AMES NATIONAL CORP
Form 10-K
March 10, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2010. Commission File Number 0-32637.

AMES NATIONAL CORPORATION
(Exact name of registrant as specified in its charter)

IOWA	42-1039071
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
405 FIFTH STREET, AMES, IOWA	50010
(Address of principal executive offices)	(Zip Code)

(515) 232-6251
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Exchange Act: NONE

Securities registered pursuant to Section 12(g) of the Exchange Act:

COMMON STOCK, $2.00 PAR VALUE
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act 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 during the preceding 12 months (of for such shorter period that the registrant was required to submit and post such files). Yes o No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this
Form 10-K. 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 "accelerated filer, large accelerated filer, and a 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 June 30, 2010, the aggregate market value of voting stock held by non-affiliates of the registrant, based upon the closing sale price for the registrant's common stock in the NASDAQ Capital Market, was $178,066,848. Shares of common stock beneficially owned by each executive officer and director of the Company and by each person who beneficially owns 5% or more of the outstanding common stock have been excluded on the basis that such persons may be deemed to be an affiliate of the registrant. This determination of affiliate status is not necessarily a conclusive determination for any other purpose.

The number of shares outstanding of the registrant's common stock on February 28, 2011, was 9,432,915.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement, as filed with the Securities and Exchange Commission on March 18, 2011, are incorporated by reference into Part III of this Form 10-K.

TABLE OF CONTENTS

Part I		
Item 1.	Business	3
Item 1A.	Risk Factors	20
Item 1B.	Unresolved Staff Comments	25
Item 2.	Properties	25
Item 3.	Legal Proceedings	26
Item 4.	Reserved	26
Part II		
Item 5.	Market for Registrant's Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities	27
Item 6.	Selected Financial Data	28
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	29
Item 7A.	Quantitative and Qualitative Disclosures about Market Risk	64
Item 8.	Financial Statements and Supplementary Data	67
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	109
Item 9A.	Controls and Procedures	109
Item 9B.	Other Information	109
Part III		
Item 10.	Directors, Executive Officers and Corporate Governance	109
Item 11.	Executive Compensation	110
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters	110
Item 13.	Certain Relationships and Related Transactions and Director Independence	110
Item 14.	Principal Accountant Fees and Services	111
Part IV		
Item 15.	Exhibits and Financial Statement Schedules	111

Table of Contents

PART I

ITEM 1. BUSINESS

General

Ames National Corporation (the "Company") is an Iowa corporation and bank holding company registered under the Bank Holding Company Act of 1956, as amended. The Company owns 100% of the stock of five banking subsidiaries consisting of two national banks and three state-chartered banks, as described below. All of the Company's operations are conducted in the State of Iowa and primarily within the central Iowa counties of Boone, Marshall, Polk and Story where the Company's banking subsidiaries are located. The Company does not engage in any material business activities apart from its ownership of its banking subsidiaries. The principal executive offices of the Company are located at 405 Fifth Street, Ames, Iowa 50010. The Company's telephone number is (515) 232-6251 and website address is www.amesnational.com.

The Company was organized and incorporated on January 21, 1975 under the laws of the State of Iowa to serve as a holding company for its principal banking subsidiary, First National Bank, Ames, Iowa ("First National") located in Ames, Iowa. In 1983, the Company acquired the stock of the State Bank & Trust Co. ("State Bank") located in Nevada, Iowa; in 1991, the Company, through a newly-chartered state bank known as Boone Bank & Trust Co. ("Boone Bank"), acquired certain assets and assumed certain liabilities of the former Boone State Bank & Trust Company located in Boone, Iowa; in 1995, the Company acquired the stock of the Randall-Story State Bank ("Randall-Story Bank") located in Story City, Iowa; and in 2002, the Company chartered and commenced operations of a new national banking organization, United Bank & Trust NA ("United Bank"), located in Marshalltown, Iowa. First National, State Bank, Boone Bank, Randall-Story Bank and United Bank are each operated as a wholly owned subsidiary of the Company. These five financial institutions are referred to in this Form 10-K collectively as the "Banks" and individually as a "Bank".

The principal sources of Company revenue are: (i) interest and fees earned on loans made by the Company and Banks; (ii) interest on fixed income investments held by the Company and the Banks; (iii) fees on trust services provided by those Banks exercising trust powers; (iv) service charges on deposit accounts maintained at the Banks; and (v) securities gains. The Company's principal expenses are: (i) interest expense on deposit accounts and other borrowings; (ii) salaries and employee benefits; (iii) data processing costs associated with maintaining the Banks' loan and deposit functions; (iv) occupancy expenses for maintaining the Banks' facilities; and (v) FDIC insurance assessments. The largest component contributing to the Company's net income is net interest income, which is the difference between interest earned on earning assets (primarily loans and investments) and interest paid on interest bearing liabilities (primarily deposit accounts and other borrowings). One of management's principal functions is to manage the spread between interest earned on earning assets and interest paid on interest bearing liabilities in an effort to maximize net interest income while maintaining an appropriate level of interest rate risk.

Table of Contents

The Banks' lending activities consist primarily of short-term and medium-term commercial and residential real estate loans, agricultural and business operating loans and lines of credit, equipment loans, vehicle loans, personal loans and lines of credit, home improvement loans and origination of mortgage loans for sale into the secondary market. The Banks also offer a variety of demand, savings and time deposits, cash management services, merchant credit card processing, safe deposit boxes, wire transfers, direct deposit of payroll and social security checks and automated teller machine access. Four of the five Banks also offer trust services.

The Company provides various services to the Banks which include, but are not limited to, management assistance, internal auditing services, human resources services and administration, compliance management, marketing assistance and coordination, loan review and support with respect to computer systems and related procedures.

Banking Subsidiaries

First National Bank, Ames, Iowa. First National is a nationally-chartered, commercial bank insured by the Federal Deposit Insurance Corporation (the "FDIC"). It was organized in 1903 and became a wholly owned subsidiary of the Company in 1975 through a bank holding company reorganization whereby the then shareholders of First National exchanged all of their First National stock for stock in the Company. First National provides full-service banking to businesses and residents within the Ames community and surrounding area. It provides a variety of products and services designed to meet the needs of the market it serves. It has an experienced staff of bank officers including many who have spent the majority of their banking careers with First National and who emphasize long-term customer relationships. First National conducts business out of three full-service offices, all located in the city of Ames and a full-service office built in Ankeny, Iowa that opened in April of 2007.

As of December 31, 2010, First National had capital of $52,342,000 and 90 full-time equivalent employees. Full-time equivalents represent the number of people a business would employ if all its employees were employed on a full-time basis. It is calculated by dividing the total number of hours worked by all full and part-time employees by the number of hours a full-time individual would work for a given period of time. First National had net income for the years ended December 31, 2010, 2009 and 2008 of approximately $6,869,000, $5,309,000 and $1,237,000, respectively. Total assets as of December 31, 2010, 2009 and 2008 were approximately $519,836,000, $471,243,000 and $445,212,000, respectively.

State Bank & Trust Co., Nevada, Iowa. State Bank is an Iowa, state-chartered, FDIC insured commercial bank. State Bank was acquired by the Company in 1983 through a stock transaction whereby the then shareholders of State Bank exchanged all their State Bank stock for stock in the Company. State Bank was organized in 1939 and provides full-service banking to businesses and residents within the Nevada area from its main Nevada location and one office in Colo, Iowa. It has a strong presence in agricultural, commercial and residential real estate lending.

As of December 31, 2010, State Bank had capital of $14,144,000 and 24 full-time equivalent employees. State Bank had net income for the years ended December 31, 2010, 2009 and 2008 of approximately $2,465,000, $1,462,000 and $1,738,000, respectively. Total assets as of December 31, 2010, 2009 and 2008 were approximately $135,695,000, $134,947,000 and $121,792,000, respectively.

Boone Bank & Trust Co., Boone, Iowa. Boone Bank is an Iowa, state-chartered, FDIC insured commercial bank. Boone Bank was organized in 1992 by the Company under a new state charter in connection with a purchase and assumption transaction whereby Boone Bank purchased certain assets and assumed certain liabilities of the former Boone State Bank & Trust Company in exchange for a cash payment. It provides full service banking to businesses and residents within the Boone community and surrounding area. It is actively engaged in agricultural, consumer and commercial lending, including real estate, operating and equipment loans. It conducts business from its main office and a full service office, both located in Boone.

4

Table of Contents

As of December 31, 2010, Boone Bank had capital of $12,968,000 and 27 full-time equivalent employees. Boone Bank had net income for the years ended December 31, 2010, 2009 and 2008 of approximately $1,736,000, $1,473,000 and $1,406,000, respectively. Total assets as of December 31, 2010, 2009 and 2008 were approximately $105,089,000, $104,957,000 and $101,882,000, respectively.

Randall-Story State Bank, Story City, Iowa. Randall-Story Bank is an Iowa, state-chartered, FDIC insured commercial bank. Randall-Story Bank was acquired by the Company in 1995 through a stock transaction whereby the then shareholders of Randall-Story Bank exchanged all their Randall-Story Bank stock for stock in the Company. Randall-Story Bank was organized in 1928 and provides full-service banking to Story City and the surrounding area. While its primary emphasis is in agricultural lending, Randall-Story Bank also provides the traditional lending services typically offered by community banks.

As of December 31, 2010, Randall-Story Bank had capital of $8,809,000 and 13 full-time equivalent employees. Randall-Story Bank had net income for the years ended December 31, 2010, 2009 and 2008 of approximately $1,144,000, $888,000 and $831,000, respectively. Total assets as of December 31, 2010, 2009 and 2008 were approximately $85,062,000, $79,497,000 and $78,199,000, respectively.

United Bank & Trust NA, Marshalltown, Iowa. United Bank is a nationally-chartered, commercial bank insured by the FDIC. It was newly chartered in June of 2002 and offers a broad range of deposit and loan products, as well as trust services to customers located in the Marshalltown and surrounding Marshall County area.

As of December 31, 2010, United Bank had capital of $10,653,000 and 22 full-time equivalent employees. United Bank had net income (loss) for the years ended December 31, 2010, 2009 and 2008 of approximately $1,205,000, $387,000 and $(87,000), respectively. Total assets as of December 31, 2010, 2009 and 2008 were approximately $106,819,000, $112,441,000 and $99,441,000, respectively.

Business Strategy and Operations

As a locally owned, multi-bank holding company for five community banks, the Company emphasizes strong personal relationships to provide products and services that meet the needs of the Banks' customers. The Company seeks to achieve growth and maintain a strong return on equity. To accomplish these goals, the Banks focus on small-to-medium size businesses that traditionally wish to develop an exclusive relationship with a single bank. The Banks, individually and collectively, have the size to give the personal attention required by business owners, in addition to the credit expertise to help businesses meet their goals.

Table of Contents

The Banks offer a full range of deposit services that are typically available in most financial institutions, including checking accounts, savings accounts and time deposits of various types, ranging from money market accounts to longer-term certificates of deposit. One major goal in developing the Banks' product mix is to keep the product offerings as simple as possible, both in terms of the number of products and the features and benefits of the individual services. The transaction accounts and time certificates are tailored to each Bank's principal market area at rates competitive in that Bank's market. In addition, retirement accounts such as IRAs (Individual Retirement Accounts) are available. The FDIC insures all deposit accounts up to the maximum amount. The Banks solicit these accounts from small-to-medium sized businesses in their respective primary trade areas, and from individuals who live and/or work within these areas. No material portion of the Banks' deposits has been obtained from a single person or from a few persons. Therefore, the Company does not believe that the loss of the deposits of any person or of a few persons would have an adverse effect on the Banks' operations or erode their deposit base.

Loans are provided to creditworthy borrowers regardless of their race, color, national origin, religion, sex, age, marital status, disability, receipt of public assistance or any other basis prohibited by law. The Banks intend to fulfill this commitment while maintaining prudent credit standards. In the course of fulfilling this obligation to meet the credit needs of the communities which they serve, the Banks give consideration to each credit application regardless of the fact that the applicant may reside in a low to moderate income neighborhood, and without regard to the geographic location of the residence, property or business within their market areas.

The Banks provide innovative, quality financial products, such as Internet banking and trust services that meet the banking needs of their customers and communities. The loan programs and acceptance of certain loans may vary from time-to-time depending on the funds available and regulations governing the banking industry. The Banks offer all basic types of credit to their local communities and surrounding rural areas, including commercial, agricultural and consumer loans. The types of loans within these categories are as follows:

Commercial Loans. Commercial loans are typically made to sole proprietors, partnerships, corporations and other business entities such as municipalities where the loan is to be used primarily for business purposes. These loans are typically secured by assets owned by the borrower and often times involve personal guarantees given by the owners of the business. The types of loans the Banks offer include:

- financing guaranteed under Small Business Administration programs
- operating and working capital loans
- loans to finance equipment and other capital purchases
- commercial real estate loans
- business lines of credit
- term loans
- loans to professionals
- letters of credit

Agricultural Loans. The Banks, by nature of their location in central Iowa, are directly and indirectly involved in agriculture and agri-business lending. This includes short-term seasonal lending associated with cyclical crop and livestock production, intermediate term lending for machinery, equipment and breeding stock acquisition and long-term real estate lending. These loans are typically secured by the crops, livestock, equipment or real estate being financed. The basic tenet of the Banks' agricultural lending philosophy is a blending of strong, positive cash flow supported by an adequate collateral position, along with a demonstrated capacity to withstand short-term negative impact if necessary. Applicable governmental subsidies and affiliated programs are utilized if warranted to accomplish these parameters. Approximately 18% of the loan portfolio consists of loans made for agricultural purposes.

6

Table of Contents

Consumer Loans. Consumer loans are typically available to finance home improvements and consumer purchases, such as automobiles, household furnishings and boats. These loans are made on both a secured and an unsecured basis. The following types of consumer loans are available:

- automobiles and trucks
- boats and recreational vehicles
- personal loans and lines of credit
- home equity lines of credit
- home improvement and rehabilitation loans
- consumer real estate loans

Other types of credit programs, such as loans to nonprofit organizations, to public entities, for community development and to other governmental programs also are available.

First National, Boone Bank, State Bank and United Bank offer trust services typically found in a commercial bank with trust powers, including the administration of estates, conservatorships, personal and corporate trusts and agency accounts. The Banks also provide farm management, investment and custodial services for individuals, businesses and non-profit organizations.

The Banks earn income from the origination of residential mortgages that are sold in the secondary real estate market without retaining the mortgage servicing rights.

The Banks offer traditional banking services, such as safe deposit boxes, wire transfers, direct deposit of payroll and social security checks, automated teller machine access and automatic drafts (ACH) for various accounts.

Credit Management

The Company strives to achieve sound credit risk management. In order to achieve this goal, the Company has established uniform credit policies and underwriting criteria for the Banks' loan portfolios. The Banks diversify in the types of loans offered and are subject to regular credit examinations, annual internal and external loan audits and annual review of large loans, as well as quarterly reviews of loans experiencing deterioration in credit quality. The Company attempts to identify potential problem loans early, charge off loans promptly and maintain an adequate allowance for loan losses. The Company has established credit guidelines for the Banks' lending portfolios which include guidelines relating to the more commonly requested loan types, as follows:

Commercial Real Estate Loans - Commercial real estate loans, including agricultural real estate loans, are normally based on loan to appraisal value ratios of not to exceed 80% and secured by a first priority lien position. Loans are typically subject to interest rate adjustments no less frequently than 5 years from origination. Fully amortized monthly repayment terms normally do not exceed twenty years. Projections and cash flows that show ability to service debt within the amortization period are required. Property and casualty insurance is required to protect the Banks' collateral interests. Commercial and agricultural real estate loans represent approximately 44% of the loan portfolio. Major risk factors for commercial real estate loans, as well as the other loan types described below, include a geographic concentration in central Iowa; the dependence of the local economy upon several large governmental entities, including Iowa State University and the Iowa Department of Transportation; and the health of Iowa's agricultural sector that is dependent on weather conditions and government programs.

Table of Contents

Commercial and Agricultural Operating Lines - These loans are made to businesses and farm operations with terms up to twelve months. The credit needs are generally seasonal with the source of repayment coming from the entity's normal business cycle. Cash flow reviews are completed to establish the ability to service the debt within the terms of the loan. A first priority lien on the general assets of the business normally secures these types of loans. Loan to value limits vary and are dependent upon the nature and type of the underlying collateral and the financial strength of the borrower. Crop and hail insurance is required for most agricultural borrowers. Loans are generally guaranteed by the principal(s).

Commercial and Agricultural Term Loans – These loans are made to businesses and farm operations to finance equipment, breeding stock and other capital expenditures. Terms are generally the lesser of five years or the useful life of the asset. Term loans are normally secured by the asset being financed and are often additionally secured with the general assets of the business. Loan to value is generally 75% of the cost or value of the assets. Loans are normally guaranteed by the principal(s). Commercial and agricultural operating and term loans represent approximately 29% of the loan portfolio.

Residential First Mortgage Loans – Proceeds of these loans are used to buy or refinance the purchase of residential real estate with the loan secured by a first lien on the real estate. Most of the residential mortgage loans originated by the Banks (including servicing rights) are sold in the secondary mortgage market due to the higher interest rate risk inherent in the 15 and 30 year fixed rate terms consumers prefer. Loans that are originated and not sold in the secondary market generally have higher interest rates and have rate adjustment periods of no longer than seven years. The maximum amortization of first mortgage residential real estate loans is 30 years. The loan-to-value ratios normally do not exceed 80% without credit enhancements such as mortgage insurance. Property insurance is required on all loans to protect the Banks' collateral position. Loans secured by one to four family residential properties represent approximately 22% of the loan portfolio.

Home Equity Term Loans – These loans are normally for the purpose of home improvement or other consumer purposes and are secured by a junior mortgage on residential real estate. Loan-to-value ratios normally do not exceed 90% of market value.

Home Equity Lines of Credit - The Banks offer a home equity line of credit generally with a maximum term of 60 months. These loans are secured by a junior mortgage on the residential real estate and normally do not exceed a loan-to-market value ratio of 90% with the interest adjusted quarterly.

Consumer Loans – Consumer loans are normally made to consumers under the following guidelines. Automobiles - loans on new and used automobiles generally will not exceed 90% and 75% of the value, respectively. Recreational vehicles and boats – 90% and 66% of the value, respectively. Mobile home - maximum term on these loans is 180 months with the loan-to-value ratio generally not exceeding 66%. Each of these loans is secured by a first priority lien on the assets and requires insurance to protect the Banks' collateral position. Unsecured - The term for unsecured loans generally does not exceed 12 months. Consumer and other loans represent approximately 5% of the loan portfolio.

Table of Contents

Employees

At December 31, 2010, the Banks had a total of 176 full-time equivalent employees and the Company had an additional 11 full-time employees. The Company and Banks provide their employees with a comprehensive program of benefits, including comprehensive medical and dental plans, long-term and short-term disability coverage, and a 401(k) profit sharing plan. Management considers its relations with employees to be satisfactory. Unions represent none of the employees.

Market Area

The Company operates five commercial banks with locations in Story, Boone, Polk and Marshall Counties in central Iowa.

First National is located in Ames, Iowa with a population of 58,965. The major employers are Iowa State University, Ames Laboratories, Iowa Department of Transportation, Mary Greeley Medical Center, Ames Community Schools, City of Ames, Sauer-Danfoss and McFarland Clinic. First National's primary business includes providing retail banking services and business and consumer lending. First National has a minimum exposure to agricultural lending.

Boone Bank is located in Boone, Iowa with a population of 12,661. Boone is the county seat of Boone County. The major employers are Fareway Stores, Inc., Iowa National Guard, Union Pacific Railroad, Boone County Hospital and Communication Data Services. Boone Bank provides lending services to the agriculture, commercial and real estate markets.

State Bank is located in Nevada, Iowa with a population of 6,798. Nevada is the county seat of Story County. The major employers are Print Graphics, General Financial Supply, Mid-American Manufacturing, Mid-States Millwright & Builders, Inc., Burke Corporation and Almaco. State Bank provides various types of loans with a major agricultural presence. It provides a wide variety of banking services including trust, deposit, ATM, and merchant card processing.

Randall-Story Bank is located in Story City, Iowa with a population of 3,431. The major employers are Bethany Manor, American Packaging, M.H. Eby, Inc. and Record Printing. Located in a major agricultural area, it has a strong presence in this type of lending. As a full service commercial bank, it provides a full line of products and services.

United Bank is located in Marshalltown, Iowa with a population of 27,552. The major employers are Iowa Veterans Home, Marshalltown School District, JBS Swift & Co., Emerson Process Management/Fisher Division, Lennox Industries and Marshalltown Medical & Surgical Center. The Bank offers a full line of loan, deposit, and trust services. Loan services include primarily commercial and consumer types of credit including operating lines, equipment loans, automobile financing and real estate loans.

Table of Contents

Competition

The geographic market area served by the Banks is highly competitive with respect to both loans and deposits. The Banks compete principally with other commercial banks, savings and loan associations, credit unions, mortgage companies, finance divisions of auto and farm equipment companies, agricultural suppliers and other financial service providers. Some of these competitors are local, while others are statewide or nationwide. The major commercial bank competitors include Great Western Bank, U.S. Bank National Association and Wells Fargo Bank, each of which have a branch office or offices within the Banks' primary trade areas. Among the advantages such larger banks have are their ability to finance extensive advertising campaigns and to allocate their investment assets to geographic regions of higher yield and demand. These larger banking organizations have much higher legal lending limits than the Banks and thus are better able to finance large regional, national and global commercial customers.

In order to compete with the other financial institutions in their primary trade areas, the Banks use, to the fullest extent possible, the flexibility which is accorded by independent status. This includes an emphasis on specialized services, local promotional activity and personal contacts by the Banks' officers, directors and employees. In particular, the Banks compete for deposits principally by offering depositors a wide variety of deposit programs, convenient office locations, hours and other services. The Banks compete for loans primarily by offering competitive interest rates, experienced lending personnel and quality products and services.

As of December 31, 2010, there were 36 FDIC insured institutions having approximately 89 offices or branch offices within Boone, Story, Polk and Marshall County, Iowa where the Banks' offices are primarily located. First National, State Bank and Randall-Story Bank together have the largest percentage of deposits in Story County.

The Banks also compete with the financial markets for funds. Yields on corporate and government debt securities and commercial paper affect the ability of commercial banks to attract and hold deposits. Commercial banks also compete for funds with equity, money market, and insurance products offered by brokerage and insurance companies. This competitive trend will likely continue in the future.

The Company anticipates bank competition will continue to change materially over the next several years as more financial institutions, including the major regional and national banks, continue to consolidate. Credit unions, which are not subject to income taxes, have a significant competitive advantage and provide additional competition in the Company's local markets.

Supervision and Regulation

The following discussion generally refers to certain statutes and regulations affecting the banking industry. These references provide brief summaries and therefore do not purport to be complete and are qualified in their entirety by reference to those statutes and regulations. In addition, due to the numerous statutes and regulations that apply to and regulate the banking industry, many are not referenced below.

Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("the Dodd-Frank Act"). In response to the current national and international economic recession and to strengthen supervision of financial institutions and systemically important nonbank financial institutions, Congress and the U.S. government have taken a variety of actions, including the enactment of the Dodd-Frank Act on July 21, 2010. The Dodd-Frank Act represents the most comprehensive change to banking laws since the Great Depression of the 1930s and mandates changes in several key areas: regulation and compliance (both with respect to financial institutions and systemically important nonbank financial companies), securities regulation, executive compensation, regulation of derivatives, corporate governance, transactions with affiliates, deposit insurance assessments and consumer protection. While the changes in the law required by the Dodd-Frank Act will most significantly have a major impact on large institutions, even relatively

small institutions such as the Company will be affected.

