circumstances that could affect the repayment of an individual loan are brought to management's attention through an established monitoring process. Individual lenders initiate changes as appropriate for ratings 1 through 5 and changes for ratings 6 through 9 are initiated via communications with management. The likelihood of loss increases as the risk rating increases and is generally preceded by a loan appearing on the Watch List, which consists of all loans with a risk rating of 6 or worse.

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In all portfolio segments, the primary risks are that a borrower's income stream diminishes to the point they are not able to make scheduled principal and interest payments and any collateral securing the loan has declined in value. For commercial loans, including construction and commercial real estate loans, that income stream is generated by the operations of the business. For consumer loans, including 1-4 family residential and home equity loans, that income stream typically consists of wages. The risk of declining collateral values is present for most types of loans. For commercial loans, accounts receivable, fixed assets, and inventory generally comprise the collateral. Accounts receivable can diminish in value if collections are not timely. Fixed assets tend to depreciate over time and inventory can become obsolete. For all types of loans secured by real estate, it is possible for the value of the real estate to decline.

The allowance for loan losses is established through a provision for loan losses charged to expense. Loans in each of the Company's segments are charged against the allowance for loan losses when management believes that collectibility of the principal is unlikely. The allowance is an amount that management believes will be adequate to absorb probable losses on existing loans, based on an evaluation of the collectibility of loans and prior loss experience. This evaluation also takes into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, the review of specific problem loans, and current economic conditions that may affect the borrower's ability to pay. While management uses the best information available to make its evaluation, future adjustments to the allowance may be necessary if there are significant changes in economic conditions or the other factors relied upon.

The allowance for loan losses consists of specific and general components. The specific component relates to loans that meet the definition of impaired. The general component covers the remaining loans and is based on historical loss experience adjusted for qualitative factors such as delinquency trends, loan growth, economic elements, and local market conditions. These same policies are applied to all segments of loans. In addition, regulatory agencies, as integral parts of their examination processes, periodically review West Bank's allowance for loan losses, and may require West Bank to make additions to the allowance based on their judgments about information available to them at the time of their examinations.

The following tables detail changes in the allowance for loan losses by segment for the three months ended March 31, 2012 and 2011.

	Three Months Ended March 31, 2012						
		Real Estate					
	Commercial	Construction and Land	1-4 Family Residential	Home Equity	Commercial	Consumer and Other	Total
Beginning balance	$4,409	$3,572	$ 1,215	$832	$ 6,667	$ 83	$16,778
Charge-offs	—	(42)	(39)	(95)	—	(12)	(188)
Recoveries	47	—	7	5	—	2	61
Provision [(1)]	(540)	604	51	(141)	30	(4)	—
Ending balance	$3,916	$4,134	$ 1,234	$601	$ 6,697	$ 69	$16,651

	Three Months Ended March 31, 2011						
		Real Estate					
	Commercial	Construction and Land	1-4 Family Residential	Home Equity	Commercial	Consumer and Other	Total
Beginning balance	$7,940	$3,787	$ 647	$658	$ 5,823	$ 232	$19,087
Charge-offs	(1,479)	—	(526)	—	(248)	—	(2,253)
Recoveries	153	—	16	5	—	2	176
Provision [(1)]	(512)	103	492	54	441	(78)	500

Ending balance	$6,102	$3,890	$ 629	$717	$ 6,016	$156	$17,510

(1) The negative provisions for the various segments are either related to the decline in each of those portfolio segments during the time periods disclosed or improvement in the credit quality factors related to those portfolio segments.

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The following tables show a breakdown of the allowance for loan losses disaggregated on the basis of impairment analysis method by segment as of March 31, 2012, and December 31, 2011.

	March 31, 2012						
		Real Estate					
	Commercial	Construction and Land	1-4 Family Residential	Home Equity	Commercial	Consumer and Other	Total
Ending balance:							
Individually evaluated for impairment	$—	$2,630	$ 113	$—	$ 200	$ 11	$2,954
Collectively evaluated for impairment	3,916	1,504	1,121	601	6,497	58	13,697
Total	$3,916	$4,134	$ 1,234	$601	$ 6,697	$ 69	$16,651

	December 31, 2011						
		Real Estate					
	Commercial	Construction and Land	1-4 Family Residential	Home Equity	Commercial	Consumer and Other	Total
Ending balance:							
Individually evaluated for impairment	$100	$2,630	$ 84	$156	$ 200	$ 12	$3,182
Collectively evaluated for impairment	4,309	942	1,131	676	6,467	71	13,596
Total	$4,409	$3,572	$ 1,215	$832	$ 6,667	$ 83	$16,778

The following tables show the recorded investment in loans, exclusive of unamortized fees and costs, disaggregated on the basis of impairment analysis method by segment as of March 31, 2012, and December 31, 2011.