Table of Contents

Pursuant to the Dodd-Frank Act, the Banks will be subject to regulations promulgated by a new consumer protection bureau housed within the Federal Reserve, known as the Bureau of Consumer Financial Protection (the "Bureau" or "BCFP"). The Bureau will promulgate rules and orders with respect to consumer financial products and services and will have substantial power to define the rights of consumers and responsibilities of lending institutions, such as the Banks. The Bureau will not, however, examine or supervise the Banks for compliance with such regulations; rather, enforcement authority will remain with the Banks' primary federal regulator although the Banks may be required to submit reports or other materials to the Bureau upon its request. The date upon which the Bureau will begin to exercise its authority has been designated by the Secretary of the Treasury as July 21, 2011.

The Dodd-Frank Act also included a provision that supplements the Federal Trade Commission Act's (the "FTC Act") prohibitions against practices that are unfair or deceptive by also prohibiting practices that are "abusive." This term has not yet been defined by implementing regulations but, once it is defined, the Banks will be required to evaluate all of their consumer financial products and services to ensure they are in compliance with this provision.

In addition, the Dodd-Frank Act requires the Company and Banks to: (1) be subject to a new assessment model from the FDIC based upon assets, not deposits (as described herein) and (2) be subject to enhanced executive compensation and corporate governance requirements.

The Dodd-Frank Act also lifts the prohibition on paying interest on demand deposits effective July 21, 2011. This may change the nature of some of the products and services that financial institutions have traditionally used, such as earnings credits.

The extent to which the new legislation and existing and planned governmental initiatives thereunder will succeed in ameliorating tight credit conditions or otherwise result in an improvement in the national economy is uncertain. In addition, because most of the component parts of the Dodd-Frank Act will be subject to intensive agency rulemaking and subsequent public comment over the next several months, it is difficult to predict the ultimate effect of the Dodd-Frank Act on the Company or the Banks at this time. Operational expenses of the Company may increase as a result of new compliance requirements.

Emergency Economic Stabilization Act of 2008. On October 3, 2008, President Bush signed into law the Emergency Economic Stabilization Act of 2008 ("EESA"), giving the US Treasury authority to take certain actions to restore liquidity and stability to the U.S. banking markets. Based upon the authority contained in the EESA, a number of programs to implement the EESA have been established. Those programs include the following:

Capital Purchase Program ("CPP"). Pursuant to this program, the US Treasury, on behalf of the US government, will purchase up to $250 billion of preferred stock, along with warrants to purchase common stock, from certain financial institutions, including bank holding companies, savings and loan holding companies and banks or savings associations not controlled by a holding company. On publically traded financial institutions, the investment will have a dividend rate of 5% per year, until the fifth anniversary of the US Treasury's investment and a dividend of 9% thereafter. The Company did not participate in the CCP program.

Table of Contents

Temporary Liquidity Guarantee Program ("TLGP"). This program contains both a debt guarantee component, whereby the FDIC will guarantee until June 30, 2012, the senior unsecured debt issued by eligible financial institutions between October 14, 2008 and June 30, 2009, and an account transaction guarantee component, whereby the FDIC will insure 100% of non-interest bearing deposit transaction accounts held at eligible financial institutions, such as payment processing accounts, payroll accounts and working capital accounts, through June 30, 2010. The Banks have opted out of the debt guarantee component and opted into the transaction guarantee component of this program. Importantly, however, the Dodd-Frank Act requires all insured financial institutions, such as the Banks, to provide such products with FDIC insurance from December 31, 2010 until December 31, 2012. This protection will also apply to interest-bearing NOW accounts or Interest on Lawyers Trust Accounts. The FDIC has not stated that deposit insurance premiums will increase because of the provision.

Given the current international, national and regional economic climate, it is unclear what effect the provisions of the EESA will have with respect to the profitability and operations of both the Company and the Banks. In addition, the US government, either through the US Treasury or some other federal agency, may also advance additional programs that could materially impact the profitability and operations of both the Company and the Banks. The failure of these governmental efforts to stabilize national and international markets could have a material effect on the Company's business, financial condition, results of operations or access to the credit markets.

Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (the "S.A.F.E. Act") Requirements. The S.A.F.E. Act and related rules require residential mortgage loan originators who are employees of regulated financial institutions, such as the Banks, to be registered with the Nationwide Mortgage Licensing System and Registry, a database created by the Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators to support the licensing of mortgage loan originators by the states. Employees of regulated financial institutions are generally prohibited from originating residential mortgage loans unless they are registered. According to the final rule, due to various system modifications and enhancements required to make the existing system capable to accept federal registrants, the system is not expected to be available to accept federal registrants before January 2011. Individuals and institutions will be directed on how to proceed by the appropriate agency.

USA Patriot Act. The USA Patriot Act was enacted in 2001 which, together with regulations issued pursuant to this act, substantially broadened previously existing anti-money laundering laws and regulations, increased compliance, due diligence and reporting obligations for financial institutions, created new crimes and penalties and required federal banking agencies, in reviewing mergers and other acquisition transactions, to consider the effectiveness of the parties in combating money laundering activities. The act requires all financial institutions to establish certain anti-money laundering compliance and due diligence programs that are reasonably designed to detect and report instances of money laundering. The Company believes its compliance policies, procedures and controls satisfy the material requirements of the Patriot Act and regulations.

Table of Contents

Sarbanes-Oxley Act. The Sarbanes-Oxley Act was enacted in 2002 to, among other things, increase corporate responsibility and to protect investors by improving the accuracy and reliability of corporate disclosures pursuant to the federal securities laws. This act generally applies to all companies that are required to file periodic reports with the Securities and Exchange Commission under the Securities Exchange Act of 1934. The act implements significant changes in the responsibilities of officers and directors of public companies and makes certain changes to the corporate reporting obligation of those companies and their external auditors. Among the requirements and prohibitions addressed by the act are certifications required by CEOs and CFOs of periodic reports filed with the SEC; accelerated reporting of stock transactions by directors, officers and large shareholders; prohibitions against personal loans from companies to directors and executive officers (except loans made in the ordinary course of business); requirements for public companies' audit committees; requirements for auditor independence; the forfeiture of bonuses or other incentive-based compensation and profits from the sale of an issuer's securities by directors and executive officers in the 12-month period following initial publication of any financial statements that later require restatement; various increased criminal penalties for violations of securities laws; and the creation of a public company accounting oversight board. Rules adopted by the SEC to implement various provisions of the act include CEO and CFO certifications related to fair presentation of financial statements and financial information in public filings, as well as management's evaluation of disclosure controls and procedures; disclosure of whether any audit committee members qualify as a "financial expert"; disclosures related to audit committee composition and auditor pre-approval policies; disclosure related to adoption of a written code of ethics; reconciling non-GAAP financial information with GAAP in public communications; disclosure of off-balance sheet transactions; and disclosure related to director independence and the director nomination process. The Company has adopted modifications to its corporate governance procedures to comply with the provisions of the act and regulations.

Incentive Compensation Regulation. The regulators issued on June 21, 2010 final guidance to ensure that incentive compensation arrangements at financial institutions take into account risk and are consistent with safe and sound banking practices. The guidance was designed to ensure that incentive compensation arrangements appropriately tie rewards to longer-term performance and do not undermine the safety and soundness of the entity or create undue risks to the financial system. As a result of this guidance, the Company and the Banks will incorporate the risks related to incentive compensation into their broader risk-management framework.

The Company and the Banks are subject to extensive federal and state regulation and supervision. Regulation and supervision of financial institutions is primarily intended to protect depositors and the FDIC rather than shareholders of the Company. The laws and regulations affecting banks and bank holding companies have changed significantly over recent years, particularly with the passage of the Financial Services Modernization Act. There is reason to expect that similar changes will continue in the future. Any change in applicable laws, regulations or regulatory policies may have a material effect on the business, operations and prospects of the Company. The Company is unable to predict the nature or the extent of the effects on its business and earnings that any fiscal or monetary policies or new federal or state legislation may have in the future.

Table of Contents

The Company

The Company is a bank holding company by virtue of its ownership of the Banks, and is registered as such with the Board of Governors of the Federal Reserve System (the "Federal Reserve"). The Company is subject to regulation under the Bank Holding Company Act of 1956, as amended (the "BHCA"), which subjects the Company and the Banks to supervision and examination by the Federal Reserve. Under the BHCA, the Company files with the Federal Reserve annual reports of its operations and such additional information as the Federal Reserve may require.

Source of Strength to the Banks. The Federal Reserve takes the position that a bank holding company is required to serve as a source of financial and managerial strength to its subsidiary banks and may not conduct its operations in an unsafe or unsound manner. In addition, it is the Federal Reserve's position that in serving as a source of strength to its subsidiary banks, bank holding companies should use available resources to provide adequate capital funds to its subsidiary banks during periods of financial stress or adversity. It should also maintain the financial flexibility and capital raising capacity to obtain additional resources for providing assistance to its subsidiary banks. A bank holding company's failure to meet its obligations to serve as a source of strength to its subsidiary banks will generally be considered by the Federal Reserve to be an unsafe and unsound banking practice, or a violation of the Federal Reserve's regulations, or both.

Federal Reserve Approval. Bank holding companies must obtain the approval of the Federal Reserve before they: (i) acquire direct or indirect ownership or control of any voting stock of any bank if, after such acquisition, they would own or control, directly or indirectly, more than 5% of the voting stock of such bank; (ii) merge or consolidate with another bank holding company; or (iii) acquire substantially all of the assets of any additional banks.

Non-Banking Activities. With certain exceptions, the BHCA also prohibits bank holding companies from acquiring direct or indirect ownership or control of voting stock in any company other than a bank or a bank holding company unless the Federal Reserve finds the company's business to be incidental to the business of banking. When making this determination, the Federal Reserve in part considers whether allowing a bank holding company to engage in those activities would offer advantages to the public that would outweigh possible adverse effects. A bank holding company may engage in permissible non-banking activities on a de novo basis, if the holding company meets certain criteria and notifies the Federal Reserve within ten (10) business days after the activity has commenced.

Under the Financial Services Modernization Act, eligible bank holding companies may elect (with the approval of the Federal Reserve) to become a "financial holding company." Financial holding companies are permitted to engage in certain financial activities through affiliates that had previously been prohibited activities for bank holding companies. Such financial activities include securities and insurance underwriting and merchant banking. At this time, the Company has not elected to become a financial holding company, but may choose to do so at some time in the future.

Control Transactions. The Change in Bank Control Act of 1978, as amended, requires a person or group of persons acquiring "control" of a bank holding company to provide the Federal Reserve with at least 60 days prior written notice of the proposed acquisition. Following receipt of this notice, the Federal Reserve has 60 days to issue a notice disapproving the proposed acquisition, but the Federal Reserve may extend this time period for up to another 30 days. An acquisition may be completed before the disapproval period expires if the Federal Reserve issues written notice of its intent not to disapprove the action. Under a rebuttable presumption established by the Federal Reserve, the acquisition of 10% or more of a class of voting stock of a bank holding company with a class of securities registered under Section 12 of the Securities Exchange Act of 1934, as amended, would constitute the acquisition of control. In addition, any "company" would be required to obtain the approval of the Federal Reserve under the BHCA before acquiring 25% (or 5% if the "company" is a bank holding company) or more of the outstanding shares of the Company, or otherwise obtain control over the Company.

Table of Contents

Affiliate Transactions. The Company and the Banks are deemed affiliates within the meaning of the Federal Reserve Act, and transactions between affiliates are subject to certain restrictions. Generally, the Federal Reserve Act: (i) limits the extent to which the financial institution or its subsidiaries may engage in "covered transactions" with an affiliate; and (ii) requires all transactions with an affiliate, whether or not "covered transactions," to be on terms substantially the same, or at least as favorable to the institution or subsidiary, as those provided to a non-affiliate. The term "covered transaction" includes the making of loans, purchase of assets, issuance of a guarantee and similar transactions.

State Law on Acquisitions. Iowa law permits bank holding companies to make acquisitions throughout the state. However, Iowa currently has a deposit concentration limit of 15% on the amount of deposits in the state that any one banking organization can control and continue to acquire banks or bank deposits (by acquisitions), which applies to all depository institutions doing business in Iowa.

Banking Subsidiaries

Applicable federal and state statutes and regulations governing a bank's operations relate, among other matters, to capital adequacy requirements, required reserves against deposits, investments, loans, legal lending limits, certain interest rates payable, mergers and consolidations, borrowings, issuance of securities, payment of dividends, establishment of branches and dealings with affiliated persons.

First National and United Bank are national banks subject to primary federal regulation and supervision by the OCC. The FDIC, as an insurer of the deposits, also has some limited regulatory authority over First National and United Bank. State Bank, Boone Bank and Randall-Story Bank are state banks subject to regulation and supervision by the Iowa Division of Banking. The three state Banks are also subject to regulation and examination by the FDIC, which insures their respective deposits to the maximum extent permitted by law. The federal laws that apply to the Banks regulate, among other things, the scope of their business, their investments, their reserves against deposits, the timing of the availability of deposited funds and the nature and amount of and collateral for loans. The laws and regulations governing the Banks generally have been promulgated to protect depositors and the deposit insurance fund of the FDIC and not to protect stockholders of such institutions or their holding companies.

The OCC and FDIC each have authority to prohibit banks under their supervision from engaging in what it considers to be an unsafe and unsound practice in conducting their business. The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") requires federal banking regulators to adopt regulations or guidelines in a number of areas to ensure bank safety and soundness, including internal controls, credit underwriting, asset growth, management compensation, ratios of classified assets to capital and earnings. FDICIA also contains provisions which are intended to change independent auditing requirements, restrict the activities of state-chartered insured banks, amend various consumer banking laws, limit the ability of "undercapitalized banks" to borrow from the Federal Reserve's discount window, require regulators to perform periodic on-site bank examinations and set standards for real estate lending.

Table of Contents

Borrowing Limitations. Each of the Banks is subject to limitations on the aggregate amount of loans that it can make to any one borrower, including related entities. Subject to numerous exceptions based on the type of loans and collateral, applicable statutes and regulations generally limit loans to one borrower of 15% of total equity and reserves. Each of the Banks is in compliance with applicable loans to one borrower requirements.

FDIC Insurance. Under the Dodd-Frank Act, a permanent increase in deposit insurance was authorized to $250,000 (insurance coverage had previously been temporarily raised to that level until December 13, 2013). The coverage limit is per depositor, per insured depository institution for each account ownership category. The FDIC has adopted a risk-based insurance assessment system under which depository institutions contribute funds to the FDIC insurance fund based on their risk classification. The FDIC may terminate the deposit insurance of any insured depository institution if it determines after an administrative hearing that the institution has engaged or is engaging in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law.

The FDIC imposes an assessment against all depository institutions for deposit insurance. This assessment is based on the risk category of the institution and, prior to 2009, ranged from five to 43 basis points of the institution's deposits. The FDIC issued a final rule on December 22, 2008, that raised the current deposit insurance assessment rates uniformly by seven basis points (to a range from 12 to 50 basis points) effective for the first quarter 2009. On February 27, 2009, the FDIC issued a final rule that changed the calculation of FDIC insurance rates beginning in the second quarter of 2009. Under this rule, the FDIC first establishes an institution's initial base assessment rate. This initial base assessment rate ranges, depending on the risk category of the institution, from 12 to 45 basis points. The FDIC then adjusts the initial base assessment (higher or lower) to obtain the total base assessment rate. The adjustment to the initial base assessment rate is based upon an institution's levels of unsecured debt, secured liabilities, and brokered deposits. The total base assessment rate currently ranges from 7 to 77.5 basis points of the institution's deposits. The FDIC issued a final rule on February 7, 2011, effective April 1, 2011, that redefines the deposit insurance assessment base as average consolidated total assets minus average tangible equity and adopts a new assessment rate schedule effective April 1, 2011. The total base assessment rate beginning on April 1, 2011 will range from 2.5 to 45 basis points based upon an institutions risk category. Calculated assessment rates are based upon an institution's assessment base.

The FDIC announced on November 12, 2009, that insured depository institutions were required to prepay three years of deposit insurance premiums on December 30, 2009. Under the rule, the prepaid amount was based on an estimate of the institution's assessment rate in effect on September 30, 2009, its third quarter 2009 assessment base, and an estimated rate of increase in that assessment base.

The Dodd-Frank Act also set a new minimum Deposit Insurance fund ("DIF") reserve ratio at 1.35% of estimated insured deposits. The Board of Directors of the FDIC on December 14, 2010 issued a final rule to set the insurance fund's designated reserve ratio (DRR) at 2.00% of estimated insured deposits. The FDIC is required to attain this ratio by September 30, 2020. In addition, the Dodd-Frank Act will have a significant impact on the calculation of deposit insurance assessment premiums going forward. Specifically, the Dodd-Frank Act generally requires the FDIC to define the deposit insurance assessment base for an insured depository institution as an amount equal to the institution's average consolidated total assets during the assessment period minus average tangible equity. The FDIC has issued a proposed rulemaking that implements this change to the assessment calculation but has said that the new assessment rate schedule should result in the collection of assessment revenue that is approximately revenue neutral even though the new assessment base under Dodd-Frank Act is larger than the current assessment base. Because of this change, the new proposed assessment rates are lower than current rates and range generally from 2.5 basis points to 45 basis points. Notably, there is a separate insurance assessment rate schedule that has been proposed for larger institutions (i.e., institutions with at least $10 billion in assets).

16

Table of Contents

The proposed FDIC rules also provide the FDIC's board with the flexibility to adopt actual rates that are higher or lower than the total base assessment rates adopted without notice and comment if certain restrictions are met.

Capital Adequacy Requirements. The Federal Reserve, the FDIC and the OCC (collectively, the "Agencies") have adopted risk-based capital guidelines for banks and bank holding companies that are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks and bank holding companies and account for off-balance sheet items. Failure to achieve and maintain adequate capital levels may give rise to supervisory action through the issuance of a capital directive to ensure the maintenance of required capital levels. Each of the Banks is in compliance with applicable risk-based capital level requirements as of December 31, 2010.

The current guidelines require all federally regulated banks to maintain a minimum risk-based total capital ratio equal to 8%, of which at least 4% must be Tier 1 capital. Tier 1 capital includes common shareholders' equity, qualifying perpetual preferred stock and minority interests in equity accounts of consolidated subsidiaries, but excludes goodwill and most other intangibles and the allowance for loan and lease losses. Tier 2 capital includes the excess of any preferred stock not included in Tier 1 capital, mandatory convertible securities, hybrid capital instruments, subordinated debt and intermediate term preferred stock, 45% of unrealized gain of equity securities and general reserve for loan and lease losses up to 1.25% of risk weighted assets.

Under these guidelines, banks' assets are given risk weights of 0%, 20%, 50% or 100%. Most loans are assigned to the 100% risk category, except for first mortgage loans fully secured by residential property and, under certain circumstances, residential construction loans (both carry a 50% rating). Most investment securities are assigned to the 20% category, except for municipal or state revenue bonds (which have a 50% rating) and direct obligations of or obligations guaranteed by the United States Treasury or United States Government Agencies (which have a 0% rating).

The Agencies have also implemented a leverage ratio, which is equal to Tier 1 capital as a percentage of average total assets less intangibles, to be used as a supplement to the risk based guidelines. The principal objective of the leverage ratio is to limit the maximum degree to which a bank may leverage its equity capital base. The minimum required leverage ratio for top rated institutions is 3%, but most institutions are required to maintain an additional cushion of at least 100 to 200 basis points. Any institution operating at or near the 3% level is expected to be a strong banking organization without any supervisory, financial or operational weaknesses or deficiencies. Any institutions experiencing or anticipating significant growth would be expected to maintain capital ratios, including tangible capital positions, well above the minimum levels.

Table of Contents

Prompt Corrective Action. Regulations adopted by the Agencies impose even more stringent capital requirements. The FDIC and other Agencies must take certain "prompt corrective action" when a bank fails to meet capital requirements. The regulations establish and define five capital levels: (i) "well-capitalized," (ii) "adequately capitalized," (iii) "undercapitalized," (iv) "significantly undercapitalized" and (v) "critically undercapitalized." Increasingly severe restrictions are imposed on the payment of dividends and management fees, asset growth and other aspects of the operations of institutions that fall below the category of being "adequately capitalized". Undercapitalized institutions are required to develop and implement capital plans acceptable to the appropriate federal regulatory agency. Such plans must require that any company that controls the undercapitalized institution must provide certain guarantees that the institution will comply with the plan until it is adequately capitalized. As of December 31, 2010 each of the Banks was categorized as "well capitalized" under regulatory prompt corrective action provisions.

Restrictions on Dividends. The dividends paid to the Company by the Banks are the major source of Company cash flow. Various federal and state statutory provisions limit the amount of dividends banking subsidiaries are permitted to pay to their holding companies without regulatory approval. Federal Reserve policy further limits the circumstances under which bank holding companies may declare dividends. For example, a bank holding company should not continue its existing rate of cash dividends on its common stock unless its net income is sufficient to fully fund each dividend and its prospective rate of earnings retention appears consistent with its capital needs, asset quality and overall financial condition. In addition, the Federal Reserve and the FDIC have issued policy statements which provide that insured banks and bank holding companies should generally pay dividends only out of current operating earnings. Federal and state banking regulators may also restrict the payment of dividends by order.

First National Bank and United Bank, as a national bank, generally may pay dividends, without obtaining the express approval of the OCC, in an amount up to its retained net profits for the preceding two calendar years plus retained net profits up to the date of any dividend declaration in the current calendar year. Retained net profits as defined by the OCC, consists of net income less dividends declared during the period. On March 16, 2009, the OCC informed the Company of the OCC's decision to establish individual minimum capital ratios for First National in excess of the capital ratios that would otherwise be imposed under applicable regulatory standards. The OCC is requiring First National to maintain, on an ongoing basis, Tier 1 Leverage Capital of 9% of Adjusted Total Assets and Total Risk Based Capital of 11% of Risk-Weighted Assets. As of December 31, 2010 and 2009, First National exceeded these requirements. Boone Bank, Randall-Story Bank and State Bank are also restricted under Iowa law to paying dividends only out of their undivided profits. Additionally, the payment of dividends by the Banks is affected by the requirement to maintain adequate capital pursuant to applicable capital adequacy guidelines and regulations, and the Banks generally are prohibited from paying any dividends if, following payment thereof, the Bank would be undercapitalized.

Reserves Against Deposits. The Federal Reserve requires all depository institutions to maintain reserves against their transaction accounts (primarily checking accounts) and non-personal time deposits. Generally, reserves of 3% must be maintained against total transaction accounts of $55,200,000 or less (subject to an exemption not in excess of the first $10,700,000 of transaction accounts). A reserve of $1,656,000 plus 10% of amounts in excess of $55,200,000 must be maintained in the event total transaction accounts exceed $55,200,000. The balances maintained to meet the reserve requirements imposed by the Federal Reserve may be used to satisfy applicable liquidity requirements. Because required reserves must be maintained in the form of vault cash or a noninterest bearing account at a Federal Reserve Bank, the effect of this reserve requirement is to reduce the earning assets of the Banks.

Table of Contents

Regulatory Enforcement Authority

The enforcement powers available to federal and state banking regulators are substantial and include, among other things, the ability to assess civil monetary penalties, to issue cease-and-desist or removal orders and to initiate injunctive actions against banking organizations and institution-affiliated parties. In general, enforcement actions must be initiated for violations of laws and regulations and unsafe or unsound practices. Other actions, or inactions, may provide the basis for enforcement action, including misleading or untimely reports filed with regulatory authorities. Applicable law also requires public disclosure of final enforcement actions by the federal banking agencies.

National Monetary Policies

In addition to being affected by general economic conditions, the earnings and growth of the Banks are affected by the regulatory authorities' policies, including the Federal Reserve. An important function of the Federal Reserve is to regulate the money supply, credit conditions and interest rates. Among the instruments used to implement these objectives are open market operations in U.S. Government securities, changes in reserve requirements against bank deposits and the Federal Reserve Discount Rate, which is the rate, charged member banks to borrow from the Federal Reserve Bank. These instruments are used in varying combinations to influence overall growth and distribution of credit, bank loans, investments and deposits, and their use may also affect interest rates charged on loans or paid on deposits.

The monetary policies of the Federal Reserve have had a material impact on the operating results of commercial banks in the past and are expected to have a similar impact in the future. Also important in terms of effect on banks are controls on interest rates paid by banks on deposits and types of deposits that may be offered by banks. The Depository Institutions Deregulation Committee, created by Congress in 1980, phased out ceilings on the rate of interest that may be paid on deposits by commercial banks and savings and loan associations, with the result that the differentials between the maximum rates banks and savings and loans can pay on deposit accounts have been eliminated. The effect of deregulation of deposit interest rates has been to increase banks' cost of funds and to make banks more sensitive to fluctuation in market rates.

Availability of Information on Company Website

The Company files periodic reports with the Securities and Exchange Commission ("SEC"), including annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K. The Company makes available on or through its website free of charge all periodic reports filed by the Company with the SEC, including any amendments to such reports, as soon as reasonably practicable after such reports have been electronically filed with the SEC. The address of the Company's website on the Internet is: www.amesnational.com.

The Company will provide a paper copy of these reports free of charge upon written or telephonic request directed to John P. Nelson, Vice President and Secretary, 405 Fifth Street, Ames, Iowa 50010 or (515) 232-6251 or by email request at info@amesnational.com. The information found on the Company's website is not part of this or any other report the Company files with the SEC.

Table of Contents

Executive Officers of Company and Banks

The following table sets forth summary information about the executive officers of the Company and certain executive officers of the Banks. Unless otherwise indicated, each executive officer has served in his current position for the past five years.

Name	Age	Position with the Company or Bank and Principal Occupation and Employment During the Past Five Years
Kathy L. Baker	64	Named President and Director of United Bank on January 1, 2008. Previously served as a Vice President in the lending department of United Bank.
Scott T. Bauer	48	Named President of First National in 2007. Previously served as Executive Vice President and Senior Vice President of First National. Director of First National.
Kevin G. Deardorff	56	Vice President & Technology Director of the Company.
Stephen C. McGill	56	President of State Bank since 2003. Previously served as Senior Vice President of State Bank. Director of State Bank.
John P. Nelson	44	Vice President, Secretary and Treasurer of Company. Director and Chairman of Randall-Story Bank.
Thomas H. Pohlman	60	Named President of the Company in 2007. Previously served as Chief Operating Officer of the Company in 2006 and President of First National from 1999 to 2007. Director of the Company and Director and Chairman of First National, State Bank, Boone Bank and United Bank.
Jeffrey K. Putzier	49	President of Boone Bank since 1999. Director of Boone Bank.
Richard J. Schreier	43	Named President of Randall-Story in May, 2008. Director of Randall-Story. Previously served as Senior Vice President of lending at Randall-Story and State Bank.
Terrill L. Wycoff	67	Executive Vice President of First National since 2000. Director of First National.

ITEM 1A. RISK FACTORS

Set forth below is a description of risk factors related to the Company's business, provided to enable investors to assess, and be appropriately apprised of, certain risks and uncertainties the Company faces in conducting its business. An investor should carefully consider the risks described below and elsewhere in this Report, which could materially and adversely affect the Company's business, results of operations or financial condition. The risks and uncertainties discussed below are also applicable to forward-looking statements contained in this Report and in other reports filed by the Company with the Securities and Exchange Commission. Given these risks and uncertainties, investors are cautioned not to place undue reliance on forward-looking statements.

Table of Contents

General Business, Economic and Political Conditions.

The Company's earnings and financial condition are affected by general business, economic and political conditions. For example, a depressed economic environment increases the likelihood of lower employment levels and recession, which could adversely affect the Company's earnings and financial condition. General business and economic conditions that could affect the Company include short-term and long-term interest rates, inflation, fluctuations in both debt and equity capital markets and the strength of the national and local economies in which the Company operates. Political conditions can also affect the Company's earnings through the introduction of new regulatory schemes and changes in tax laws.

The national and global economic downturn has recently resulted in extreme levels of market volatility locally, nationally and internationally. This downturn has depressed the overall market value of financial institutions, and may limit or impede industry access to capital, or have a material adverse effect on the financial condition or results of operations of banking companies in general, including the Company, with respect to, for example, the establishment of reserves should conditions deteriorate further.

In this respect, while the duration and severity of the adverse economic cycle appears to be lessening at the moment, and although the U.S. Department of the Treasury and the FDIC, among others, have implemented programs in an effort to stabilize the national economy, the ultimate effectiveness of these programs remains uncertain at this time.

The current economic downturn has caused many lending institutions to experience declines in the performance of their loans. The values of real estate collateral supporting mortgage loans have declined and may continue to do so, providing less security for those loans. Across the industry, bank holding companies and bank stock prices have been volatile, as has the ability of banks to raise capital and borrow. Because of the uncertainty and upheaval within the financial markets and industry, there is a potential for new federal and/or state laws and regulations regarding lending, funding and liquidity practices of banks. Any new legislation or regulations could negatively impact the Company's operations.

Individual Minimum Capital Ratios

In March of 2009, the OCC imposed individual minimum capital ratios requiring First National to maintain, on an ongoing basis, Tier One Leverage Capital of 9% of Adjusted Total Assets and Total Risk Based Capital of 11% of Risk Weighted Assets. As of December 31, 2010, First National exceeded these capital ratios. Failure to maintain the individual minimum capital ratios could result in additional regulatory action against First National.

Risks Associated with Loans

A significant source of risk for the Company arises from the possibility that losses will be sustained because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loans. The Company has underwriting and credit monitoring procedures and credit policies, including the establishment and review of the allowance for loan losses, that management believes are appropriate to minimize this risk by assessing the likelihood of nonperformance, tracking loan performance and diversifying the Company's loan portfolio. Such policies and procedures, however, may not prevent unexpected losses that could adversely affect results of operations. During 2010, the Company's allowance for loan losses and its level of impaired loans decreased by $131,000 and $3,755,000, respectively, over 2009 figures. These amounts may increase during 2011, if economic conditions deteriorate, which would adversely impact the Company's borrowers.

Table of Contents

Bank regulatory agencies periodically review the Company's allowance for loan losses and may require an increase in the provision for loan losses, an increase in loans considered to be "impaired" or the recognition of further loan charge-offs, based on current economic conditions. Any increases in the allowance for loan losses will result in a decrease in net income and capital and may have a material adverse effect on the Company's financial condition, results of operations and cash flows.

The Company makes various assumptions and judgments about the collectability of the Company's loan portfolio, including the creditworthiness of the Company's borrowers and the value of the real estate and other assets serving as collateral for the repayment of the Company's loans. Despite the Company's underwriting and monitoring practices, the Company's loan customers may not repay their loans according to their terms, and the collateral securing the payment of these loans may be insufficient to pay any remaining loan balance. The Company may experience significant loan losses, which could have a material adverse effect on its operating results. Because the Company must use assumptions regarding individual loans and the economy, the current allowance for loan losses may not be sufficient to cover actual loan losses, and increases in the allowance may be necessary. The Company may need to significantly increase the Company's provision for losses on loans if one or more of the Company's larger credit relationships becomes delinquent. Material additions to the Company's allowance would materially decrease the Company's net income. The Company cannot provide any assurance that its monitoring procedures and policies will reduce certain lending risks or that the Company's allowance for loan losses will be adequate to cover actual losses.

Other Real Estate Owned

"Other real estate owned" consists of real estate collateral that the Company has received in foreclosure, or accepted in lieu of foreclosure, of impaired loans. The carrying value of the Company's holdings of other real estate owned slightly increased to $10,539,000 as of December 31, 2010 from $10,480,000 as of December 31, 2009, primarily due to foreclosures, offset in part by sales of other real estate owned. Management obtains independent appraisals or performs evaluations to determine that these properties are carried at the lower of the new costs basis or fair value less cost to sell. These independent appraisals or evaluations are performed periodically by management with respect to current and any future other real estate owned, and any subsequent write-downs will be recorded as a charge to operations, if necessary, to reduce the carrying value of a property to the lower of its cost or fair value less cost to sell. Due to potential changes in economic conditions, it is reasonably possible that changes in fair values will occur in the near term and that such changes could materially affect the amounts reported in the Company's financial statements.

Table of Contents

Rising Interest Rates

An increase in interest rates that may occur in connection with the recovery of the economy could negatively impact the Company's net interest margin if interest expense increases more quickly than interest income. The Company's earning assets (primarily its loan and investment portfolio) have longer maturities than its interest bearing liabilities (primarily its deposits and other borrowings). Therefore, in a rising interest rate environment, interest expense will increase more quickly than interest income, as the interest bearing liabilities reprice more quickly than earning assets. In response to this challenge, the Banks model quarterly the changes in income that would result from various changes in interest rates. Management believes Bank earning assets have the appropriate maturity and repricing characteristics to optimize earnings and the Banks' interest rate risk positions.

Liquidity Risk

Maintaining adequate liquidity is essential to the banking business. An inability to raise funds through deposits, borrowing, sale of securities or other sources could have a substantial negative impact on the Company's liquidity. Access to funding sources in amounts necessary to finance the Company's activities or with terms that are acceptable to the Company could be impaired by factors that affect the Company specifically or the financial services industry or economy in general. Factors that could detrimentally impact the Company's access to liquidity sources include a decrease in the level of the Company's business activity as a result of a downturn in the markets or adverse regulatory action against the Company. The Company's ability to borrow could be impaired by factors such as a disruption in the financial markets or negative views and expectations of the prospects for the financial services industry in light of the recent turmoil facing the industry.

Customer Concern over Deposit Insurance

With recent increased concerns about bank failures, customers may be concerned about the extent to which their deposits are insured by the FDIC. Customers may withdraw deposits in an effort to ensure that the amount they have on deposit with their bank is fully insured. Decreases in deposits, if they were to occur, could adversely affect the Company's funding costs and net income.

Concentration of Operations

The Company's operations are concentrated in central Iowa. As a result of this geographic concentration, the Company's results may correlate to the economic conditions in this area, which were adversely impacted by the general decline in economic and market activity experienced during 2010, 2009 and 2008. Continuing deterioration in economic conditions, particularly in the industries on which this area depends (including agriculture which, in turn, is dependent upon weather conditions and government support programs), may adversely affect the quality of the Company's loan portfolio and the demand for the Company's products and services, and accordingly, its financial condition and results of operations.

Table of Contents

Competition with Larger Financial Institutions

The banking and financial services business in the Company's market area continues to be a competitive field and is becoming more competitive as a result of:

- changes in regulations;
- changes in technology and product delivery systems; and
- the accelerating pace of consolidation among financial services providers.

It may be difficult to compete effectively in the Company's market, and results of operations could be adversely affected by the nature or pace of change in competition. The Company competes for loans, deposits and customers with various bank and non-bank financial services providers, many of which are much larger in total assets and capitalization, have greater access to capital markets and offer a broader array of financial services.

Trading Volume

The trading volume in the Company's common stock on the Nasdaq Capital Market is relatively limited compared to those of larger companies listed on the Nasdaq Capital Market, the Nasdaq Global Markets, the New York Stock Exchange or other consolidated reporting systems or stock exchanges. A change in the supply or demand for the Company's common stock may have a more significant impact on the price of the Company's stock than for more actively traded companies.

Technological Advances

The financial services industry is undergoing technological changes with frequent introductions of new technology-driven products and services. In addition to improving customer services, the effective use of technology increases efficiency and enables financial institutions to reduce costs. The Company's future success will depend, in part, on its ability to address the needs of its customers by using technology to provide products and services that will satisfy customer demands for convenience, as well as to create additional efficiencies in the Company's operations. Many of our competitors have substantially greater resources than the Company to invest in technological improvements.

Information Security

The Company depends on data processing, communication and information exchange on a variety of computing platforms and networks and over the internet. The Company cannot be certain all of its systems are entirely free from vulnerability to attack, despite safe guards it has installed. Additionally, the Company relies on and does business with a variety of third-party service providers and vendors with respect to the Company's business, data and communications needs. If information security is breached, or one of the Company's service providers or vendors breaches compliance procedures, information could be lost or misappropriated, resulting in financial loss or costs to the Company or damages to others. If information security is breached, the Company's financial condition, results of operations and future prospects could be adversely affected.

Table of Contents

Government Regulations

Current and future legislation and the policies established by federal and state regulatory authorities will affect the Company's operations. The Company and its Banks are subject to extensive supervision of, and examination by, federal and state regulatory authorities which may limit the Company's growth and the return to our shareholders by restricting certain activities, such as:

- the payment of dividends to the Company's shareholders;
- the payment of dividends to the Company from the Banks;
- possible mergers with or acquisitions of or by other institutions;
- investment policies;
- loans and interest rates on loans;
- interest rates paid on deposits;
- expansion of branch offices; and/or
- the possibility to provide or expand securities or trust services.

On July 21, 2010, the Dodd-Frank Act was signed into law. The Dodd-Frank Act represents a comprehensive overhaul of the financial services industry within the United States and, among many other things, establishes the new federal BCFP, requires the BCFP and other federal agencies to implement over the next six to eighteen months many new and significant rules and regulations. At this time, it is difficult to predict the extent to which the Dodd-Frank Act or the resulting rules and regulations will impact the Company's and the Banks' business. Compliance with the new law and regulations may result in additional costs, which could be significant, and could adversely impact the Company's results of operations, financial condition or liquidity.

The Company cannot predict what changes, if any, will be made to existing federal and state legislation and regulations or the effect that any changes may have on future business and earnings prospects. The cost of compliance with regulatory requirements may adversely affect the Company's net income.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Company's office is housed in the main office of First National located at 405 Fifth Street, Ames, Iowa and occupies approximately 3,400 square feet. A lease agreement between the Company and First National provides the Company will make available for use by First National an equal amount of interior space at the Company's building located at 2330 Lincoln Way, Ames, Iowa in lieu of rental payments. The main office owned by First National, consists of approximately 45,000 square feet and includes a drive-through banking facility. In addition to its main office, First National conducts its business through two full-service offices, the University office and the North Grand office. A full-service office opened in April of 2007 in Ankeny, Iowa and occupies approximately 14,000 square feet. The University office is located in a 16,000 square foot multi-tenant property owned by the Company. A 24-year lease

agreement with the Company has been modified in 2002 to provide that an equal amount of interior space will be made available to the Company at First National's main office at 405 Fifth Street in lieu of rental payments. First National will continue to rent the drive-up facilities of approximately 1,850 square feet at this location for $1,200 per month. All of the properties owned by the Company and First National are free of any mortgages.

Table of Contents

State Bank conducts its business from its main office located at 1025 Sixth Street, Nevada, Iowa and from a full-service office located in Colo, Iowa. All of these properties are owned by State Bank free of any mortgage.

Boone Bank conducts its business from its main office located at 716 Eighth Street, Boone, Iowa and from one additional full-service office also located in Boone, Iowa. All properties are owned by Boone Bank free of any mortgage.

Randall-Story Bank conducts its business from its main office located at 606 Broad Street, Story City, Iowa which is owned by Randall-Story Bank free of any mortgage.

United Bank conducts its business from its main office located at 2101 South Center Street, Marshalltown, Iowa. The 5,200 square foot premise was constructed in 2002. In 2005, United Bank purchased an office location at 29 S. Center Street in Marshalltown that is 1,972 square feet. In 2007, United Bank purchased a commercial building located at 10 Westwood Drive, in Marshalltown that is 2,304 square feet for future expansion. All properties are owned by United Bank free of any mortgage.

The property the Company owns is located at 2330 Lincoln Way, Ames, Iowa consisting of a multi tenant building of approximately 16,000 square feet. First National leases 5,947 square feet of this building to serve as its University Office and remaining rentable space is leased to six tenants for business purposes. The Company owns a real estate property adjacent to 2330 Lincoln Way at 2318 Lincoln Way which consists of a single story commercial building with 2,400 square feet of leased space that is currently leased by one tenant for business purposes.

ITEM 3. LEGAL PROCEEDINGS

The Banks are from time to time parties to various legal actions arising in the normal course of business. The Company believes that there is no threatened or pending proceeding against the Company or the Banks, which, if determined adversely, would have a material adverse effect on the business or financial condition of the Company or the Banks.

ITEM 4. RESERVED

Table of Contents

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

On February 28, 2011, the Company had approximately 494 shareholders of record and an estimated 878 additional beneficial owners whose shares were held in nominee titles through brokerage or other accounts. The Company's common stock is traded on the NASDAQ Capital Market under the symbol "ATLO". Trading in the Company's common stock is, however, relatively limited. The closing price of the Company's common stock was $18.82 on February 28, 2011.

Based on information provided to and gathered by the Company on an informal basis, the Company believes that the high and low sales price for the common stock on a per share basis during the last two years is as follows:

	2010 Market Price			2009 Market Price	
Quarter	High	Low	Quarter	High	Low
1st	$21.99	$17.00	1st	$28.79	$14.87
2nd	$20.84	$17.26	2nd	$27.00	$16.68
3rd	$20.25	$16.61	3rd	$27.00	$22.21
4th	$22.84	$18.90	4th	$25.00	$18.50

The Company declared aggregate annual cash dividends in 2010 and 2009 of approximately $4,150,000 and $3,773,000, respectively, or $0.44 per share in 2010 and $0.40 per share in 2009. In February 2011, the Company declared a cash dividend of approximately $1,226,000 or $0.13 per share. Quarterly dividends declared during the last two years were as follows:

Quarter	2010 Cash dividends declared per share	2009 Cash dividends declared per share
1st	$ 0.11	$ 0.10
2nd	$ 0.11	$ 0.10
3rd	$ 0.11	$ 0.10
4th	$ 0.11	$ 0.10

The decision to declare cash dividends in the future and the amount thereof rests within the discretion of the Board of Directors of the Company and will be subject to, among other things, the future earnings, capital requirements and financial condition of the Company and certain regulatory restrictions imposed on the payment of dividends by the Banks. Such restrictions are discussed in greater detail in Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources and in Note 12 (Regulatory Matters) to the Company's financial statements included herein.

Table of Contents

ITEM 6. SELECTED FINANCIAL DATA

The following financial data of the Company for the five years ended December 31, 2006 through 2010 is derived from the Company's historical audited financial statements and related footnotes. The information set forth below should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operation" and the consolidated financial statements and related notes contained elsewhere in this Annual Report.

Selected Financial Data

(dollars in thousands, except per share amounts)	Year Ended December 31, 2010	2009	2008	2007	2006
STATEMENT OF INCOME DATA					
Interest income	$37,294	$38,891	$45,514	$47,562	$44,296
Interest expense	7,775	10,226	16,402	23,537	21,306
Net interest income	29,519	28,665	29,112	24,025	22,990
Provision (credit) for loan losses	664	1,558	1,313	(94)	(183)
Net interest income after provision (credit) for loan losses	28,855	27,107	27,799	24,119	23,173
Noninterest income (loss)	6,936	6,924	(3,008)	7,208	6,674
Noninterest expense	18,321	22,732	17,594	16,776	15,504
Income before provision for income tax	17,470	11,299	7,197	14,551	14,343
Provision for income tax	4,504	2,293	845	3,542	3,399
Net income	$12,966	$9,006	$6,352	$11,009	$10,944
DIVIDENDS AND EARNINGS PER SHARE DATA					
Cash dividends declared	$4,150	$3,773	$10,564	$10,183	$9,801
Cash dividends declared per share	$0.44	$0.40	$1.12	$1.08	$1.04
Basic and diluted earnings per share	$1.37	$0.95	$0.67	$1.17	$1.16
Weighted average shares outstanding	9,432,915	9,432,915	9,431,393	9,427,503	9,422,402
BALANCE SHEET DATA					
Total assets	$962,975	$915,570	$858,141	$861,591	$838,853
Net loans	418,094	415,434	452,880	463,651	429,123
Deposits	743,862	722,164	664,795	690,119	680,356
Stockholders' equity	121,363	112,340	103,837	110,021	112,923
Equity to assets ratio	12.60%	12.27%	12.10%	12.77%	13.46%

Table of Contents

	Year Ended December 31,				
	2010	2009	2008	2007	2006
FIVE YEAR FINANCIAL PERFORMANCE					
Net income	$12,966	$9,006	$6,352	$11,009	$10,944
Average assets	928,610	880,057	857,705	843,788	818,450
Average stockholders' equity	118,889	108,412	107,794	111,371	109,508
Return on assets (net income divided by average assets)	1.40 %	1.02 %	0.74 %	1.30 %	1.34 %
Return on equity (net income divided by average equity)	10.91 %	8.31 %	5.89 %	9.89 %	9.99 %
Net interest margin (net interest income divided by average earning assets)	3.74 %	3.78 %	3.94 %	3.39 %	3.29 %
Efficiency ratio (noninterest expense divided by noninterest income plus net interest income)	50.26 %	63.87 %	67.40 %	53.71 %	52.27 %
Dividend payout ratio (dividends per share divided by net income per share)	32.12 %	42.11 %	167.16 %	92.31 %	89.66 %
Dividend yield (dividends per share divided by closing year-end market price)	2.03 %	1.89 %	4.22 %	5.54 %	4.95 %
Equity to assets ratio (average equity divided by average assets)	12.80 %	12.32 %	12.57 %	13.20 %	13.38 %

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

The following discussion is provided for the consolidated operations of the Company and its Banks. The purpose of this discussion is to focus on significant factors affecting the Company's financial condition and results of operations.

The Company does not engage in any material business activities apart from its ownership of the Banks and the managing of its own bond, equity and loan portfolios. Products and services offered by the Banks are for commercial and consumer purposes, including loans, deposits and trust services. The Banks also offer investment services through a third-party broker-dealer. The Company employs eleven individuals to assist with financial reporting, human resources, marketing, audit, compliance, technology systems and the coordination of management activities, in addition to 176 full-time equivalent individuals employed by the Banks.

The Company's primary competitive strategy is to utilize seasoned and competent Bank management and local decision-making authority to provide customers with prompt response times and flexibility in the products and services offered. This strategy is viewed as providing an opportunity to increase revenues through the creation of a competitive advantage over other financial institutions. The Company also strives to remain operationally efficient to improve profitability while enabling the Banks to offer more competitive loan and deposit rates.

Table of Contents

The principal sources of Company revenues and cash flows are: (i) interest and fees earned on loans made by the Company and Banks; (ii) interest on fixed income investments held by the Company and the Banks; (iii) fees on trust services provided by those Banks exercising trust powers; (iv) service charges on deposit accounts maintained at the Banks; and (v) securities gains. The Company's principal expenses are: (i) interest expense on deposit accounts and other borrowings; (ii) salaries and employee benefits; (iii) data processing costs associated with maintaining the Banks' loan and deposit functions; (iv) occupancy expenses for maintaining the Banks' facilities; and (v) FDIC insurance assessments. The largest component contributing to the Company's net income is net interest income, which is the difference between interest earned on earning assets (primarily loans and investments) and interest paid on interest bearing liabilities (primarily deposit accounts and other borrowings). One of management's principal functions is to manage the spread between interest earned on earning assets and interest paid on interest bearing liabilities in an effort to maximize net interest income while maintaining an appropriate level of interest rate risk.