	March 31, 2012						
		Real Estate					
	Commercial	Construction and Land	1-4 Family Residential	Home Equity	Commercial	Consumer and Other	Total
Ending balance:							
Individually evaluated for impairment	$834	$16,466	$ 1,821	$—	$ 4,746	$ 32	$23,899
Collectively evaluated for impairment	256,020	87,540	60,882	23,080	392,301	5,484	825,307
Total	$256,854	$104,006	$ 62,703	$23,080	$ 397,047	$ 5,516	$849,206

	December 31, 2011						
		Real Estate					
	Commercial	Construction and Land	1-4 Family Residential	Home Equity	Commercial	Consumer and Other	Total
Ending balance:							
Individually evaluated for impairment	$5,377	$17,359	$ 1,377	$156	$ 4,762	$ 42	$29,073
Collectively evaluated for impairment	250,325	84,248	61,841	26,267	381,375	6,113	810,169

Total	$255,702	$101,607	$ 63,218	$26,423	$ 386,137	$6,155	$839,242

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5. Fair Value Measurements

Accounting guidance on fair value measurements and disclosures defines fair value, establishes a framework for measuring the fair value of assets and liabilities using a hierarchy system, and defines required disclosures. It clarifies that fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in the market in which the reporting entity transacts business.

The Company's balance sheet contains securities available for sale that are recorded at fair value on a recurring basis. The three-level valuation hierarchy for disclosure of fair value is as follows:

Level 1 uses quoted market prices in active markets for identical assets or liabilities.

Level 2 uses observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3 uses unobservable inputs that are not corroborated by market data.

When available, quoted market prices are used to determine the fair value of investment securities and such items are classified within Level 1 of the fair value hierarchy. Examples include U.S. Treasury securities and certain corporate bonds. For other securities, the Company determines fair value based on various sources and may apply matrix pricing with observable prices for similar bonds where a price for the identical bond is not observable. Securities measured at fair value by such methods are classified as Level 2. The fair values of Level 2 securities are determined by pricing models that consider observable market data, such as interest rate volatilities, LIBOR yield curve, credit spreads and prices from market makers, and live trading systems. Certain securities are not valued based on observable inputs and are, therefore, classified as Level 3. The fair value of these securities is based on management's best estimates. The Company's policy is to recognize transfers between levels at the end of each reporting period, if applicable.

Generally, management obtains the fair value of investment securities at the end of each reporting period via a third party pricing service. Management, with the assistance of an independent investment advisory firm, reviewed the valuation process used by the third party and believes that process is valid. On a quarterly basis management corroborates the fair values of investment securities by obtaining pricing from an independent investment advisory firm and compares the two sets of fair values. Any significant variances are reviewed and investigated. In addition, the Company has instituted a practice of further testing the fair values of a sample of securities. For that sample, the prices are further validated by management, with assistance from an independent investment advisory firm, by obtaining details of the inputs used by the pricing service. Those inputs were independently tested, and we concluded the fair values were consistent with GAAP requirements and securities were properly classified in the fair value hierarchy.

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The following tables present the balances of assets and liabilities measured at fair value on a recurring basis by level as of March 31, 2012, and December 31, 2011.

	March 31, 2012			
Description	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
U.S. government agencies and corporations	$17,815	$—	$17,815	$—
State and political subdivisions	53,855	—	53,855	—
Collateralized mortgage obligations	192,450	—	192,450	—
Mortgage-backed securities	39,387	—	39,387	—
Trust preferred securities	1,946	—	757	1,189
Corporate notes and other investments	735	—	735	—
Total	$306,188	$—	$304,999	$1,189

	December 31, 2011			
Description	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
U.S. government agencies and corporations	$13,003	$—	$13,003	$—
State and political subdivisions	52,517	—	52,517	—
Collateralized mortgage obligations	175,498	—	175,498	—
Mortgage-backed securities	35,636	—	35,636	—
Trust preferred securities	2,011	—	766	1,245
Corporate notes and other investments	4,480	3,708	772	—
Total	$283,145	$3,708	$278,192	$1,245

There were no transfers between Levels of the fair value hierarchy during the three months ended March 31, 2012.