The Company reported net income of $12,966,000 for the year ended December 31, 2010 compared to $9,006,000 and $6,352,000 reported for the years ended December 31, 2009 and 2008, respectively. This represents an increase in net income of 44.0% when comparing 2010 with 2009. The increase in net income in 2010 from 2009 was primarily the result of improved net interest income, lower provision for loan losses and lower non-interest expense due to other real estate owned costs and FDIC insurance assessments. The increase in net income in 2009 from 2008 was primarily the result of improved non-interest income due to the losses associated with other-than-temporary impairment of investment securities in 2008 as compared to 2009. This improvement was offset in part by higher non-interest expense associated primarily with other real estate owned and FDIC insurance assessments. Earnings per share for 2010 were $1.37 compared to $0.95 in 2009 and $0.67 in 2008. All five Banks demonstrated profitable operations during 2010.

The Company's return on average equity for 2010 was 10.91% compared to 8.31% and 5.89% in 2009 and 2008, respectively, and the return on average assets for 2010 was 1.40% compared to 1.02% in 2009 and 0.74% in 2008. The increase in return on average equity and assets when comparing 2010 to 2009 was primarily a result of the increased net income. The increase in return on average equity and assets when comparing 2009 to 2008 was primarily a result of the other-than-temporary impairment on investment securities recorded in 2008, offset in part by increased costs associated with other real estate owned and FDIC insurance assessments.

The following discussion will provide a summary review of important items relating to:

Challenges
Key Performance Indicators
Industry Results
Critical Accounting Policies
Income Statement Review
Balance Sheet Review
Asset Quality Review and Credit Risk Management
Liquidity and Capital Resources
Interest Rate Risk
Inflation
Forward-Looking Statements
Performance Graph

Table of Contents

Challenges

Management has identified certain events or circumstances that may negatively impact the Company's financial condition and results of operations in the future and is attempting to position the Company to best respond to those challenges.

In March of 2009, the Office of Comptroller of the Currency ("OCC") imposed individual minimum capital ratios requiring First National to maintain, on an ongoing basis, Tier One Leverage Capital of 9% of Adjusted Total Assets and Total Risk Based Capital of 11% of Risk Weighted Assets. As of December 31, 2010, First National exceeded these capital ratios. Failure to maintain the individual minimum capital ratios could result in additional regulatory action against First National.

Interest rates are likely to increase as the economy continues its gradual recovery and an increasing interest rate environment may present a challenge to the Company. Increases in interest rates may negatively impact the Company's net interest margin if interest expense increases more quickly than interest income. The Company's earning assets (primarily its loan and investment portfolio) have longer maturities than its interest bearing liabilities (primarily deposits and other borrowings); therefore, in a rising interest rate environment, interest expense may increase more quickly than interest income as the interest bearing liabilities reprice more quickly than earning assets. In response to this challenge, the Banks model quarterly the changes in income that would result from various changes in interest rates. Management believes Bank earning assets have the appropriate maturity and repricing characteristics to optimize earnings and the Banks' interest rate risk positions.

The Company's market in central Iowa has numerous banks, credit unions, and investment and insurance companies competing for similar business opportunities. This competitive environment will continue to put downward pressure on the Banks' net interest margins and thus affect profitability. Strategic planning efforts at the Company and Banks continue to focus on capitalizing on the Banks' strengths in local markets while working to identify opportunities for improvement to gain competitive advantages.

Loans amounted to $418.1 million and $415.4 million as of December 31, 2010 and 2009, respectively. The loan portfolio increased 0.6% during the year ended December 31, 2010. The increase in the loan portfolio is primarily due to increases in the commercial and agricultural operating and commercial real estate loan portfolios. A decline in the loan portfolio would have a negative impact on the Company's earnings for the year.

The economic conditions for commercial real estate developers in the Des Moines metropolitan area deteriorated in 2009 and 2008 and significantly contributed to the Company's increased level of non-performing loans, other real estate owned and related costs in 2009 and 2008. In 2010, there were no significant additional impaired loans in the Des Moines market. During the year ended December 31, 2010, the Company foreclosed on one real estate property (other real estate owned) totaling $402,000 in the Des Moines market. Presently, the Company has $2.9 million in impaired loans with two Des Moines development companies with specific reserves totaling $223,000. The Company has additional customer relationships with real estate developers in the Des Moines area that may become impaired in the future if economic conditions do not improve or become worse. The Company has a limited number of such credits and is actively engaged with the customers to minimize credit risk.

Table of Contents

Other real estate owned amounted to $10.5 million as of December 31, 2010 and 2009. Other real estate owned costs amounted to $195,000, $4,198,000 and $151,000 for the years ended December 31, 2010, 2009 and 2008, respectively. Management obtains independent appraisals or performs evaluations to determine that these properties are carried at the lower of the new cost basis or fair value less cost to sell. It is at least reasonably possible that change in fair values will occur in the near term and that such changes could have a negative impact on the Company's earnings.

The FDIC imposes an assessment against all depository institutions for deposit insurance. The FDIC has the authority to increase insurance assessments. FDIC insurance assessments amounted to $1,120,000, $1,675,000 and $243,000 for the years ended December 31, 2010, 2009 and 2008, respectively. In 2010, 161 banks failed compared to 140 bank failures in 2009 and 25 in 2008. An increase in FDIC deposit assessments will have a negative impact on the Company's earnings.

The Company operates in a highly regulated environment and is subject to extensive regulation, supervision and examination. The compliance burden and impact on the Company's operations and profitability with respect to the Dodd-Frank Act are currently unknown, as the Dodd-Frank Act delegates to various federal agencies the task of implementing its many provisions through regulation. Hundreds of new federal regulations, studies and reports addressing all of the major areas of the new law, including the regulation of financial institutions and their holding companies, will be required, ensuring that federal rules and policies in this area will be further developing for months and years to come. Based on the provisions of the Dodd-Frank Act and anticipated implementing regulations, it is highly likely that financial institutions as well as their holding companies will be subject to significantly increased regulation and compliance obligations that expose them to noncompliance risk and consequences. The Bureau of Financial Consumer Protection ("BCFP") has broad rulemaking authority to administer and carry out the purposes and objectives of the new federal consumer protection laws, and to prevent evasions thereof," with respect to all financial institutions that offer financial products and services to consumers. The BCFP is also authorized to prescribe rules, applicable to any covered person or service provider, identifying and prohibiting acts or practices that are "unfair, deceptive, or abusive" in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service ("UDAP authority"). The full reach and impact of the BCFP's broad new rulemaking powers and UDAP authority on the operations of financial institutions offering consumer financial products or services is currently unknown. Notwithstanding, insured depository institutions with assets of $10 billion or less will continue to be supervised and examined by their primary federal regulators, rather than the BCFP, with respect to compliance with the federal consumer protection laws. Regulatory authorities have extensive discretion in connection with their supervisory and enforcement activities, including but not limited to the imposition of restrictions on the operation of an institution, the classification of assets by the institution and the adequacy of an institution's allowance for loan losses. Any change in such regulation and oversight, whether in the form of restrictions on activities, regulatory policy, regulations, or legislation, including but not limited to changes in the regulations governing banks, could have a material impact on the Company's operations. It is unknown at this time to what extent legislation will be passed into law or regulatory proposals will be adopted, or the effect that such passage or adoption will have on the banking industry or the Company. Applicable laws and regulations may change, and there is no assurance that such changes will not adversely affect the Company's business.

Table of Contents

Key Performance Indicators

Certain key performance indicators for the Company and the industry are presented in the following chart. The industry figures are compiled by the Federal Deposit Insurance Corporation (FDIC) and are derived from 7,657 commercial banks and savings institutions insured by the FDIC. Management reviews these indicators on a quarterly basis for purposes of comparing the Company's performance from quarter to quarter against the industry as a whole.

Selected Indicators for the Company and the Industry

	Year Ended December 31,					
	2010		2009		2008	
	Company	Industry	Company	Industry	Company	Industry
Return on assets	1.40 %	0.66 %	1.02 %	0.09 %	0.74 %	0.12 %
Return on equity	10.91 %	5.99 %	8.31 %	0.90 %	5.89 %	1.24 %
Net interest margin	3.74 %	3.76 %	3.78 %	3.47 %	3.94 %	3.18 %
Efficiency ratio	50.26 %	57.22 %	63.87 %	55.53 %	67.40 %	59.02 %
Capital ratio	12.80 %	8.90 %	12.32 %	8.65 %	12.57 %	7.49 %

Key performance indicators include:

Return on Assets

This ratio is calculated by dividing net income by average assets. It is used to measure how effectively the assets of the Company are being utilized in generating income. The Company's return on assets ratio is higher than that of the industry, primarily as a result of the Company's lower provision for loan losses and non-interest expense relative to the industry.

Table of Contents

Return on Equity

This ratio is calculated by dividing net income by average equity. It is used to measure the net income or return the Company generated for the shareholders' equity investment in the Company. The Company's return on equity ratio is higher than the industry primarily as a result of the Company's lower provision for loan losses and non-interest expense relative to the industry.

Net Interest Margin

This ratio is calculated by dividing net interest income by average earning assets. Earning assets consist primarily of loans and investments that earn interest. This ratio is used to measure how well the Company is able to maintain interest rates on earning assets above those of interest-bearing liabilities, which is the interest expense paid on deposit accounts and other borrowings. The Company's net interest margin is comparable to that of the industry.

Efficiency Ratio

This ratio is calculated by dividing noninterest expense by net interest income and noninterest income. The ratio is a measure of the Company's ability to manage noninterest expenses. The Company's efficiency ratio is lower than the industry average. The Company's efficiency ratio decreased in 2010 as compared to 2009 primarily as a result of the impairment of other real estate owned in 2009 with no significant impairment in 2010.

Capital Ratio

The capital ratio is calculated by dividing average total equity capital by average total assets. It measures the level of average assets that are funded by shareholders' equity. Given an equal level of risk in the financial condition of two companies, the higher the capital ratio, generally the more financially sound the company. The Company's capital ratio is significantly higher than the industry average.

Industry Results

The FDIC Quarterly Banking Profile reported the following results for the fourth quarter of 2010:

Fourth Quarter Earnings Contrast Favorably with Year-Earlier Net Loss

Lower expenses for troubled loans continued to boost the earnings of insured commercial banks and savings institutions in fourth quarter 2010. The 7,657 institutions filing year-end reports posted quarterly net income of $21.7 billion, a substantial improvement over the $1.8 billion net loss in fourth quarter 2009 and the second-highest quarterly total reported since second quarter 2007. The greatest year-over-year improvement in earnings occurred at the largest banks, but almost two out of every three institutions (62%) reported better net income than a year ago. One in four institutions reported a net loss in the fourth quarter, an improvement from a year ago when more than one in three (35%) were unprofitable.

Table of Contents

Provisions Fall to Lowest Level in More than Three Years

Insured institutions set aside $31.6 billion in provisions for loan losses in the fourth quarter, almost 50% less than the $62.9 billion they set aside a year earlier. This is the smallest quarterly loss provision for the industry since third quarter 2007. Much of the year-over-year reduction in provisions was concentrated among some of the largest banks. Seven large institutions accounted for more than half of the $31.3 billion reduction. However, a majority of insured institutions (54%) reduced their provisions in the fourth quarter compared to a year ago.

Revenue Growth Slows

Revenue growth was sluggish in the fourth quarter. Net operating revenue (net interest income plus total noninterest income) was $163.6 billion, only $2.8 billion (1.7%) higher than a year earlier and $2.1 billion (1.3%) less than in third quarter 2010. This is the second-smallest year-over-year increase in quarterly net operating income in the past two years (after the $911 million year-over-year increase in second quarter 2010). Despite the small size of the aggregate increase, revenues were up at almost two-thirds of all institutions (62.4%).

Fee Income Declines

Among the notable areas of noninterest revenue weakness, service charge income on deposit accounts at banks filing Call Reports was $2.1 billion (20.7%) lower than a year earlier. This is the second consecutive quarter that deposit account fees have declined by 20% or more from the prior year. Asset servicing income was $2.2 billion (32.3%) lower, and securitization income was down by $1.5 billion (90.7%). Both declines were primarily the result of changes in accounting rules that affected financial reporting in 2010.1The new accounting rules also were responsible for much of the $7.5 billion (7.5%) year-over-year increase in quarterly net interest income. A majority of institutions (59.8%) reported higher net interest margins than a year ago, but fourth quarter margins were lower than third quarter margins at 55% of institutions.

Higher Asset Values Contribute to Income Improvement

The industry's bottom line also benefited from improvement in asset values. Gains on sales of loans and other assets totaled $4 billion in the fourth quarter, more than three times the $1.3 billion in gains that sales produced in fourth quarter 2009. Realized gains on securities totaled $2.3 billion, compared to $5 million in realized losses a year earlier.

Full-Year Earnings Represent Sharp Improvement from Revised 2009 Loss

Full-year 2010 net income totaled $87.5 billion, compared to a revised net loss of $10.6 billion in 2009. This is the highest full-year earnings total for the industry since 2007. More than two out of every three institutions (67.5%) reported higher earnings in 2010 than in 2009. The proportion of unprofitable institutions fell from 30.6% in 2009 to 21% in 2010. This is the first time in six years that the percentage of institutions reporting full-year net losses has declined. The largest factor in the improvement in the industry's net income was a $92.6 billion (37.1%) reduction in loan-loss provisions. The second-largest source of improvement was a $28.7 billion decline in charges for goodwill impairment.2 An additional contribution came from realized gains on securities and other assets, which were $10.8 billion higher. The improvement in full-year earnings was limited by increased income taxes, which were $32.2 billion higher than in 2009. Overall net operating revenue growth was relatively weak in 2010. The $10.8 billion (1.6%) increase was the second-worst year-over-year change in the past 16 years, after the $20.4 billion decline registered in 2008. Noninterest income from service charges on deposit accounts was $5.5 billion (13.1%) lower than in 2009. This is the first time in the 69 years that these data have been collected that full-year service charge income has declined. Insured institutions paid $53.9 billion in dividends in 2010, an increase of $6.7 billion (14.3%) over 2009, but less than half the annual record of $110.3 billion paid in 2007. Retained earnings totaled $33.6 billion,

marking the first year since 2006 that the industry as a whole has reported internal capital growth.

Table of Contents

Loan Losses Continue to Decline across Most Major Categories

Net loan and lease charge-offs (NCOs) totaled $41.9 billion in the fourth quarter, a decline of $13 billion (23.7%) compared to fourth quarter 2009. With the exception of credit cards (which reflected the application of new accounting rules in 2010), almost all major loan categories posted year-over-year declines in quarterly charge-offs. Real estate construction and development loan charge-offs were $4.2 billion lower, while charge-offs of commercial and industrial (C&I) loans were down by $4 billion. Closed-end one-to-four family residential real estate NCOs were $3.1 billion lower, and home equity line of credit NCOs fell by $1.5 billion. NCOs of nonfarm nonresidential real estate loans were only $101 million higher than a year earlier. Reported credit card NCOs were $2.9 billion higher due to the inclusion in 2010 of NCOs on securitized credit card balances that were not included in prior years. Even with the reporting change, the year-over-year increase in quarterly credit card NCOs was the smallest in two years. On a consecutive-quarter basis, credit card NCOs have fallen in each of the past three quarters.

Nonperforming Asset Balances Fall for Third Consecutive Quarter

The amount of loan and lease balances that were noncurrent (90 days or more past due or in nonaccrual status) fell for a third consecutive quarter, declining by $17.9 billion (4.7%). Noncurrent balances declined in all major loan categories, led by real estate construction loans (down $7.4 billion), C&I loans (down $3.2 billion), multifamily residential real estate loans (down $2.1 billion), and closed-end one-to-four family residential real estate loans (down $2 billion). The industry's inventory of other real estate owned (primarily property acquired through foreclosure) declined for the first time since fourth quarter 2005, falling by $374 million. At the end of 2010, noncurrent assets and other real estate owned represented 3.11% of total industry assets, the lowest share since the end of third quarter 2009. 1 See FASB Statements 166 and 167 in Notes to Users.2 Amendments to prior financial reports received from one large institution resulted in a $10.4 billion reduction in expenses for goodwill impairment in third quarter 2010 and $20.3 billion in increased expenses for goodwill impairment in the first two quarters of 2009.

Reserve Balances Shrink as Loss Provisions Trail Net Charge-Offs

Reserves for loan and lease losses declined for a third consecutive quarter, falling by $11.1 billion (4.6%), as net charge-offs of $41.9 billion exceeded loss provisions of $31.6 billion. Four large banks accounted for more than half of the decline in industry reserves, as more than a third of all institutions (39.4%) reduced their loss reserve balances in the fourth quarter. However, owing to the decline in noncurrent loans, the industry's "coverage ratio" of reserves to noncurrent loans and leases remained essentially unchanged from the previous quarter, at 64.2%. More than half of all institutions (52.3%) increased their coverage ratios in the fourth quarter, while 39.3% reported coverage ratio declines.

Table of Contents

Tier 1 Capital Posts Small Increase

Equity capital fell by $8.5 billion (0.6%) in the fourth quarter, the first quarterly decline since fourth quarter 2008. The drop was caused by a $16.2 billion (71.9%) decline in unrealized gains on securities held for sale. In contrast, insured institution tier 1 leverage capital, which is not affected by changes in securities values, increased by $3.4 billion (0.3%). Total regulatory capital declined by $616 million, reflecting the reduction in loan-loss reserves in the fourth quarter. At the end of 2010, almost 96% of all insured institutions, representing more than 99% of all insured institution assets, met or exceeded the minimum requirements of the highest regulatory capital category, according to the calculations used for purposes of Prompt Corrective Action.

Loan Balances Decline at a Majority of Institutions

Total assets of insured institutions declined by $51.8 billion (0.4%) in the fourth quarter. Assets in trading accounts fell by $43.1 billion (5.6%), while total loan and lease balances dropped by $13.6 billion (0.2%). The largest reductions in loan portfolios occurred in real estate construction and development loans, where balances fell by $32.5 billion (9.2%); non-credit card consumer loans (down $29 billion, or 4.9%); and home equity lines of credit, where drawn balances shrank by $11 billion (1.7%). Securities portfolios rose by $26.1 billion (1%), as institution holdings of mortgage-backed securities increased by $42.7 billion (3%). Among loan categories that posted increases during the quarter, credit cards had a seasonal increase of $18.1 billion (2.6%); one-to-four family residential mortgage loans increased for the second quarter in a row, rising by $17 billion (0.9%); and C&I loans also posted a second consecutive quarterly increase, rising by $11.8 billion (1%). Loan balances fell at almost 60% of insured institutions in the fourth quarter.

Deposit Growth Remains Strong

Deposits grew strongly for a second consecutive quarter, rising by $149.3 billion (1.6%), after a $132.7 billion (1.5%) increase in the third quarter. Noninterest-bearing deposits in domestic offices increased by $81.6 billion (5.1%). Nondeposit liabilities fell by $200.4 billion (7.8%), as Federal Home Loan Bank advances declined by $15.9 billion (4%), other secured borrowings dropped by $64.9 billion (14.3%), and liabilities in trading accounts fell by $30.2 billion (9.5%). At year-end, deposits funded 70.7% of total industry assets, the highest proportion since the end of first quarter 1996.

Failures Reached an 18-Year High in 2010

The number of insured institutions reporting quarterly financial results fell from 7,761 to 7,657 in the fourth quarter. Thirty insured institutions failed during the quarter and an additional 73 were absorbed in mergers. There were three new charters added in the quarter. For all of 2010, mergers absorbed 197 institutions, while 157 insured commercial banks and savings institutions failed. This is the largest annual number of bank failures since 1992, when 181 institutions failed. Only 11 new reporters were added during 2010, the smallest annual total in the FDIC's 77-year history. The number of institutions on the FDIC's "Problem List" increased from 860 to 884 in the fourth quarter. Total assets of "problem" institutions increased from $379 billion to $390 billion.

Table of Contents

Critical Accounting Policies

The discussion contained in this Item 7 and other disclosures included within this Annual Report are based on the Company's audited consolidated financial statements. These statements have been prepared in accordance with accounting principles generally accepted in the United States of America. The financial information contained in these statements is, for the most part, based on the financial effects of transactions and events that have already occurred. However, the preparation of these statements requires management to make certain estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses.

The Company's significant accounting policies are described in the "Notes to Consolidated Financial Statements" accompanying the Company's audited financial statements. Based on its consideration of accounting policies that involve the most complex and subjective estimates and judgments, management has identified the allowance for loan losses, valuation of other real estate owned and the assessment of other-than-temporary impairment for certain financial instruments to be the Company's most critical accounting policies.

Allowance for Loan Losses

The allowance for loan losses is established through a provision for loan losses that is treated as an expense and charged against earnings. Loans are charged against the allowance for loan losses when management believes that collectability 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 area. To the extent actual results differ from forecasts and management's judgment, the allowance for loan losses may be greater or lesser than future charge-offs. Due to potential changes in conditions, it is at least reasonably possible that changes in estimates will occur in the near term and that such changes could be material to the amounts reported in the Company's financial statements.

For further discussion concerning the allowance for loan losses and the process of establishing specific reserves, see the section of this Annual Report entitled "Asset Quality Review and Credit Risk Management" and "Analysis of the Allowance for Loan Losses".

Other Real Estate Owned

Real estate properties acquired through or in lieu of foreclosure are initially recorded at the fair value less estimated selling cost at the date of foreclosure. Any write-downs based on the asset's fair value at the date of acquisition are charged to the allowance for loan losses. After foreclosure, valuations are periodically performed by management and property held for sale is carried at the lower of the new cost basis or fair value less cost to sell. Impairment losses on property to be held and used are measured as the amount by which the carrying amount of a property exceeds its fair value. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. The portion of interest costs relating to development of real estate is capitalized. Independent appraisals or evaluations are periodically performed by management, and any subsequent write-downs are recorded as a charge to operations, if necessary, to reduce the carrying value of a property to the lower of its cost basis or fair value less cost to sell. These appraisals or evaluations are inherently subjective and require estimates that are susceptible to significant revisions as more information becomes available. Due to potential changes in conditions, it is at least reasonably possible that changes in fair values will occur in the near term and that such changes could materially affect the amounts reported in the Company's financial statements.

38

Table of Contents

Other-Than-Temporary Impairment of Investment Securities

Declines in the fair value of available-for-sale securities below their cost that are deemed to be other-than-temporary are generally reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the intent to sell the investment securities and the more likely than not requirement that the Company will be required to sell the investment securities prior to recovery (2) the length of time and the extent to which the fair value has been less than cost and (3) the financial condition and near-term prospects of the issuer. Due to potential changes in conditions, it is at least reasonably possible that changes in management's assessment of other-than-temporary impairment will occur in the near term and that such changes could be material to the amounts reported in the Company's financial statements.

Income Statement Review

The following highlights a comparative discussion of the major components of net income and their impact for the last three years.

Average Balances and Interest Rates

The following two tables are used to calculate the Company's net interest margin. The first table includes the Company's average assets and the related income to determine the average yield on earning assets. The second table includes the average liabilities and related expense to determine the average rate paid on interest bearing liabilities. The net interest margin is equal to the interest income less the interest expense divided by average earning assets. Refer to the net interest income discussion following the tables for additional detail.

Table of Contents

ASSETS

(dollars in thousands)	2010 Average balance	2010 Revenue/ expense	2010 Yield/ rate	2009 Average balance	2009 Revenue/ expense	2009 Yield/ rate	2008 Average balance	2008 Revenue/ expense	2008 Yield/ rate
Interest-earning assets									
Loans 1									
Commercial	$ 68,905	$ 3,869	5.61 %	$ 68,677	$ 3,535	5.15 %	$ 82,448	$ 4,915	5.96 %
Agricultural	41,941	2,443	5.82 %	36,351	2,196	6.04 %	32,230	2,227	6.91 %
Real estate	284,515	16,542	5.81 %	304,362	18,074	5.94 %	324,863	20,754	6.39 %
Consumer and other	22,327	1,207	5.41 %	25,078	1,407	5.61 %	24,241	1,562	6.44 %
Total loans (including fees)	$ 417,688	$ 24,061	5.76 %	$ 434,468	$ 25,212	5.80 %	$ 463,782	$ 29,458	6.35 %
Investment securities									
Taxable	239,853	6,965	2.90 %	203,735	7,967	3.91 %	$ 196,619	$ 9,813	4.99 %
Tax-exempt 2	183,541	8,875	4.84 %	151,340	7,991	5.28 %	140,425	8,894	6.33 %
Total investment securities	$ 423,394	$ 15,840	3.74 %	$ 355,075	$ 15,958	4.49 %	$ 337,044	$ 18,707	5.55 %
Interest bearing deposits and federal funds sold	32,130	489	1.52 %	41,645	499	1.20 %	13,971	364	2.61 %
Total interest-earning assets	$ 873,212	$ 40,390	4.63 %	$ 831,189	$ 41,669	5.01 %	$ 814,797	$ 48,529	5.96 %
Noninterest-earning assets									
Cash and due from banks	$ 19,544			$ 20,720			$ 19,581		
Premises and equipment, net	11,718			12,216			13,007		
Other, less allowance for loan losses	24,136			15,932			10,320		
Total noninterest-earning assets	$ 55,398			$ 48,868			$ 42,908		

TOTAL ASSETS	$ 928,610	$ 880,057	$ 857,705

1 Average loan balance includes nonaccrual loans, if any. Interest income collected on nonaccrual loans has been included.
2 Tax-exempt income has been adjusted to a tax-equivalent basis using an incremental tax rate of 35%.

Table of Contents

Average Balances and Interest Rates (continued)

LIABILITIES AND STOCKHOLDERS' EQUITY

(dollars in thousands)	2010 Average balance	2010 Revenue/ expense	2010 Yield/ rate	2009 Average balance	2009 Revenue/ expense	2009 Yield/ rate	2008 Average balance	2008 Revenue/ expense	2008 Yield/ rate
Interest-bearing liabilities									
Deposits									
Savings, NOW accounts, and money markets	$ 386,010	$ 1,369	0.35 %	$ 355,504	$ 1,650	0.46 %	$ 317,346	$ 3,658	1.15 %
Time deposits < $100,000	147,453	3,076	2.09 %	157,749	4,488	2.84 %	170,223	6,603	3.88 %
Time deposits > $100,000	89,290	1,651	1.85 %	84,786	2,290	2.70 %	97,193	3,947	4.06 %
Total deposits	$ 622,753	$ 6,096	0.98 %	$ 598,040	$ 8,428	1.41 %	$ 584,762	$ 14,208	2.43 %
Other borrowed funds	87,758	1,679	1.91 %	83,841	1,798	2.14 %	78,764	2,194	2.79 %
Total interest-bearing liabilities	$ 710,511	$ 7,775	1.09 %	$ 681,881	$ 10,226	1.50 %	$ 663,526	$ 16,402	2.47 %
Noninterest-bearing liabilities									
Demand deposits	94,286			84,245			78,033		
Other liabilities	4,924			5,519			8,352		
Stockholders' equity	118,889			108,412			107,794		
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 928,610			$ 880,057			$ 857,705		
Net interest income		$ 32,615	3.74 %		$ 31,443	3.78 %		$ 32,127	3.94 %

Spread Analysis

Interest income/average assets	$ 40,390	4.35 %	$ 41,669	4.73 %	$ 48,529	5.66 %
Interest expense/average assets	7,775	0.84 %	10,226	1.16 %	16,402	1.91 %
Net interest income/average assets	32,615	3.51 %	31,443	3.57 %	32,127	3.75 %

Rate and Volume Analysis

The rate and volume analysis is used to determine how much of the change in interest income or expense is the result of a change in volume or a change in interest rate. For example, real estate loan interest income decreased $1,532,000 in 2010 compared to 2009. Decreased volume of real estate loans lowered income in 2010 by $1,147,000 and lower interest rates lowered interest income in 2010 by $385,000.

Table of Contents

The following table sets forth, on a tax-equivalent basis, a summary of the changes in net interest income resulting from changes in volume and rates.

(dollars in thousands)	2010 Compared to 2009			2009 Compared to 2008		
	Volume	Rate	Total 1	Volume	Rate	Total 1
Interest income						
Loans						
Commercial	$ 12	$ 322	$ 334	$ (761)	$ (618)	$ (1,379)
Agricultural	329	(82)	247	267	(298)	(31)
Real estate	(1,147)	(385)	(1,532)	(1,266)	(1,414)	(2,680)
Consumer and other	(151)	(49)	(200)	52	(207)	(155)
Total loans (including fees)	(957)	(194)	(1,151)	(1,708)	(2,537)	(4,245)
Investment securities						
Taxable	1,267	(2,269)	(1,002)	344	(2,190)	(1,846)
Tax-exempt	1,592	(708)	884	653	(1,556)	(903)
Total investment securities	2,859	(2,977)	(118)	997	(3,746)	(2,749)
Interest bearing deposits and federal funds sold	(127)	117	(10)	500	(365)	135
Total interest-earning assets	1,775	(3,054)	(1,279)	(211)	(6,649)	(6,860)
Interest-bearing liabilities Deposits						
Savings, NOW accounts, and money markets	132	(413)	(281)	396	(2,404)	(2,008)
Time deposits < $100,000	(279)	(1,133)	(1,412)	(454)	(1,661)	(2,115)
Time deposits > $100,000	116	(755)	(639)	(457)	(1,200)	(1,657)
Total deposits	(31)	(2,301)	(2,332)	(515)	(5,265)	(5,780)
Other borrowed funds	81	(200)	(119)	136	(532)	(396)
Total interest-bearing liabilities	50	(2,501)	(2,451)	(379)	(5,797)	(6,176)
	$ 1,725	$ (553)	$ 1,172	$ 168	$ (852)	$ (684)

Net interest
income-earning assets

1 The change in interest due to both volume and yield/rate has been allocated to change due to volume and change due to yield/rate in proportion to the absolute value of the change in each.

Net Interest Income

The Company's largest contributing component to net income is net interest income, which is the difference between interest earned on earning assets and interest paid on interest bearing liabilities. The volume of and yields earned on earning assets and the volume of and the rates paid on interest bearing liabilities determine net interest income. Refer to the tables preceding this paragraph for additional detail. Interest earned and interest paid is also affected by general economic conditions, particularly changes in market interest rates, by government policies and the action of regulatory authorities. Net interest income divided by average earning assets is referred to as net interest margin. For the years December 31, 2010, 2009 and 2008, the Company's net interest margin was 3.74%, 3.78% and 3.94%, respectively.

Table of Contents

Net interest income during 2010, 2009 and 2008 totaled $29,519,000, $28,665,000 and $29,112,000, respectively, representing a 3% increase in 2010 compared to 2009 and a 2% decrease in 2009 from 2008. Net interest income increased in 2010 as compared to 2009 due primarily to increases in average interest-earning assets, offset in part by yields on investments declining more than yields on deposits. Net interest income declined in 2009 as compared to 2008 as yields on loans and investment securities declined more than yields on deposits and other borrowings.

The high level of competition in the local markets will continue to put downward pressure on the net interest margin of the Company. Currently, the Company's largest market, Ames, Iowa, has ten banks, two thrifts, six credit unions and several other financial investment companies. Multiple banks are also located in the Company's other communities creating similarly competitive environments.

Provision for Loan Losses

The provision for loan losses reflects management's judgment of the expense to be recognized in order to maintain an adequate allowance for loan losses. The Company's provision for loan losses for the year ended December 31, 2010 was $664,000 compared to $1,558,000 for the previous year. The lower provision for loan losses in 2010 as compared to 2009 was due primarily to a lower provision for loan losses on impaired loans for the year ended December 31, 2010 as compared to the year ended December 31, 2009. The Company's provision for loan losses for the year ended December 31, 2009 was $1,558,000 compared to $1,313,000 for the previous year. Increases in the general factors used to calculate the provision for loan losses due to weakening economic conditions and a higher level of specific reserve on impaired loans, offset in part by a decrease in the loan portfolio, were the primary reasons the provision for loan losses increased from 2008 to 2009. Refer to the Asset Quality and Credit Risk Management discussion for additional details with regard to loan loss provision expense.

Management believes the allowance for loan losses is adequate to absorb probable losses in the current portfolio. This statement is based upon management's continuing evaluation of inherent risks in the current loan portfolio, current levels of classified assets and general economic factors. The Company will continue to monitor the allowance and make future adjustments to the allowance as conditions dictate. Due to potential changes in conditions, it is at least reasonably possible that changes in estimates will occur in the near term and that such changes could be material to the amounts reported in the Company's financial statements.

Noninterest Income (Loss) and Expense

Total noninterest income (loss) is comprised primarily of fee-based revenues from trust and agency services, bank-related service charges on deposit activities, net securities gains, other-than-temporary impairment of investment securities, merchant and ATM fees related to electronic processing of merchant and cash transactions and gain on the sale of loans held for sale.

Table of Contents

Noninterest income (loss) during the years ended 2010, 2009 and 2008 totaled $6,936,000, $6,924,000 and ($3,008,000), respectively. The slightly higher non-interest income in 2010 as compared to 2009 related primarily to higher trust department income and merchant and ATM fees, offset in part by decreases in service fees and security gains. Trust income increases are due primarily to increases in the customer base. Increase in merchant and ATM fees are due primarily to increase in usage. Decreases in service fees are due in part to regulatory changes associated with overdraft fees. The higher non-interest income in 2009 as compared to 2008 related primarily to significant other-than-temporary impairment of investment securities in 2008, offset in part by lower securities gains in 2009 as compared to 2008. Impairment for 2008 primarily related to charges of $8,451,000 related to Federal National Mortgage Association and Federal Home Loan Mortgage Corporation preferred stock and $3,603,000 related to three corporate bonds. Excluding securities gains in 2010 and 2009, noninterest income increased 3.9% in 2010 as compared to 2009. Excluding the other-than-temporary impairment of investment securities and securities gains in 2009 and 2008, noninterest income increased 4.3% in 2009 as compared to 2008.

Noninterest expense for the Company consists of all operating expenses other than interest expense on deposits and other borrowed funds. Historically, the Company has not had any material expenses relating to discontinued operations, extraordinary losses or adjustments from a change in accounting principles. Salaries and employee benefits are the largest component of the Company's operating expenses and comprise 59% of noninterest expenses in 2010.

Noninterest expense during the years ended 2010, 2009 and 2008 totaled $18,321,000, $22,732,000 and $17,594,000, respectively, representing a 19% decrease in 2010 compared to a 29% increase in 2009. The primary reason for the decrease in 2010 was the decreases in other real estate owned costs, due primarily to impairment write downs in 2009, and the decrease in FDIC insurance assessment, due to a one-time special assessment in 2009 and lower assessment rates in 2010. The primary reason for the increase in 2009 compared to 2008 was the increases in other real estate owned costs, due primarily to impairment write downs, and the increase in FDIC insurance assessment, due to a one-time special assessment and increased assessment rates. The percentage of noninterest expense to average assets was 1.97% in 2010, compared to 2.58% and 2.05% during 2009 and 2008, respectively.

Provision for Income Taxes

The provision for income taxes for 2010, 2009 and 2008 was $4,504,000, $2,293,000 and $845,000, respectively. This amount represents an effective tax rate of 26% during 2010, compared to 20% and 12% for 2009 and 2008, respectively. The Company's marginal federal tax rate is currently 35%. The difference between the Company's effective and marginal tax rate is primarily related to investments made in tax exempt securities.

Balance Sheet Review

The Company's assets are comprised primarily of loans and investment securities. Average earning asset maturity or repricing dates are less than five years for the combined portfolios as the assets are funded for the most part by short term deposits with either immediate availability or less than one year average maturities. This exposes the Company to risk with regard to changes in interest rates that are more fully explained in Item 7A of this Annual Report "Quantitative and Qualitative Disclosures about Market Risk".

Table of Contents

Total assets increased to $962,975,000 in 2010 compared to $915,570,000 in 2009, a 5.2% increase. The increase in assets was due primarily to increases in the Company's investment securities portfolio of $51,253,000 when comparing year end 2010 and 2009.

Loan Portfolio

Net loans as of December 31, 2010 totaled $418,094,000, up slightly from the $415,434,000 as of December 31, 2009, an increase of 0.6%. The increase in loan volume occurred in spite of a continuing weakness in loan demand. Loans are the primary contributor to the Company's revenues and cash flows. The average yield on loans was 202 and 131 basis points higher in 2010 and 2009, respectively, in comparison to the average tax-equivalent investment portfolio yields.

Types of Loans

The following table sets forth the composition of the Company's loan portfolio for the past five years ending at December 31, 2010.

(dollars in thousands)	2010	2009	2008	2007	2006
Real Estate					
Construction	$ 19,597	$ 22,864	$ 35,326	$ 46,568	$ 30,600
1-4 family residential	88,933	91,673	95,988	104,762	103,620
Commercial	139,370	141,741	153,366	147,023	139,149
Agricultural	31,931	30,788	33,547	33,684	31,092
Commercial	78,173	69,031	76,653	78,616	73,760
Agricultural	45,630	42,356	40,324	36,133	33,434
Consumer and other	22,052	24,693	24,528	22,782	24,276
Total loans	425,686	423,146	459,732	469,568	435,931
Deferred loan fees, net	71	60	72	137	276
Total loans net of deferred fees	$ 425,615	$ 423,086	$ 459,660	$ 469,431	$ 435,655

The Company's loan portfolio consists of real estate loans, commercial loans, agricultural loans and consumer loans. As of December 31, 2010, gross loans totaled approximately $426 million, which equals approximately 57% of total deposits and 44% of total assets. The Company's peer group (consisting of 438 bank holding companies with total assets of $500 to $1,000 million) loan to deposit ratio as of December 31, 2010 was a much higher 80%. The primary factor relating to the lower loan to deposit ratio for the Company compared to peer group averages is a more conservative underwriting philosophy. As of December 31, 2010, the majority of the loans were originated directly by the Banks to borrowers within the Banks' principal market areas. There are no foreign loans outstanding during the years presented.

Real estate loans include various types of loans for which the Banks hold real property as collateral and consist of loans primarily on commercial properties and single family residences. Real estate loans typically have fixed rates for up to five years, with the Company's loan policy permitting a maximum fixed rate maturity of up to 15 years. The majority of construction loan volume is given to contractors to construct commercial buildings and these loans generally have maturities of up to 12 months. The Banks originate residential real estate loans for sale to the secondary market for a fee.

Table of Contents

Commercial loans consist primarily of loans to businesses for various purposes, including revolving lines to finance current operations, floor-plans, inventory and accounts receivable; capital expenditure loans to finance equipment and other fixed assets; and letters of credit. These loans generally have short maturities, have either adjustable or fixed rates and are unsecured or secured by inventory, accounts receivable, equipment and/or real estate.

Agricultural loans play an important part in the Banks' loan portfolios. Iowa is a major agricultural state and is a national leader in both grain and livestock production. The Banks play a significant role in their communities in financing operating, livestock and real estate activities for area producers.

Consumer loans include loans extended to individuals for household, family and other personal expenditures not secured by real estate. The majority of the Banks' consumer lending is for vehicles, consolidation of personal debts, household appliances and improvements.

The interest rates charged on loans vary with the degree of risk and the amount and maturity of the loan. Competitive pressures, market interest rates, the availability of funds and government regulation further influence the rate charged on a loan. The Banks follow a loan policy, which has been approved by both the board of directors of the Company and the Banks, and is overseen by both Company and Bank management. These policies establish lending limits, review and grading criteria and other guidelines such as loan administration and allowance for loan losses. Loans are approved by the Banks' board of directors and/or designated officers in accordance with respective guidelines and underwriting policies of the Company. Credit limits generally vary according to the type of loan and the individual loan officer's experience. Loans to any one borrower are limited by applicable state and federal banking laws.

Table of Contents

Maturities and Sensitivities of Loans to Changes in Interest Rates as of December 31, 2010

The contractual maturities of the Company's loan portfolio are as shown below. Actual maturities may differ from contractual maturities because individual borrowers may have the right to prepay loans with or without prepayment penalties.

(dollars in thousands)	Within one year	After one year but within five years	After five years	Total
Real Estate				
Construction	$ 10,006	$ 8,819	$ 772	$ 19,597
1-4 family residential	29,227	39,295	20,411	88,933
Commercial	18,914	102,176	18,280	139,370
Agricultural	9,664	17,366	4,901	31,931
Commercial	36,001	39,540	2,632	78,173
Agricultural	30,110	14,261	1,259	45,630
Consumer and other	2,745	13,945	5,362	22,052
Total loans	$ 136,667	$ 235,402	$ 53,617	$ 425,686

	After one year but within five years	After five years
Loan maturities after one year with:		
Fixed rates	$ 177,828	$ 41,177
Variable rates	57,574	12,440
	$ 235,402	$ 53,617

Loans Held For Sale

Mortgage origination funding awaiting delivery to the secondary market totaled $1,993,000 and $1,023,000 as of December 31, 2010 and 2009, respectively. Residential mortgage loans are originated by the Banks and sold to several secondary mortgage market outlets based upon customer product preferences and pricing considerations. The mortgages are sold in the secondary market to eliminate interest rate risk and to generate secondary market fee income. It is not anticipated at the present time that loans held for sale will become a significant portion of total assets.

Investment Portfolio

Total investments as of December 31, 2010 were $469,908,000, an increase of $51.3 million or 12% from the prior year end. As of December 31, 2010 and 2009, the investment portfolio comprised 49% and 46% of total assets, respectively.

Table of Contents

The following table presents the fair values, which represent the carrying values due to the available-for-sale classification, of the Company's investment portfolio as of December 31, 2010, 2009 and 2008, respectively. This portfolio provides the Company with a significant amount of liquidity.

(dollars in thousands)	2010	2009	2008
U.S. treasury securities	$503	$525	$546
U.S. government agencies	87,412	106,640	49,695
U.S. government mortgage-backed securities	127,349	101,590	67,516
State and political subdivisions	228,373	178,052	128,741
Corporate bonds	20,372	24,300	55,237
Equity securities	5,898	7,548	11,279
Total	$469,907	$418,655	$313,014

Investments in states and political subdivisions represent purchases of municipal bonds located primarily in the state of Iowa and contiguous states.

Corporate bond investments with a fair value of $358,000 with one issuer are considered other-than-temporarily impaired at December 31, 2010. There are no other corporate bonds that the Company would consider to be other-than-temporarily impaired as of December 31, 2010.

The equity securities portfolio consisted primarily of financial and utility stocks as of December 31, 2010, 2009, and 2008. The investment in the equity securities portfolio also includes an issue of Federal National Mortgage Association preferred stock and an issue of Federal Home Loan Mortgage Corporation preferred stock with a combined fair value of $19,000 at December 31, 2010, which has been classified as other-than-temporarily impaired. During the year ended December 31, 2010, the Company recognized $4,500 of other-than-temporary impairment charges in the equity securities portfolio. Management believes that there are no additional other-than-temporary impairments in the equity securities portfolio at December 31, 2010; however, it is possible that the Company may incur impairment losses in 2011.

As of December 31, 2010, the Company did not have securities from a single issuer, except for the United States Government or its agencies, which exceeded 10% of consolidated stockholders' equity.

Table of Contents

Investment Maturities as of December 31, 2010

The investments in the following table are reported by contractual maturity. Expected maturities may differ from contractual maturities because issuers of the securities may have the right to call or prepay obligations with or without prepayment penalties.

(dollars in thousands)	Within one year	After one year but within five years	After five years but within ten years	After ten years	Total
U.S. treasury securities	$503	$—	$—	$—	$503
U.S. government agencies	3,186	68,905	14,548	773	87,412
U.S. government mortgage-backed securities	1,043	117,561	7,966	779	127,349
States and political subdivisions*	23,133	98,410	91,430	15,400	228,373
Corporate bonds	2,911	13,440	3,663	358	20,372
Total	$30,776	$298,316	$117,607	$17,310	$464,009
Weighted average yield					
U.S. treasury	5.19%	0.00%	0.00%	0.00%	5.19%
U.S. government agencies	4.58%	2.58%	2.29%	4.50%	2.62%
U.S government mortgage-backed securities	3.05%	3.97%	4.15%	5.41%	3.52%
States and political subdivisions*	3.98%	4.43%	5.16%	6.01%	4.83%
Corporate bonds	5.74%	5.00%	5.80%	0.00%	5.23%
Total	4.19%	3.85%	4.75%	5.88%	4.18%

*Yields on tax-exempt obligations of states and political subdivisions have been computed on a tax-equivalent basis.

Deposits

Total deposits equaled $743,862,000 and $722,164,000 as of December 31, 2010 and 2009, respectively. The increase of $21,698,000 can be attributed primarily to an increase in public funds. Also the mix of deposits has changed, as depositors have moced deposits to demand, NOW and money market from time deposit accounts. The deposit category seeing the largest balance increase was money market accounts.

The Company’s primary source of funds is customer deposits. The Company attempts to attract noninterest-bearing deposits, which are a low-cost funding source. In addition, the Banks offer a variety of interest-bearing accounts designed to attract both short-term and longer-term deposits from customers. Interest-bearing accounts earn interest at rates established by Bank management based on competitive market factors and the Company’s need for funds. While nearly 59% of the Banks’ certificates of deposit mature in the next year, it is anticipated that a majority of these certificates will be renewed. Rate sensitive certificates of deposits in excess of $100,000 are subject to somewhat higher volatility with regard to renewal volume as the Banks adjust rates based upon funding needs. In the event a substantial volume of certificates is not renewed, the Company has sufficient liquid assets and borrowing lines to fund

significant runoff. A sustained reduction in deposit volume would have a significant negative impact on the Company's operation and liquidity. The Company had $1,249,000 and $694,000 of brokered deposits as of December 31, 2010 and 2009, respectively.

Table of Contents

Average Deposits by Type

The following table sets forth the average balances for each major category of deposit and the weighted average interest rate paid for deposits during the years ended December 31, 2010, 2009 and 2008.

	2010		2009		2008	
(dollars in thousands)	Average Amount	Average Rate	Average Amount	Average Rate	Average Amount	Average Rate
Noninterest bearing demand deposits	$94,286	0.00 %	$84,245	0.00 %	$78,033	0.00 %
Interest bearing demand deposits	194,281	0.35 %	174,716	0.42 %	155,689	0.96 %
Money market deposits	154,264	0.37 %	147,782	0.54 %	134,295	1.53 %
Savings deposits	37,465	0.32 %	33,007	0.34 %	27,362	0.40 %
Time certificates < $100,000	147,453	2.09 %	157,749	2.84 %	170,223	3.88 %
Time certificates > $100,000	89,290	1.85 %	84,786	2.70 %	97,193	4.06 %
	$717,039		$682,285		$662,795	

Deposit Maturity

The following table shows the amounts and remaining maturities of time certificates of deposit that had balances of $100,000 and over as of December 31, 2010, 2009 and 2008.