The following table presents changes in securities available for sale with significant unobservable inputs (Level 3) for the three months ended March 31, 2012 and 2011.

	Three Months Ended March 31,	
	2012	2011
Beginning balance	$1,245	$1,339
Transfer into level 3	—	—
Total gains or (losses):		
Included in earnings	(46)	—
Included in other comprehensive income	(10)	88
Sale of security	—	—
Principal payments	—	—
Ending balance	$1,189	$1,427

The ending balances in the previous table consist of one pooled TPS valued at $1,189 as of March 31, 2012.

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Certain assets are measured at fair value on a nonrecurring basis; that is, they are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). The following tables present those assets carried on the balance sheet by caption and by level within the valuation hierarchy as of March 31, 2012, and December 31, 2011.

	March 31, 2012			
Description	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Loans	$15,563	$—	$—	$15,563
Other real estate owned	9,963	—	—	9,963
Total	$25,526	$—	$—	$25,526

	December 31, 2011			
Description	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Loans	$20,513	$—	$—	$20,513
Other real estate owned	10,967	—	—	10,967
Total	$31,480	$—	$—	$31,480

Loans in the tables above consist of impaired loans for which a fair value adjustment has been recorded. Impaired loans are evaluated and valued at the lower of cost or fair value when the loan is identified as impaired. Fair value is measured based on the value of the collateral securing these loans and is classified as Level 3 in the fair value hierarchy. Collateral may be real estate or business assets such as equipment, inventory, or accounts receivable. Fair value is determined by appraisals. Appraised or reported values may be discounted based on management's opinions concerning market developments or the client's business. Other real estate owned in the tables above consist of property acquired through foreclosures and settlements of loans. Property acquired is carried at fair value of the property, less estimated disposal costs, and is classified as Level 3 in the fair value hierarchy.

GAAP requires disclosure of the fair value of financial assets and financial liabilities, including those that are not measured and reported at fair value on a recurring basis or nonrecurring basis. The methodologies for estimating the fair value of financial assets and financial liabilities that are measured at fair value on a recurring or nonrecurring basis are discussed above. The methodologies for other financial assets and financial liabilities are discussed below.

Cash and due from banks: The carrying amount approximates fair value.

Federal funds sold: The carrying amount approximates fair value.

Federal Home Loan Bank stock: The fair value of this restricted stock is estimated at its carrying value and redemption price of $100 per share.

Loans held for sale: The fair values of loans held for sale are based on estimated selling prices.

Loans: The fair values of loans are estimated using discounted cash flow analysis based on observable market interest rates currently being offered for loans with similar terms to borrowers with similar credit quality.

Deposits: The carrying amounts for demand and savings deposits, which represent the amounts payable on demand, approximate their fair values. The fair values for fixed-rate and variable-rate certificates of deposit are estimated using discounted cash flow analysis, based on observable market interest rates currently being offered on certificates with similar terms.

Accrued interest receivable and payable: The fair values of both accrued interest receivable and payable approximate their carrying amounts.

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Short-term and other borrowings: The carrying amounts of federal funds purchased and securities sold under agreements to repurchase approximate their fair values. The fair values of Federal Home Loan Bank (FHLB) advances and subordinated notes are estimated using discounted cash flow analysis, based on observable market interest rates currently being offered with similar terms.

Commitments to extend credit and standby letters of credit: The approximate fair values of commitments and standby letters of credit are based on the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and creditworthiness of the counterparties.

The following table includes the carrying amounts and approximate fair values as of March 31, 2012, and December 31, 2011.

		March 31, 2012		December 31, 2011	
	Fair Value Hierarchy Level	Carrying Amount	Approximate Fair Value	Carrying Amount	Approximate Fair Value
Financial assets:					
Cash and due from banks	Level 1	$32,803	$32,803	$35,772	$35,772
Federal funds sold	Level 1	75,703	75,703	51,332	51,332
Securities available for sale	See previous table	306,188	306,188	283,145	283,145
Federal Home Loan Bank stock	Level 1	11,475	11,475	11,352	11,352
Loans held for sale	Level 2	901	907	4,089	4,139
Loans, net	Level 2	832,390	842,963	822,181	829,675
Accrued interest receivable	Level 1	5,871	5,871	4,183	4,183
Financial liabilities:					