(dollars in thousands)	2010	2009	2008
3 months or less	$17,160	$17,814	$18,808
Over 3 through 12 months	41,180	45,007	38,589
Over 12 through 36 months	29,210	20,752	20,987
Over 36 months	7,308	3,481	2,995
Total	$94,858	$87,054	$81,379

Borrowed Funds

Borrowed funds that may be utilized by the Company are comprised of Federal Home Loan Bank (FHLB) advances, federal funds purchased, Treasury, Tax, and Loan option notes, and repurchase agreements. Borrowed funds are an alternative funding source to deposits and can be used to fund the Company's assets and unforeseen liquidity needs. FHLB advances are loans from the FHLB that can mature daily or have longer maturities for fixed or floating rates of interest. Federal funds purchased are borrowings from other banks that mature daily. Securities sold under agreement to repurchase (repurchase agreements) are similar to deposits as they are funds lent by various Bank customers; however, investment securities are pledged to secure such borrowings. The Company has repurchase agreements that generally reprice daily. Term repurchase agreements are funds lent by a third party with securities pledged to secure such borrowings. These term repurchase agreements have longer terms. Treasury, Tax, and Loan option notes consist of short term borrowing of tax deposits from the federal government and are not a significant source of borrowing for the Company.

Table of Contents

The following table summarizes the outstanding amount of, and the average rate on, borrowed funds as of December 31, 2010, 2009 and 2008.

	2010		2009		2008	
(dollars in thousands)	Balance	Average Rate	Balance	Average Rate	Balance	Average Rate
Federal funds purchased and repurchase agreements	$ 54,859	0.63 %	$ 40,490	0.64 %	$ 38,510	1.30 %
Other short-term borrowings	2,047	0.00 %	139	0.00 %	1,064	0.00 %
FHLB advances	16,745	2.91 %	16,500	3.12 %	23,500	2.90 %
Term repurchase agreements	20,000	3.36 %	20,000	3.77 %	20,000	3.77 %
Total	$ 93,651	1.61 %	$ 77,129	1.98 %	$ 83,074	2.33 %

Table of Contents

Average Annual Borrowed Funds

The following table sets forth the average amount of, the average rate paid and maximum outstanding balance on, borrowed funds for the years ended December 31, 2010, 2009 and 2008.

(dollars in thousands)	2010 Average Balance	2010 Average Rate	2009 Average Balance	2009 Average Rate	2008 Average Balance	2008 Average Rate
Federal funds purchased and repurchase agreements	$ 49,300	0.66 %	$ 42,795	0.92 %	$ 40,340	2.11 %
Other short-term borrowings	610	0.00 %	616	0.00 %	689	1.89 %
FHLB advances	17,848	3.28 %	20,430	3.11 %	17,735	3.34 %
Term repurchase agreements	20,000	3.83 %	20,000	3.85 %	20,000	3.69 %
Total	$ 87,758	1.91 %	$ 83,841	2.14 %	$ 78,764	2.79 %
Maximum Amount Outstanding during the Year						
Federal funds purchased and repurchase agreements	$ 76,559		$ 50,493		$ 48,699	
Other short-term borrowings	$ 3,131		$ 3,053		$ 1,351	
FHLB advances	$ 18,500		$ 23,500		$ 23,500	
Term repurchase agreements	$ 20,000		$ 20,000		$ 20,000	

Off-Balance-Sheet Arrangements

The Company is party to financial instruments with off-balance-sheet risk in the normal course of business. These financial instruments include commitments to extend credit and standby letters of credit that assist customers with their credit needs to conduct business. The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheet. As of December 31, 2010, the most likely impact of these financial

instruments on revenues, expenses, or cash flows of the Company would come from unidentified credit risk causing higher provision expense for loan losses in future periods. These financial instruments are not expected to have a significant impact on the liquidity or capital resources of the Company. For additional information, see Note 11 of the "Notes to Consolidated Statements" and the "Liquidity and Capital Resources" section of this discussion.

Table of Contents

Contractual Obligations

The following table sets forth the balance of contractual obligations by maturity period as of December 31, 2010 (in thousands).

	Payments due by period				
Contractual Obligations	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Deposits	$ 743,862	$ 645,427	$ 77,312	$ 21,123	$ —
Federal funds purchased and securities sold under agreements to repurchase	54,859	54,859	—	—	—
Other short-term borrowings	2,047	2,047	—	—	—
FHLB advances and other long-term borrowings (1)	36,745	2,066	2,139	7,148	25,392
Operating lease obligation	35	8	16	11	—
Purchase obligations (2)	2,416	672	1,344	400	—
Total	$ 839,964	$ 705,079	$ 80,811	$ 28,682	$ 25,392

(1) FHLB advances and other long-term borrowings consist of various FHLB borrowings with fixed rates with final maturities through 2025. Other long-term borrowings consist of term repurchase agreements having maturities greater than one year and can be called by the issuing financial institution with final maturities through 2018.
(2) Purchase obligations include data processing and Internet banking services contracts that include termination provisions that would accelerate all future payments in the event the Company changed service providers prior to the contracts' expirations.

Asset Quality Review and Credit Risk Management

The Company's credit risk is centered in the loan portfolio, which on December 31, 2010, totaled $418,094,000 as compared to $415,434,000 as of December 31, 2009, an increase of 0.6%. Net loans comprise 43% of total assets as of the end of 2010. The object in managing loan portfolio risk is to reduce the risk of loss resulting from a customer's failure to perform according to the terms of a transaction and to quantify and manage credit risk on a portfolio basis. As the following chart indicates, the Company's non-performing assets have decreased and total $17,214,000 as of December 31, 2010. The Company's level of problem assets as a percentage of assets of 1.79% as of December 31, 2010, is lower than the average for FDIC insured institutions as of December 31, 2010, of 3.11%. Management believes that the allowance for loan losses remains adequate based on its analysis of the non-performing assets and the portfolio as a whole.

Table of Contents

Non-performing Assets

The following table sets forth information concerning the Company's non-performing assets for the past five years ended December 31, 2010.

(dollars in thousands)	2010	2009	2008	2007	2006
Non-performing assets:					
Nonaccrual loans	$6,277	$10,187	$6,339	$3,249	$291
Loans 90 days or more past due	21	121	469	1,300	758
Total non-performing loans	6,298	10,308	6,808	4,549	1,049
Securities available-for-sale	377	660	358	—	—
Other real estate owned	10,539	10,480	13,334	2,846	2,808
Total non-performing assets	$17,214	$21,448	$20,500	$7,395	$3,857

The accrual of interest on non-accrual and other impaired loans is discontinued at 90 days or when, in the opinion of management, the borrower may be unable to meet payments as they become due. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received and principal obligations are expected to be recoverable. Interest income on restructured loans is recognized pursuant to the terms of the new loan agreement. Interest income on other impaired loans is monitored and based upon the terms of the underlying loan agreement. However, the recorded net investment in impaired loans, including accrued interest, is limited to the present value of the expected cash flows of the impaired loan or the observable fair value of the loan's collateral.

At December 31, 2010 and 2009, the Company had non-performing loans of approximately $6,298,000 and $10,308,000, respectively. The economic conditions for commercial real estate developers in the Des Moines metropolitan area deteriorated in 2009 and 2008 and contributed to the Company's increased level of non-performing loans, other real estate owned and related costs in 2009 and 2008. In 2010, there were no significant additional impaired loans in the Des Moines market. During the year ended December 31, 2010, the Company foreclosed on one real estate property (other real estate owned) totaling $402,000 in the Des Moines market. Presently, the Company has $2.9 million in impaired loans with two Des Moines development companies with specific reserves totaling $223,000. The Company has additional customer relationships with real estate developers in the Des Moines area that may become impaired in the future if economic conditions do not improve or become worse. The Company has a limited number of such credits and is actively engaged with the customers to minimize credit risk.

Impaired loans totaled $6,432,000 as of December 31, 2010 and were $3,755,000 lower than the impaired loans as of December 31, 2009. The Company considers impaired loans to generally include the non-performing loans (consisting of nonaccrual loans and loans past due 90 days or more and still accruing) and other loans that may or may not meet the former nonperforming criteria but are considered to meet the definition of impaired.

Table of Contents

The allowance for loan losses related to these impaired loans was approximately $445,000 and $999,000 at December 31, 2010 and 2009, respectively. The average balances of impaired loans for the years ended December 31, 2010 and 2009 were $7,095,000 and $8,498,000, respectively. For the years ended December 31, 2010, 2009 and 2008, interest income, which would have been recorded under the original terms of such loans, was approximately $425,000, $564,000 and $478,000, respectively, with $233,000, $32,000 and $155,000, respectively, recorded. Loans greater than 90 days past due and still accruing interest were approximately $21,000 and $121,000 at December 31, 2010 and 2009, respectively.

Summary of the Allowance for Loan Losses

The provision for loan losses represents an expense charged against earnings to maintain an adequate allowance for loan losses. The allowance for loan losses is management's best estimate of probable losses inherent in the loan portfolio as of the balance sheet date. Factors considered in establishing an appropriate allowance include: an assessment of the financial condition of the borrower; a realistic determination of value and adequacy of underlying collateral; historical charge offs; the condition of the local economy; the condition of the specific industry of the borrower; an analysis of the levels and trends of loan categories; and a review of delinquent and classified loans.

The adequacy of the allowance for loan losses is evaluated quarterly by management and the respective Bank boards. This evaluation focuses on specific loan reviews, changes in the type and volume of the loan portfolio given the current economic conditions and historical loss experience. Any one of the following conditions may result in the review of a specific loan: concern about whether the customer's cash flow or collateral are sufficient to repay the loan; delinquent status; criticism of the loan in a regulatory examination; the accrual of interest has been suspended; or other reasons, including when the loan has other special or unusual characteristics which warrant special monitoring.

While management uses available information to recognize losses on loans, further reductions in the carrying amounts of loans may be necessary based on changes in local economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the estimated losses on loans. Such agencies may require the Company to recognize additional losses based on their judgment about information available to them at the time of their examination. Due to potential changes in conditions, it is at least reasonably possible that changes in estimates will occur in the near term and that such changes could be material to the amounts reported in the Company's financial statements.

Analysis of the Allowance for Loan Losses

The Company's policy is to charge-off loans when, in management's opinion, the loan is deemed uncollectible, although concerted efforts are made to maximize future recoveries. The following table sets forth information regarding changes in the Company's allowance for loan losses for the most recent five years.

Table of Contents

(dollars in thousands)	2010	2009	2008	2007	2006
Balance at beginning of period	$ 7,652	$ 6,779	$ 5,781	$ 6,533	$ 6,765
Charge-offs:					
Real estate					
Construction	22	105	76	402	—
1-4 Family residential	163	155	89	1	6
Commercial	20	415	70	25	—
Agricultural	50	15	—	—	—
Commercial	391	54	77	—	—
Agricultural	42	—	—	—	—
Consumer and other	179	122	115	299	99
Total charge-offs	867	866	427	727	105
Recoveries:					
Real estate					
Construction	—	6	—	—	—
1-4 Family residential	1	27	3	1	1
Commercial	—	98	1	—	—
Agricultural	—	—	—	—	—
Commercial	5	3	35	21	6
Agricultural	32	—	—	—	—
Consumer and other	34	47	73	47	49
Total recoveries	72	181	112	69	56
Net charge-offs	795	685	315	658	49
Provisions charged (credited) to operations	664	1,558	1,313	(94)	(183)
Balance at end of period	$ 7,521	$ 7,652	$ 6,779	$ 5,781	$ 6,533
Average loans outstanding	$ 417,688	$ 434,468	$ 463,782	$ 454,088	$ 438,166
Ratio of net charge-offs during the period to average loans outstanding	0.19 %	0.16 %	0.07 %	0.14 %	0.01 %
Ratio of allowance for loan losses to total loans net of deferred fees	1.77 %	1.81 %	1.47 %	1.23 %	1.50 %

Table of Contents

The allowance for loan losses decreased to $7,521,000 at the end of 2010 in comparison to the allowance of $7,652,000 at year end 2009 as a result of net charge offs of $795,000, offset in part by provisions in 2010 in the amount of $664,000. The lower provision for loan losses in 2010 as compared to 2009 was due primarily to a lower provision for loan losses on impaired loans for the year ended December 31, 2010 as compared to the year ended December 31, 2009. The allowance for loan losses increased to $7,652,000 at the end of 2009 in comparison to the allowance of $6,779,000 at year end 2008 as a result of provisions in 2009 in the amount of $1,558,000 offset by net charge offs of $685,000. The increase in the provision for loan losses was due primarily to an increase in factors related to weakening economic conditions and an increase in the specific reserve on impaired loans, offset in part by a decrease in the loan portfolio. The allowance for loan losses increased to $6,779,000 at the end of 2008 in comparison to the allowance of $5,781,000 at year end 2007 as a result of provisions in 2008 in the amount of $1,313,000 offset by net charge offs of $315,000. The increase in the provision for loan losses was due primarily to an increase in factors related to weakening economic conditions and an increase in the level of risks associated with the construction and commercial real estate loan portfolios. The allowance for loan losses decreased to $5,781,000 at the end of 2007 in comparison to the allowance of $6,533,000 at year end 2006 as a result of net charge-offs of $658,000 in 2007 and a reduction in specific reserves for problem credits.

General reserves for loan categories normally range from 1.08% to 2.10% of the outstanding loan balances. As loan volume increases, the general reserve levels increase with that growth and as loan volume decreases, the general reserve levels decrease with that decline. The loan provisions recognized in 2010 were due primarily to a continuing weakness in the economic conditions and an increase in the loan portfolio. The loan provisions recognized in 2009 were due primarily to weakening economic conditions and an increase in the specific reserve on impaired loans, offset in part by a decrease in the loan portfolio. The loan provisions recognized in 2008 were due primarily to weakening economic conditions and an increase in the level of risks associated with the construction and commercial real estate loan portfolios. The allowance relating to commercial real estate, 1-4 family residential and commercial loans are the largest reserve components. Construction and commercial real estate loans have higher general reserve levels than 1-4 family and agricultural real estate loans as management perceives more risk in this type of lending. Elements contributing to the higher risk level include a higher percentage of watch and problem loans, higher past due percentages, declining collateral values and less favorable economic conditions for those portfolios. As of December 31, 2010, commercial real estate loans have general reserves ranging from 1.42% to 1.78%. The level of non-performing loans as of December 31, 2010 has decreased since 2009 and remains at a manageable level.

Loans that the Banks have identified as having higher risk levels are reviewed individually in an effort to establish adequate loss reserves. These reserves are considered specific reserves and are directly impacted by the credit quality of the underlying loans. Normally, as the actual or expected level of non-performing loans increase, the specific reserves also increase. For December 31, 2010, the specific reserve decreased to $445,000 from $999,000, as the volume of problem credits decreased and economic conditions stabilized.

As of December 31, 2009, the specific reserve increased to $999,000 from $257,000 at the prior year end, as the volume of problem credits increased and economic conditions worsened. As of December 31, 2008, the specific reserve increased to $257,000 from $247,000 at the prior year end, as the volume of problem credits increased in 2008. As of December 31, 2007, specific reserves decreased to $247,000 from $1,477,000 reserved at year end 2006, in part, due to the charge-off of credits with specific reserves, an improved condition of certain credits and a change in the Company's method of determining specific reserves. The revised methodology resulted from implementing guidance provided by federal regulatory agencies. As of December 31, 2006, specific reserves increased $534,000 or 2% compared to year end 2005 levels as the volume of problem credits increased in 2006. The specific reserves are dependent upon assumptions regarding the liquidation value of collateral and the cost of recovering collateral including legal fees. Changing the amount of specific reserves on individual loans has historically had the largest impact on the reallocation of the reserve among different parts of the portfolio.

Table of Contents

Other factors considered when determining the adequacy of the reserve include historical losses; watch, substandard and impaired loan volume; collecting past due loans; loan growth; loan to value ratios; loan administration; collateral values; and economic factors. The Company's concentration risks include geographic concentration in central Iowa; the local economy's dependence upon several large governmental entity employers, including Iowa State University and the Iowa Department of Transportation; and the health of Iowa's agricultural sector that, in turn, is dependent on weather conditions and government programs. However, no assurances can be made that losses will remain at the relatively favorable levels experienced over the past five years.

Allocation of the Allowance for Loan Losses

The following table sets forth information concerning the Company's allocation of the allowance for loan losses.

(dollars in thousands)	2010		2009		2008		2007		2006	
	Amount	%*	Amount	%*	Amount	%*	Amount	%*	Amount	%*
Balance at end of period applicable to:										
Real Estate										
Construction	$ 731	5 %	$ 1,040	5 %	$ 472	8 %	$ 733	10 %	$ 372	7 %
1-4 family residential	1,404	21 %	1,133	22 %	1,001	21 %	1,061	22 %	1,231	24 %
Commercial	2,720	33 %	2,683	34 %	3,566	33 %	1,964	31 %	2,396	32 %
Agricultural	486	7 %	523	7 %	395	7 %	407	7 %	428	7 %
Commercial	1,152	18 %	1,199	16 %	683	17 %	943	17 %	983	17 %
Agricultural	735	11 %	642	10 %	469	9 %	466	8 %	499	8 %
Consumer and other	293	5 %	432	6 %	193	5 %	207	5 %	276	5 %
Unallocated	—		—		—		—		348	
	$ 7,521	100 %	$ 7,652	100 %	$ 6,779	100 %	$ 5,781	100 %	$ 6,533	100 %

* Percent of loans in each category to total loans.

Liquidity and Capital Resources

Liquidity management is the process by which the Company, through its Banks' Asset and Liability Committees (ALCO), ensures adequate liquid funds are available to meet its financial commitments on a timely basis, at a reasonable cost and within acceptable risk tolerances. These commitments include funding credit obligations to borrowers, funding of mortgage originations pending delivery to the secondary market, withdrawals by depositors, maintaining adequate collateral for pledging for public funds, trust deposits and borrowings, paying dividends to shareholders, payment of operating expenses, funding capital expenditures and maintaining deposit reserve requirements.

Table of Contents

Liquidity is derived primarily from core deposit growth and retention; principal and interest payments on loans; principal and interest payments, sale, maturity and prepayment of investment securities; net cash provided from operations; and access to other funding sources. Other funding sources include federal funds purchased lines, Federal Home Loan Bank (FHLB) advances and other capital market sources.

As of December 31, 2010, the level of liquidity and capital resources of the Company remain at a satisfactory level and compare favorably to that of other FDIC insured institutions. Management believes that the Company's liquidity sources will be sufficient to support its existing operations for the foreseeable future.

The liquidity and capital resources discussion will cover the following topics:

- Review of the Company's Current Liquidity Sources
- Review of the Consolidated Statements of Cash Flows
- Review of Company Only Cash Flows
- Review of Commitments for Capital Expenditures, Cash Flow Uncertainties and Known Trends in Liquidity and Cash Flow Needs
- Capital Resources

Review of the Company's Current Liquidity Sources

Liquid assets of cash on hand, balances due from other banks, federal funds sold and interest-bearing deposits in financial institutions for December 31, 2010, 2009 and 2008 totaled $37,708,000, $43,573,000 and $51,631,000, respectively. The lower balance of liquid assets as of December 31, 2010 primarily relates to a decrease in interest bearing deposits in financial institutions, offset in part by an increased level of federal funds sold. The lower balance of liquid assets as of December 31, 2009 relates to a decreased level of federal funds sold, offset in part by an increase in interest bearing deposits in financial institutions.

Other sources of liquidity available to the Banks include total borrowing capacity with the FHLB of $54,208,000 and federal funds borrowing capacity at correspondent banks of $107,188,000. As of December 31, 2010, the Company had outstanding FHLB advances of $16,745,000, Treasury Tax and Loan option notes of $2,047,000, federal funds purchased of $500,000 and securities sold under agreement to repurchase daily and term of $54,359,000 and $20,000,000, respectively.

Total investments as of December 31, 2010, were $469,908,000 compared to $418,655,000 as of year end 2009. As of December 31, 2010 and 2009, the investment portfolio as a percentage of total assets was 49% and 46%, respectively. This provides the Company with a significant amount of liquidity since all investments are classified as available-for-sale as of December 31, 2010 and 2009 and have pretax net unrealized gains of $5,280,000 and $4,951,000, respectively.

The investment portfolio serves an important role in the overall context of balance sheet management in terms of balancing capital utilization and liquidity. The decision to purchase or sell securities is based upon the current assessment of economic and financial conditions, including the interest rate environment, liquidity and credit considerations. The portfolio's scheduled maturities represent a significant source of liquidity.

Table of Contents

Review of the Consolidated Statements of Cash Flows

Operating cash flows for the years ended December 31, 2010, 2009 and 2008 totaled $16,822,000, $11,400,000 and $12,722,000, respectively. The increase in operating cash flows in 2010 as compared to 2009 was primarily due to the changes in net income, other assets and amortization and accretion, net, offset in part by changes in impairment of other real estate owned, accrued interest receivables and loans held for sale. The decrease in operating cash flows in 2009 as compared to 2008 was primarily due to the effect of other-than-temporary impairment in investment securities and an increase in other assets, offset in part by changes in net income, deferred income taxes, impairment of other real estate owned and securities gains.

Net cash used in investing activities for the years ended December 31, 2010, 2009 and 2008 was $54,305,000, $63,254,000 and $6,648,000, respectively. The decrease in net cash used in investing activities in 2010 was primarily due to changes in investments and interest bearing deposits in financial institutions, offset in part by changes in loans and federal funds sold. The increase in net cash used in investing activities in 2009 was primarily due to an increase in investment purchases, offset in part by a decrease in loans and federal funds sold.

Net cash provided by (used in) financing activities for the years ended December 31, 2010, 2009 and 2008 totaled $34,165,000, $45,953,000 and ($7,421,000), respectively. The decrease in net cash provided by financing activities in 2010 was due primarily to changes in deposits, offset in part by changes in borrowed funds and federal funds purchased and securities sold under agreements to repurchase. The change in net cash provided by financing activities in 2009 was due primarily to an increase in deposits, offset in part by the change in borrowed funds and federal funds purchased and securities sold under agreements to repurchase. As of December 31, 2010, the Company did not have any external debt financing, off balance sheet financing arrangements or derivative instruments linked to its stock.

Review of Company Only Cash Flows

The Company's liquidity on an unconsolidated basis is heavily dependent upon dividends paid to the Company by the Banks. The Company requires adequate liquidity to pay its expenses and pay stockholder dividends. In 2010, dividends from the Banks amounted to $3,900,000 compared to $3,560,000 in 2009. Various federal and state statutory provisions limit the amount of dividends banking subsidiaries are permitted to pay to their holding companies without regulatory approval. Federal Reserve policy further limits the circumstances under which bank holding companies may declare dividends. For example, a bank holding company should not continue its existing rate of cash dividends on its common stock unless its net income is sufficient to fully fund each dividend and its prospective rate of earnings retention appears consistent with its capital needs, asset quality and overall financial condition. In addition, the Federal Reserve and the FDIC have issued policy statements which provide that insured banks and bank holding companies should generally pay dividends only out of current operating earnings. Federal and state banking regulators may also restrict the payment of dividends by order.

First National and United Bank, as national banks, generally may pay dividends, without obtaining the express approval of the Office of the Comptroller of the Currency ("OCC"), in an amount up to their retained net profits for the preceding two calendar years plus retained net profits up to the date of any dividend declaration in the current calendar year. Retained net profits, as defined by the OCC, consists of net income less dividends declared during the period. Boone Bank, Randall-Story Bank and State Bank are also restricted under Iowa law to paying dividends only out of their undivided profits. Additionally, the payment of dividends by the Banks is affected by the requirement to maintain adequate capital pursuant to applicable capital adequacy guidelines and regulations, and the Banks generally are prohibited from paying any dividends if, following payment thereof, the Bank would be undercapitalized.

Table of Contents

The Company has unconsolidated cash, interest bearing deposits and marketable investment securities totaling $12,354,000 that were available at December 31, 2010 to provide additional liquidity to the Banks.

Review of Commitments for Capital Expenditures, Cash Flow Uncertainties and Known Trends in Liquidity and Cash Flow Needs

No material capital expenditures or material changes in the capital resource mix are anticipated at this time. Commitments to extend credit totaled $79,757,000 as of December 31, 2010 compared to a total of $73,976,000 at the end of 2009. The timing of these credit commitments varies with the underlying borrowers; however, the Company has satisfactory liquidity to fund these obligations as of December 31, 2010. The primary cash flow uncertainty would be a sudden decline in deposits causing the Banks to liquidate securities. Historically, the Banks have maintained an adequate level of short term marketable investments to fund the temporary declines in deposit balances. There are no known trends in liquidity and cash flow needs as of December 31, 2010, that are of concern to management.

Capital Resources

The Company's total stockholders' equity increased to $121,363,000 at December 31, 2010, from $112,340,000 at December 31, 2009. At December 31, 2010 and 2009, stockholders' equity as a percentage of total assets was 12.6% and 12.3%, respectively. Total equity increased primarily due to net income and appreciation in the Company's investment portfolio, offset in part by dividends declared. The capital levels of the Company currently exceed applicable regulatory guidelines as of December 31, 2010.

Interest Rate Risk

Interest rate risk refers to the impact that a change in interest rates may have on the Company's earnings and capital. Management's objectives are to control interest rate risk and to ensure predictable and consistent growth of earnings and capital. Interest rate risk management focuses on fluctuations in net interest income identified through computer simulations to evaluate volatility, varying interest rate, spread and volume assumptions. The risk is quantified and compared against tolerance levels.

The Company uses a third-party computer software simulation modeling program to measure its exposure to potential interest rate changes. For various assumed hypothetical changes in market interest rates, numerous other assumptions are made such as prepayment speeds on loans, the slope of the Treasury yield curve, the rates and volumes of the Company's deposits and the rates and volumes of the Company's loans. This analysis measures the estimated change in net interest income in the event of hypothetical changes in interest rates.

Table of Contents

Another measure of interest rate sensitivity is the gap ratio. This ratio indicates the amount of interest-earning assets repricing within a given period in comparison to the amount of interest-bearing liabilities repricing within the same period of time. A gap ratio of 1.0 indicates a matched position, in which case the effect on net interest income due to interest rate movements will be minimal. A gap ratio of less than 1.0 indicates that more liabilities than assets reprice within the time period, while a ratio greater than 1.0 indicates that more assets reprice than liabilities.

The simulation model process provides a dynamic assessment of interest rate sensitivity, whereas a static interest rate gap table is compiled as of a point in time. The model simulations differ from a traditional gap analysis, as a traditional gap analysis does not reflect the multiple effects of interest rate movement on the entire range of assets and liabilities and ignores the future impact of new business strategies.

Inflation

The primary impact of inflation on the Company’s operations is to increase asset yields, deposit costs and operating overhead. Unlike most industries, virtually all of the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates generally have a more significant impact on a financial institution’s performance than they would on non-financial companies. Although interest rates do not necessarily move in the same direction or to the same extent as the price of goods and services, increases in inflation generally have resulted in increased interest rates. The effects of inflation can magnify the growth of assets and, if significant, require that equity capital increase at a faster rate than would be otherwise necessary.

Forward-Looking Statements and Business Risks

Certain statements contained in the foregoing Management’s Discussion and Analysis and elsewhere in this Annual Report that are not statements of historical fact constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (the “Act”), notwithstanding that such statements are not specifically identified. In addition, certain statements may be contained in the Company’s future filings with the SEC, in press releases and in oral and written statements made by or with the Company’s approval that are not statements of historical fact and constitute forward-looking statements within the meaning of the Act. Examples of forward-looking statements include, but are not limited to: (i) projections of revenues, expenses, income or loss, earnings or loss per share, the payment or nonpayment of dividends, capital structure and other financial items; (ii) statements of plans, objectives and expectations of the Company or its management, including those relating to products or services; (iii) statements of future economic performance; and (iv) statements of assumptions underlying such statements. Words such as “believes”, “anticipates”, “expects”, “intends”, “targeted”, “projected”, “continue”, “remain”, “will”, “should”, “ similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

Forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from those in such statement. Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to:

Local, regional and national economic conditions and the impact they may have on the Company and its customers, and management’s assessment of that impact on our estimates including, but not limited to, the allowance for loan losses and fair value of other real estate owned. Of particular relevance are the economic conditions in the concentrated geographic area in central Iowa in which the Banks conduct their operations.

Table of Contents

Changes in the level of nonperforming assets and charge-offs.

Changes in the fair value of securities available-for-sale and management's assessments of other-than-temporary impairment of such securities.

The effects of and changes in trade and monetary and fiscal policies and laws, including the changes in assessment rates established by the Federal Deposit Insurance Corporation for its Deposit Insurance Fund and interest rate policies of the Federal Open Market Committee of the Federal Reserve Board.

Changes in sources and uses of funds, including loans, deposits and borrowings, including the ability of the Banks to maintain unsecured federal funds lines with correspondent banks.

Changes imposed by regulatory agencies to increase capital to a level greater than the level required for well-capitalized financial institutions.

Inflation and interest rate, securities market and monetary fluctuations.

Political instability, acts of war or terrorism and natural disasters.

The timely development and acceptance of new products and services and perceived overall value of these products and services by customers.

Revenues being lower than expected.

Changes in consumer spending, borrowings and savings habits.

Changes in the financial performance and/or condition of the Company's borrowers.

Credit quality deterioration, which could cause an increase in the provision for loan losses.

Technological changes.

The ability to increase market share and control expenses.

Changes in the competitive environment among financial or bank holding companies and other financial service providers.

The effect of changes in laws and regulations with which the Company and the Banks must comply, including developments and changes related to the implementation of the recently-enacted Dodd-Frank Act.

Changes in the securities markets.

Table of Contents

The effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard setters, including the International Financial Reporting Standards.

The costs and effects of legal and regulatory developments, including the resolution of regulatory or other governmental inquiries and the results of regulatory examinations or reviews.

The Company's success at managing the risks involved in the foregoing items.

Certain of the foregoing risks and uncertainties are discussed in greater detail under the heading "Risk Factors" in Item 1A herein.

These factors may not constitute all factors that could cause actual results to differ materially from those discussed in any forward-looking statement. The Company operates in a continually changing business environment and new facts emerge from time to time. It cannot predict such factors nor can it assess the impact, if any, of such factors on its financial position or its results of operations. Accordingly, forward-looking statements should not be relied upon as a predictor of actual results. The Company disclaims any responsibility to update any forward-looking statement provided in this document.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's market risk is comprised primarily of interest rate risk arising from its core banking activities of making loans and taking deposits. Interest rate risk is the risk that changes in market interest rates may adversely affect the Company's net interest income. Management continually develops and applies strategies to mitigate this risk. Management does not believe that the Company's primary market risk exposure and how that exposure was managed in 2010 changed when compared to 2009.

Based on a simulation modeling analysis performed as of December 31, 2010, the following table presents the estimated change in net interest income in the event of hypothetical changes in interest rates for the various rate shock levels:

Net Interest Income at Risk

Estimated Change in Net Interest Income for Year Ending December 31, 2010

(dollars in thousands)	$ Change	% Change
+300 Basis Points	$(3,783)	-12.13%
+200 Basis Points	(2,180)	-6.99%
+100 Basis Points	(836)	-2.68%
-100 Basis Points	(2,027)	-6.50%
-200 Basis Points	(4,004)	-12.84%

Table of Contents

As shown above, at December 31, 2010, the estimated effect of an immediate 300 basis point increase in interest rates would decrease the Company's net interest income by 12.13% or approximately $3,783,000 in 2011. In the increasing interest rate environment, the assets are repricing slower than the liabilities, thus a decrease in net interest income. The estimated effect of an immediate 200 basis point decrease in rates would decrease the Company's net interest income by 12.84% or approximately $4,004,000 in 2011. In a decreasing interest rate environment, a portion of the liabilities are not repricing downward due to their already historically low rates, thus a decrease in net interest income. The Company's Asset Liability Management Policy establishes parameters for a 200 basis point change in interest rates. Under this policy, the Company and the Banks' objective is to properly structure the balance sheet to prevent a 200 basis point change in interest rates from causing a decline in net interest income by more than 15% in one year compared to the base year that hypothetically assumes no change in interest rates.

Computations of the prospective effects of hypothetical interest rate changes are based on numerous assumptions. Actual values may differ from those projections set forth above. Further, the computations do not contemplate any actions the Company may undertake in response to changes in interest rates. Current interest rates on certain liabilities are at a level that does not allow for significant repricing should market interest rates decline considerably.

Contractual Maturity or Repricing

The following table sets forth the estimated maturity or re-pricing, and the resulting interest sensitivity gap, of the Company's interest-earning assets and interest-bearing liabilities and the cumulative interest sensitivity gap at December 31, 2010. The expected maturities are presented on a contractual basis. Actual maturities may differ from contractual maturities because of prepayment assumptions, early withdrawal of deposits and competition.

Table of Contents

(dollars in thousands)	Less than three months	Three months to one year	One to five years	Over five years	Cumulative Total
Interest - earning assets					
Interest-bearing deposits and federal funds sold	$6,370	$3,085	$12,775	$—	$22,230
Investments (1)	6,051	24,725	298,316	140,816	469,908
Loans	63,542	73,125	235,402	53,617	425,686
Loans held for sale	1,993	—	—	—	1,993
Total interest - earning assets	$77,956	$100,935	$546,493	$194,433	$919,817
Interest - bearing liabilities					
Interest bearing demand deposits	$201,231	$—	$—	$—	$201,231
Money market and savings deposits	199,017	—	—	—	199,017
Time certificates < $100,000	24,663	56,493	61,937	—	143,093
Time certificates > $100,000	17,160	41,180	36,518	—	94,858
Other borrowed funds (2)	3,064	1,050	9,287	25,392	38,793
Total interest - bearing liabilities	$445,135	$98,723	$107,742	$25,392	$676,992
Interest sensitivity gap	$(367,179)	$2,212	$438,751	$169,041	$242,825
Cumulative interest sensitivity gap	$(367,179)	$(364,967)	$73,784	$242,825	$242,825
Cumulative interest sensitivity gap as a percent of total assets	-38.13%	-37.90%	7.66%	25.22%	

(1) Investments with maturities over 5 years include the market value of equity securities of $5,899.
(2) Includes $16.8 million of advances from the FHLB. Of these advances, $4.0 million are term advances, $11.5 million are callable and $1.2 million are 15 year amortizing. The term advances have been categorized based upon their maturity date. The $11.5 million of callable advances were also categorized based upon maturity, because the interest rates on such advances are near or above current market rates. The $1.2 million of amortizing advances are included in their final maturity date. Includes $20.0 million of term repurchase agreements, of which $13.0 million are callable. The callable repurchase agreements were categorized based upon maturity, because the interest rates on such advances are near or above current market rates.

As of December 31, 2010, the Company's cumulative gap ratios for assets and liabilities repricing within three months and within one year were a negative 38% and 38%, respectively, meaning more liabilities than assets are scheduled to reprice within these periods. This situation suggests that a decrease in market interest rates may benefit net interest income and that an increase in interest rates may negatively impact the Company. The liability sensitive gap position is largely the result of classifying the interest bearing NOW accounts, money market accounts and savings accounts as immediately repriceable. Certain shortcomings are inherent in the method of analysis presented in the foregoing table. For example, although certain assets and liabilities may have similar maturities and periods to repricing, they may react differently to changes in market interest rates. Also, interest rates on assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other assets and liabilities may follow changes in market interest rates. Additionally, certain assets have features that restrict changes in the interest rates of such assets, both on a short-term basis and over the lives of such assets.

66

Table of Contents

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Ames National Corporation is responsible for establishing and maintaining adequate internal control over financial reporting. Ames National Corporation's internal control system was designed to provide reasonable assurance to the Company's management and board of directors regarding the preparation and fair presentation of published financial statements. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Ames National Corporation's management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2010. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework. Based on our assessment we determined that, as of December 31, 2010, the Company's internal control over financial reporting is effective based on those criteria.

The Company's internal control over financial reporting as of December 31, 2010 has been audited by Clifton Gunderson LLP, an independent registered public accounting firm, as stated in their report which appears herein.

/s/ Thomas H. Pohlman
Thomas H. Pohlman, President
(Principal Executive Officer)

/s/ John P. Nelson
John P. Nelson, Vice President
(Principal Financial Officer)

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors
Ames National Corporation
Ames, Iowa

We have audited the accompanying consolidated balance sheets of Ames National Corporation and subsidiaries as of December 31, 2010 and 2009, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2010. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion of these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). 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 Ames National Corporation and subsidiaries as of December 31, 2010 and 2009, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2010 in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Ames National Corporation and subsidiaries' internal control over financial reporting as of December 31, 2010, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 10, 2011 expressed an unqualified opinion.

West Des Moines, Iowa
March 10, 2011

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors
Ames National Corporation
Ames, Iowa

We have audited Ames National Corporation and subsidiaries' internal control over financial reporting as of December 31, 2010, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Ames National Corporation's management is responsible for maintaining effective internal control over the financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Table of Contents

In our opinion, Ames National Corporation and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2010, based upon criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Ames National Corporation and subsidiaries as of December 31, 2010 and 2009, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2010 and our report dated March 10, 2011 expressed an unqualified opinion.

West Des Moines, Iowa
March 10, 2011

Table of Contents

AMES NATIONAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
December 31, 2010 and 2009

ASSETS	2010	2009
Cash and due from banks	$15,478,133	$18,796,664
Federal funds sold	3,000,000	—
Interest bearing deposits in financial institutions	19,229,814	24,776,088
Securities available-for-sale	469,907,901	418,655,018
Loans receivable, net	418,093,571	415,434,236
Loans held for sale	1,993,108	1,023,200
Bank premises and equipment, net	11,538,588	11,909,404
Accrued income receivable	6,098,535	5,710,226
Deferred income taxes	3,305,983	3,867,523
Other real estate owned	10,538,883	10,480,449
Other assets	3,790,329	4,916,991
Total assets	$962,974,845	$915,569,799
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Deposits		
Demand, noninterest bearing	$105,513,143	$99,918,848
NOW accounts	201,230,880	197,393,459
Savings and money market	199,017,213	184,631,343
Time, $100,000 and over	94,858,053	87,054,194
Other time	143,242,355	153,166,105
Total deposits	743,861,644	722,163,949
Federal funds purchased and securities sold under agreements to repurchase	54,858,701	40,489,505
Other short-term borrowings	2,047,175	138,874
Federal Home Loan Bank advances	16,745,497	16,500,000
Other long-term borrowings	20,000,000	20,000,000
Dividend payable	1,037,621	943,292
Accrued expenses and other liabilities	3,061,183	2,994,291
Total liabilities	841,611,821	803,229,911
STOCKHOLDERS' EQUITY		
Common stock, $2 par value, authorized 18,000,000 shares; 9,432,915 shares issued and outstanding	18,865,830	18,865,830
Additional paid-in capital	22,651,222	22,651,222
Retained earnings	76,519,493	67,703,701
Accumulated other comprehensive income-net unrealized gain on securities available-for-sale	3,326,479	3,119,135
Total stockholders' equity	121,363,024	112,339,888

Total liabilities and stockholders’ equity	$962,974,845	$915,569,799

See Notes to Consolidated Financial Statements.

Table of Contents

AMES NATIONAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME
Years Ended December 31, 2010, 2009 and 2008

	2010	2009	2008
Interest and dividend income:			
Loans, including fees	$24,061,277	$25,212,884	$29,458,407
Securities:			
Taxable	6,964,979	7,966,594	9,812,614
Tax-exempt	5,778,722	5,213,031	5,879,215
Interest bearing deposits and federal funds sold	488,980	498,798	363,931
Total interest and dividend income	37,293,958	38,891,307	45,514,167
Interest expense:			
Deposits	6,096,504	8,428,163	14,207,734
Other borrowed funds	1,678,587	1,798,149	2,193,958
Total interest expense	7,775,091	10,226,312	16,401,692
Net interest income	29,518,867	28,664,995	29,112,475
Provision for loan losses	663,798	1,558,307	1,312,785
Net interest income after provision for loan losses	28,855,069	27,106,688	27,799,690
Noninterest income (loss):			
Trust department income	1,948,519	1,541,831	1,597,096
Service fees	1,626,352	1,814,925	1,791,713
Securities gains, net	977,512	1,186,912	3,515,323
Other-than-temporary impairment of investment securities	(4,500)	(29,565)	(12,054,387)
Gain on sale of loans held for sale	942,826	1,008,566	834,129
Merchant and ATM fees	724,725	621,316	616,802
Other	720,404	780,275	690,898
Total noninterest income (loss)	6,935,838	6,924,260	(3,008,426)
Noninterest expense:			
Salaries and employee benefits	10,826,307	10,757,475	10,572,597
Data processing	1,857,259	1,892,123	2,246,473
Occupancy expenses	1,488,100	1,436,485	1,587,076
FDIC insurance assessments	1,120,058	1,675,401	242,906
Other real estate owned	194,645	4,198,315	151,428
Other operating expenses, net	2,834,212	2,772,556	2,793,774
Total noninterest expense	18,320,581	22,732,355	17,594,254
Income before income taxes	17,470,326	11,298,593	7,197,010
Provision for income taxes	4,504,052	2,292,807	845,014

Net income	$12,966,274	$9,005,786	$6,351,996
Basic and diluted earnings per share	$1.37	$0.95	$0.67

See Notes to Consolidated Financial Statements.

Table of Contents

AMES NATIONAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Years Ended December 31, 2010, 2009 and 2008

	Comprehensive Income	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance, December 31, 2007		$ 18,859,160	$ 22,588,691	$ 66,683,016	$ 1,889,656	$ 110,020,523
Comprehensive income:						
Net income	$ 6,351,996	—	—	6,351,996	—	6,351,996
Other comprehensive income, unrealized losses on securities, net of reclassification adjustment, net of tax	(2,040,339)	—	—	—	(2,040,339)	(2,040,339)
Total comprehensive income	$ 4,311,657					
Cash dividends declared, $1.12 per share		—	—	(10,563,931)	—	(10,563,931)
Sale of 3,335 shares of common stock		6,670	62,531	—	—	69,201
Balance, December 31, 2008		18,865,830	22,651,222	62,471,081	(150,683)	103,837,450
Comprehensive income:						
Net income	$ 9,005,786	—	—	9,005,786	—	9,005,786
Other comprehensive income, unrealized gains on securities, net of reclassification adjustment, net of tax	3,269,818	—	—	—	3,269,818	3,269,818

Total comprehensive income	$ 12,275,604					
Cash dividends declared, $0.40 per share		—	—	(3,773,166)	—	(3,773,166)
Balance, December 31, 2009		18,865,830	22,651,222	67,703,701	3,119,135	112,339,888
Comprehensive income:						
Net income	$ 12,966,274	—	—	12,966,274	—	12,966,274
Other comprehensive income, unrealized gains on securities, net of reclassification adjustment, net of tax	207,344	—	—	—	207,344	207,344
Total comprehensive income	$ 13,173,618					
Cash dividends declared, $0.44 per share		—	—	(4,150,482)	—	(4,150,482)
Balance, December 31, 2010		$ 18,865,830	$ 22,651,222	$ 76,519,493	$ 3,326,479	$ 121,363,024

See Notes to Consolidated Financial Statements.

Table of Contents

AMES NATIONAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2010, 2009 and 2008

	2010	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$12,966,274	$9,005,786	$6,351,996
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	663,798	1,558,307	1,312,785
Provision (credit) for off-balance sheet commitments	13,000	(21,000)	15,000
Amortization and (accretion), net	3,205,568	868,971	(184,998)
Depreciation	748,008	876,792	1,096,653
Provision (credit) for deferred income taxes	439,766	50,154	(3,710,424)
Securities gains, net	(977,512)	(1,186,912)	(3,515,323)
Other-than-temporary impairment of investment securities	4,500	29,565	12,054,387
Impairment of other real estate owned	14,900	3,879,901	—
Gain on sale of other real estate owned	(63,959)	(92,513)	(66,219)
Loss on disposal of equipment	—	1,096	—
Change in assets and liabilities:			
Decrease (increase) in loans held for sale	(969,908)	128,820	(807,050)
Decrease (increase) in accrued income receivable	(388,309)	940,061	1,372,613
Decrease (increase) in other assets	1,111,984	(3,860,396)	(841,693)
Increase (decrease) in accrued expenses and other liabilities	53,892	(778,849)	(355,962)
Net cash provided by operating activities	16,822,002	11,399,783	12,721,765
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of securities available-for-sale	(208,372,243)	(252,088,448)	(140,744,441)
Proceeds from sale of securities available-for-sale	22,326,136	68,698,126	59,489,208
Proceeds from maturities and calls of securities available-for-sale	132,889,786	83,228,240	96,590,223
Net decrease (increase) in interest bearing deposits in financial institutions	5,546,274	(14,375,327)	(9,766,148)
Net decrease (increase) in federal funds sold	(3,000,000)	16,533,000	(11,033,000)
Net decrease (increase) in loans	(4,450,923)	33,580,577	(1,677,154)
Net proceeds from the sale of other real estate owned	1,132,969	1,367,578	1,091,152
Purchase of bank premises and equipment, net	(362,514)	(202,997)	(220,090)
Other changes in other real estate owned	(14,554)	5,378	(377,539)
Net cash used in investing activities	(54,305,069)	(63,253,873)	(6,647,789)
CASH FLOWS FROM FINANCING ACTIVITIES			
Increase (decrease) in deposits	21,697,695	57,369,239	(25,324,085)
Increase in federal funds purchased and securities sold under agreements to repurchase	14,369,196	1,979,946	8,476,238
Proceeds (payments) from other short-term borrowings, net	1,908,301	(924,932)	326,386
Proceeds from long-term borrowings	3,750,000	2,500,000	21,500,000
Payments on long-term borrwings	(3,504,503)	(9,500,000)	(2,000,000)
Dividends paid	(4,056,153)	(5,471,090)	(10,468,702)
Proceeds from issuance of stock	—	—	69,201
Net cash provided by (used in) financing activities	34,164,536	45,953,163	(7,420,962)

Net decrease in cash and cash equivalents	(3,318,531)	(5,900,927)	(1,346,986)
CASH AND DUE FROM BANKS			
Beginning	18,796,664	24,697,591	26,044,577
Ending	$15,478,133	$18,796,664	$24,697,591

74

Table of Contents

AMES NATIONAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
Years Ended December 31, 2010, 2009 and 2008

	2010	2009	2008
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Cash payments for:			
Interest	$7,996,827	$10,712,422	$17,225,985
Income taxes	3,875,900	1,588,103	5,430,551
SUPLEMENTAL DISCLOSURE OF NONCASH			
INVESTING ACTIVITIES			
Transfer of loans to other real estate owned	$1,127,790	$2,307,228	$11,135,022

See Notes to Consolidated Financial Statements.

Table of Contents

Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies

Description of business: Ames National Corporation and subsidiaries (the Company) operates in the commercial banking industry through its subsidiaries in Ames, Boone, Story City, Nevada and Marshalltown, Iowa. Loan and deposit customers are located primarily in Story, Boone, Polk and Marshall Counties and adjacent counties in Iowa.

Segment information: The Company uses the "management approach" for reporting information about segments in annual and interim financial statements. The "management approach" is based on the way the chief operating decision-maker organizes segments within a company for making operating decisions and assessing performance. Based on the "management approach" model, the Company has determined that its business is comprised of one operating segment: banking. The banking segment generates revenues through personal, business, agricultural and commercial lending, management of the investment securities portfolio, deposit account services and trust services.

Consolidation: The consolidated financial statements include the accounts of Ames National Corporation (the Parent Company) and its wholly-owned subsidiaries, First National Bank, Ames, Iowa; State Bank & Trust Co., Nevada, Iowa; Boone Bank & Trust Co., Boone, Iowa; Randall-Story State Bank, Story City, Iowa; and United Bank & Trust NA, Marshalltown, Iowa (collectively, the Banks). All significant intercompany transactions and balances 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 (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, assessment of the fair value of other real estate owned and the assessment of other-than-temporary impairment for certain financial instruments.

Cash and cash equivalents: For purposes of reporting cash flows, cash and cash equivalents include cash on hand and amounts due from banks. The Company reports net cash flows for customer loan transactions, deposit transactions and short-term borrowings with maturities of 90 days or less. At December 31, 2010, the Company had approximately $10,970,000 on deposit at various financial institutions, some of which are in excess of federally insured limits. Management does not believe these balances carry a significant risk of loss but cannot provide absolute assurance that no losses would occur if these institutions were to become insolvent.

Table of Contents

Securities available-for-sale: The Company classifies all securities as available-for-sale. Securities available-for-sale are those the Company may decide to sell if needed for liquidity, asset-liability management or other reasons. Securities available-for-sale are reported at fair value, with net unrealized gains and losses reported as other comprehensive income or loss and as a separate component of stockholders' equity, net of tax.

Gains and losses on the sale of securities are determined using the specific identification method based on amortized cost and are reflected in results of operation at the time of sale. Interest and dividend income, adjusted by amortization of purchase premium or discount over the estimated life of the security using the level yield method, is included in income as earned.

Declines in the fair value of available-for-sale securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the intent to sell the investment securities and the more likely than not requirement that the Company will be required to sell the investment securities prior to recovery (2) the length of time and the extent to which the fair value has been less than cost and (3) the financial condition and near-term prospects of the issuer. Due to potential changes in conditions, it is at least reasonably possible that changes in management's assessment of other-than-temporary impairment will occur in the near term and that such changes could be material to the amounts reported in the Company's financial statements.

Loans held for sale: Loans held for sale are the loans the Banks have the intent to sell in the foreseeable future. They are carried at the lower of aggregate cost or fair value. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income. Gains and losses on sales of loans are determined by the difference between the sale proceeds and the carrying value of the loans, recognized at settlement date and recorded as noninterest income.

Loans: Loans are stated at the principal amount outstanding, net of deferred loan fees and the allowance for loan losses. Interest on loans is credited to income as earned based on the principal amount outstanding. The Banks' policy is to discontinue the accrual of interest income on any loan 90 days or more past due unless the loans are well collateralized and in the process of collection. Income on nonaccrual loans is subsequently recognized only to the extent that cash payments are received and principal obligations are expected to be recoverable. Nonaccrual loans are returned to an accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to timely payment of principal or interest.

Allowance for loan losses: The allowance for loan losses is established through a provision for loan losses and maintained at a level deemed appropriate by management to provide for known and inherent risks in the loan portfolio. The allowance is based upon an ongoing review of past loan loss experience, current economic conditions, the underlying collateral value securing the loans and other adverse situations that may affect the borrower's ability to repay. Loans which are deemed to be uncollectible are charged off and deducted from the allowance. Recoveries on loans charged-off are added to the allowance. This evaluation is inherently subjective and requires estimates that are susceptible to significant revisions as more information becomes available. Due to potential changes in conditions, it is at least reasonably possible that changes in estimates will occur in the near term and that such changes could materially affect the amounts reported in the Company's financial statements.

Table of Contents

The Company's allowance for possible loan losses consists of two components (i) specific valuation allowances based on probable losses on specific loans and (ii) general valuation allowances based on historical loan loss experience, general economic conditions and other qualitative risk factors both internal and external to the Company.

The allowances established for probable losses on specific loans are based on a regular analysis and evaluation of problem loans. Loans are classified based on an internal credit risk rating process that evaluates, among other things: (i) the obligor's ability to repay; (ii) the underlying collateral, if any; and (iii) the economic environment and industry in which the borrower operates. 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. Smaller balance homogeneous loans are evaluated for impairment in total. Such loans include residential first mortgage loans secured by one-to-four family residences, residential construction loans, and automobile loans. Commercial and agricultural loans and mortgage loans secured by other properties are evaluated individually for impairment when analysis of borrower operating results and financial condition indicates that underlying cash flows of the borrower's business are not adequate to meet its debt service requirements. Often this is associated with a delay or shortfall in payments of 90 days or more. Nonaccrual loans are often also considered impaired. Impaired loans, or portions thereof, are charged off when deemed uncollectible.

General valuation allowances are based on historical loan loss experience, general economic conditions and other qualitative risk factors both internal and external to the Company. In general, such valuation allowances are determined by evaluating, among other things: (i) actual charge offs; (ii) the experience, ability and effectiveness of the Company's lending management and staff; (iii) the effectiveness of the Company's loan policies, procedures and internal controls; (iv) changes in asset quality; (v) changes in loan portfolio volume; (vi) the composition and concentrations of credit; (vii) the impact of competition on loan structuring and pricing; (viii) the effectiveness of the internal audit loan review function; (ix) the impact of environmental risks on portfolio risks; and (x) the impact of rising interest rates on portfolio risk. Management evaluates the degree of risk that each one of these components has on the quality of the loan portfolio on a quarterly basis. Each component is determined to have either a high, moderate or low degree of risk. The results are then input into a "general allocation matrix" to determine an appropriate general valuation allowance. Included in the general valuation allowances are allocations for groups of loans with similar risk characteristics.

Premises and equipment: Premises and equipment are stated at cost less accumulated depreciation. Depreciation expense is computed using straight-line and accelerated methods over the estimated useful lives of the respective assets. Depreciable lives range from 3 to 7 years for equipment and 15 to 39 years for premises.

Table of Contents

Other real estate owned: Real estate properties acquired through or in lieu of foreclosure are initially recorded at the fair value less estimated selling cost at the date of foreclosure. Any write-downs based on the asset's fair value at the date of acquisition are charged to the allowance for loan losses. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. The portion of interest costs relating to development of real estate is capitalized. Valuations are periodically performed by management and property held for sale is carried at the lower of the new cost basis or fair value less cost to sell and any subsequent write-downs are charged to operations. Impairment losses on property to be held and used are measured as the amount by which the carrying amount of a property exceeds its fair value less costs to sell. This evaluation is inherently subjective and requires estimates that are susceptible to significant revisions as more information becomes available. Due to potential changes in conditions, it is at least reasonably possible that changes in fair values will occur in the near term and that such changes could materially affect the amounts reported in the Company's financial statements.

Trust department assets: Property held for customers in fiduciary or agency capacities are not included in the accompanying consolidated balance sheets, as such items are not assets of the Banks.

Advertising Costs: Advertising costs are expensed as incurred.

Income taxes: Deferred income taxes are provided on temporary differences between financial statement and income tax reporting. Temporary differences are differences between the amounts of assets and liabilities reported for financial statement purposes and their tax basis. Deferred tax assets are recognized for temporary differences that will be deductible in future years' tax returns and for operating loss and tax credit carryforwards. Deferred tax assets are reduced by a valuation allowance if it is deemed more likely than not that some or all of the deferred tax assets will not be realized. Deferred tax liabilities are recognized for temporary differences that will be taxable in future years' tax returns. Accounting for uncertainty in income taxes sets out a consistent framework to determine the appropriate level of tax reserves to maintain for uncertain tax positions. Benefits from tax positions taken or expected to be taken in a tax return are not recognized if the likelihood that the tax position would be sustained upon examination by a taxing authority is considered to be 50 percent or less. Interest and penalties are accounted for as a component of income tax expense.

The Company files a consolidated federal income tax return, with each entity computing its taxes on a separate company basis. For state tax purposes, the Banks file franchise tax returns, while the Parent Company files a corporate income tax return.

Comprehensive income: Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on securities available-for-sale, are reported as a separate component of the stockholders' equity section of the consolidated balance sheet, and such items, along with net income, are components of comprehensive income. Gains and losses on securities available-for-sale are reclassified to net income as the gains or losses are realized upon sale of the securities. Other-than-temporary impairment charges are reclassified to net income at the time of the charge.

Table of Contents

Financial instruments with off-balance-sheet risk: The Company, in the normal course of business, makes commitments to make loans which are not reflected in the consolidated financial statements. A summary of these commitments is disclosed in Note 11.

Transfers of financial assets: Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (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.

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

Cash and due from banks, federal funds sold and interest bearing deposits in financial institutions: The recorded amount of these assets approximates fair value.

Securities available-for-sale: Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the securities credit rating, prepayment assumptions and other factors such as credit loss assumptions.

Loans held for sale: The fair value of loans held for sale is based on prevailing market prices.

Loans receivable: The fair value of loans is calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates, which reflect the credit and interest rate risk inherent in the loan. The estimate of maturity is based on the historical experience, with repayments for each loan classification modified, as required, by an estimate of the effect of current economic and lending conditions. The effect of nonperforming loans is considered in assessing the credit risk inherent in the fair value estimate.

Deposit liabilities: Fair values of deposits with no stated maturity, such as noninterest-bearing demand deposits, savings and NOW accounts, and money market accounts, are equal to the amount payable on demand as of the respective balance sheet date. Fair values of certificates of deposit are based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered for deposits of similar remaining maturities. The fair value estimates do not include the benefit that results from the low-cost funding provided by the deposit liabilities compared to the cost of borrowing funds in the market.

Table of Contents

Federal funds sold and securities sold under agreements to repurchase: The carrying amounts of federal funds sold and securities sold under agreements to repurchase approximate fair value because of the generally short-term nature of the instruments.

Other short-term borrowings: The carrying amounts of other short-term borrowings approximate fair value because of the generally short-term nature of the instruments.

Federal Home Loan Bank advances and other long-term borrowings: Fair values of Federal Home Loan Bank advances and other long-term borrowings are estimated using discounted cash flow analysis based on interest rates currently being offered with similar terms.

Accrued income receivable and accrued interest payable: The carrying amounts of accrued income receivable and interest payable approximate fair value.

Commitments to extend credit and standby letters of credit: The fair values of commitments to extend credit and standby letters of credit are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreement and credit worthiness of the counterparties. The carry value and fair value of the commitments to extend credit and standby letters of credit are not considered significant.

Limitations: Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Earnings per share: Basic earnings per share computations for the years ended December 31, 2010, 2009 and 2008, were determined by dividing net income by the weighted-average number of common shares outstanding during the years then ended. The Company had no potentially dilutive securities outstanding during the periods presented.

Table of Contents

The following information was used in the computation of basic earnings per share for the years ended December 31, 2010, 2009, and 2008.

	2010	2009	2008
Basic earning per share computation:			
Net income	$12,966,274	$9,005,786	$6,351,996
Weighted average common shares outstanding	9,432,915	9,432,915	9,431,393
Basic EPS	$1.37	$0.95	$0.67

Reclassifications: Certain reclassifications have been made to the prior consolidated financial statements to conform to the current period presentation. These reclassifications had no effect on stockholders' equity and net income for the prior periods.

Recent accounting pronouncements: On December 23, 2009, the Financial Accounting Standards Board (FASB) issued guidance which modifies certain aspects contained in the Transfers and Servicing topic of FASB Accounting Standards Codification (ASC) 860. This standard enhances information reported to users of financial statements by providing greater transparency about transfers of financial assets, including securitization transactions, and where companies have continuing exposure to the risks related to transferred financial assets. This standard was effective for the Company as of January 1, 2010 with adoption applied prospectively for transfers that occur on or after that date. The adoption of this standard did not have a material impact on the Company's financial position or results of operations.

In January 2010, the FASB issued guidance which modifies certain aspects contained in the Fair Value Measurements and Disclosure topic of FASB ASC 820. This standard enhances information reported to users of the financial statements by providing additional and enhanced disclosures about the fair value measurements. This standard was effective for the Company as of January 1, 2010; except for the disclosures about purchases, sales, issuances and settlements in the roll forward of activity in Level 3 fair value measurements, which will be effective on January 1, 2011. The adoption of this standard did not have any impact on the Company's financial position or results of operations.

In July 2010, the FASB issued Accounting Standards Update 2010-20, Disclosure about the Credit Quality of Financing Receivables and the Allowance for Credit Losses. The new guidance increases disclosures made about the credit quality of loans and the allowance for credit losses. The disclosures provide additional information about the nature of credit risk inherent in the Company's loans, how credit risk is analyzed and assessed, and the reasons for the change in the allowance for loan losses. The requirements were generally effective for the Company as of December 31, 2010 and the appropriate required disclosures were made in the consolidated financial statements. In January 2011, the FASB delayed the effective date of the disclosures in the aforementioned guidance related to troubled debt restructurings. These new disclosures are anticipated to be effective for interim and annual periods ending after June 15, 2011.

Table of Contents

Note 2. Restrictions on Cash and Due from Banks

The Federal Reserve Bank requires member banks to maintain certain cash and due from bank reserves. The subsidiary banks' reserve requirements totaled approximately $3,530,000 and $3,357,000 at December 31, 2010 and 2009, respectively.

Note 3. Debt and Equity Securities

The amortized cost of securities available-for-sale and their approximate fair values are summarized below:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
2010:				
U.S. treasury	$499,885	$3,265	$—	$503,150
U.S. government agencies	86,336,578	1,190,768	(114,727)	87,412,619
U.S. government mortgage-backed securities	125,740,846	2,237,443	(629,668)	127,348,621
State and political subdivisions	226,352,715	3,254,157	(1,234,045)	228,372,827
Corporate bonds	19,220,366	1,183,213	(31,575)	20,372,004
Equity securities, financial industry common stock	3,402,389	—	(588,208)	2,814,181
Equity securities, other	3,074,999	9,500	—	3,084,499
	$464,627,778	$7,878,346	$(2,598,223)	$469,907,901

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
2009:				
U.S. treasury	$498,972	$26,219	$—	$525,191
U.S. government agencies	105,903,470	969,583	(233,169)	106,639,884
U.S. government mortgage-backed securities	100,106,597	1,724,922	(242,033)	101,589,486
State and political subdivisions	175,298,674	3,109,322	(355,571)	178,052,425
Corporate bonds	23,094,417	1,253,157	(47,880)	24,299,694
Equity securities, financial industry common stock	3,402,389	—	(1,056,088)	2,346,301
Equity securities, other	5,399,493	58,400	(255,856)	5,202,037
	$413,704,012	$7,141,603	$(2,190,597)	$418,655,018

Table of Contents

The amortized cost and estimated fair value of debt securities available-for-sale as of December 31, 2010, are shown below by contractual maturity. 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	Estimated Fair Value
Due in one year or less	$30,472,212	$30,776,269
Due after one year through five years	293,315,336	298,315,898
Due after five years through ten years	117,031,957	117,606,467
Due after ten years	17,330,885	17,310,587
	458,150,390	464,009,221
Equity securities	6,477,388	5,898,680
	$464,627,778	$469,907,901

At December 31, 2010 and 2009, securities with a carrying value of approximately $186,472,000 and $177,862,000, respectively, were pledged as collateral on public deposits, securities sold under agreements to repurchase and for other purposes as required or permitted by law. Securities sold under agreements to repurchase are held by the Company's safekeeping agent.

For the years ended December 31, 2010, 2009, and 2008, proceeds from sales of securities available-for-sale amounted to $22,326,136, $68,698,126 and $59,489,208, respectively. Gross realized gains and gross realized losses on sales of securities available-for-sale were $999,492 and $21,980, respectively, in 2010, $2,152,256 and $965,344, respectively, in 2009, and $4,732,750 and $1,217,427, respectively, in 2008. The tax provision applicable to the net realized gains and losses amounted to approximately $364,000, $439,000, and $1,376,000, respectively. Other-than-temporary impairments recognized as a component of income were $4,500, $29,565 and $12,054,387 in 2010, 2009, and 2008, respectively. Impairment for 2008 was attributable to charges of $8,451,000 related to Federal National Mortgage Association and Federal Home Loan Mortgage corporation preferred stock and $3,603,000 related to three corporate bonds.

The components of other comprehensive income (loss) - net unrealized gains (losses) on securities available-for-sale were as follows:

	2010	2009	2008
Unrealized holding gains (losses) arising during the period	$1,302,129	$6,347,532	$(11,777,697)
Reclassification adjustment for net losses (gains) realized in net income	(973,012)	(1,157,347)	8,539,064
Net unrealized gains (losses) before tax effect	329,117	5,190,185	(3,238,633)
Tax effect	(121,773)	(1,920,367)	1,198,294
Other comprehensive income - Net unrealized gains (losses) on securities	$207,344	$3,269,818	$(2,040,339)

Table of Contents

Unrealized losses and fair value aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of December 31, 2010 and 2009, are summarized as follows:

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
2010:						
Securities available for sale:						
U.S. government agencies	$15,321,189	$(107,139)	$372,404	$(7,588)	$15,693,593	$(114,727)
U.S. government mortgage-backed securities	43,327,689	(629,668)	—	—	43,327,689	(629,668)
State and political subsidivisions	53,299,308	(1,218,282)	497,051	(15,763)	53,796,359	(1,234,045)
Corporate obligations	2,022,914	(31,575)	—	—	2,022,914	(31,575)
Equity securities, financial industry common stock	—	—	2,814,181	(588,208)	2,814,181	(588,208)
	$113,971,100	$(1,986,664)	$3,683,636	$(611,559)	$117,654,736	$(2,598,223)

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
2009:						
Securities available for sale:						
U.S. government agencies	$ 20,945,895	$ (221,061)	$ 493,118	$ (12,108)	$ 21,439,013	$ (233,169)
U.S. government mortgage-backed securities	35,520,408	(242,033)	—	—	35,520,408	(242,033)
State and political subsidivisions	25,536,025	(292,017)	2,701,961	(63,554)	28,237,986	(355,571)
Corporate obligations	998,971	(764)	2,687,426	(47,116)	3,686,397	(47,880)
Equity securities, financial industry common stock	—	—	2,346,301	(1,056,088)	2,346,301	(1,056,088)
Equity securities, other	—	—	1,932,636	(255,856)	1,932,636	(255,856)
	$ 83,001,299	$ (755,875)	$ 10,161,442	$ (1,434,722)	$ 93,162,741	$ (2,190,597)

At December 31, 2010, debt securities have unrealized losses of $2,010,015. These unrealized losses are generally due to changes in interest rates or general market conditions. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and industry analysts' reports. Unrealized losses on equity securities totaled $588,208 as of December 31, 2010. Management analyzed the financial condition of the equity issuers and considered the general market conditions and other factors in concluding that the unrealized losses on equity securities were temporary. Due to potential changes in conditions, it is at least reasonably possible that changes in fair values and

management's assessments will occur in the near term and that such changes could materially affect the amounts reported in the Company's financial statements.

Table of Contents

Note 4. Loans Receivable

The composition of loans receivable is as follows:

	2010	2009
Commercial and agricultural	$123,802,383	$111,386,798
Real estate - mortgage	260,234,111	264,202,119
Real estate - construction	19,597,188	22,863,630
Consumer	6,622,200	7,792,077
Other	15,429,670	16,900,983
	425,685,552	423,145,607
Less:		
Allowance for loan losses	(7,520,665)	(7,651,510)
Deferred loan fees	(71,316)	(59,861)
	$418,093,571	$415,434,236

Commercial and agricultural operating loans are underwritten based on the Company's examination of current and projected cash flows to determine the ability of the borrower to repay their obligations as agreed. This underwriting includes the evaluation of cash flows of the borrower, underlying collateral, if applicable, and the borrower's ability to manage its business activities. The cash flows of borrowers and the collateral securing these loans may fluctuate in value after the initial evaluation. A first priority lien on the general assets of the business normally secures these types of loans. Loan to value limits vary and are dependent upon the nature and type of the underlying collateral and the financial strength of the borrower. Crop and hail insurance is required for most agricultural borrowers. Loans are generally guaranteed by the principal(s). The Company's commercial and agricultural operating lending is primarily in its primary market area.

Commercial and agricultural real estate loans are subject to underwriting standards and processes similar to commercial and agricultural operating loans, in addition to those unique to real estate loans. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial and agricultural real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Loan to value is generally 75% of the cost or value of the assets. Appraisals on properties securing these loans are performed by fee appraisers approved by the Board of Directors. Because payments on commercial and agricultural real estate loans are often dependent on the successful operation or management of the properties, repayment of such loans may be subject to adverse conditions in the real estate market or the economy. Management monitors and evaluates commercial and agricultural real estate loans based on collateral and risk rating criteria. The Company may require guarantees on these loans. The Company's commercial and agricultural real estate loans are secured primarily by properties located in its primary market area.

Construction loans are underwritten utilizing independent appraisals, sensitivity analysis of absorption, vacancy and lease rates and financial analysis of the developers and property owners. Construction loans are generally based upon estimates of costs and value associated with the complete project. These estimates may be inaccurate. Construction loans often involve the disbursement of funds with repayment substantially dependent on the success of the ultimate project. These loans are closely monitored by on-site inspections and are considered to have higher risks than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, general economic conditions and the availability of long-term financing. The Company may require guarantees on these loans. The Company's construction loans are secured primarily by properties located in its primary market area.

The Company originates 1-4 family real estate and consumer loans utilizing credit reports to supplement the underwriting process. The Company's manual underwriting standards for 1-4 family loans are generally in accordance with FHLMC and FNMA manual underwriting guidelines. Properties securing 1-4 four-family real estate loans are appraised by either staff appraisers or fee appraisers, both of which are independent of the loan origination function and have been approved by the Board of Directors. The loan-to-value ratios normally do not exceed 80% without credit enhancements such as mortgage insurance. The Company will lend up to 100% of the lesser of the appraised value or purchase price for conventional 1-4 family real estate loans, provided private mortgage insurance is obtained. The underwriting standards for consumer loans include a determination of the applicant's payment history on other debts and an assessment of their ability to meet existing obligations and payments on the proposed loan. To monitor and manage loan risk, policies and procedures are developed and modified, as needed by management. This activity, coupled with smaller loan amounts that are spread across many individual borrowers, minimizes risk. Additionally, market conditions are reviewed by management on a regular basis. The Company's 1-4 family real estate are secured primarily by properties located in its primary market area.

The Company maintains an audit department that reviews and validates the credit risk program on a periodic basis. Results of these reviews are presented to management and the audit committee. The loan review process complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel, as well as the Company's policies and procedures.

Summary changes in the allowance for loan losses are as follows:

	2010	2009	2008
Balance, beginning	$7,651,510	$6,779,215	$5,780,678
Provision for loan losses	663,798	1,558,307	1,312,785
Recoveries of loans charged-off	72,007	180,961	112,440
Loans charged-off	(866,650)	(866,973)	(426,688)
Balance, ending	$7,520,665	$7,651,510	$6,779,215

Table of Contents

Specific changes in the allowance for loan losses and recorded investment in loans for the year ended December 31, 2010 are as follows:

	Construction Real Estate	1-4 Family Residential Real Estate	Commercial Real Estate	Agricultural Real Estate	Commercial	Agricultural	Consumer and Other
Allowance for loan losses:							
Balance, beginning	$1,040,000	$1,133,000	$2,683,000	$523,000	$1,199,000	$642,000	$432,000
Provision (credit) for loan losses	(287,000)	433,000	57,000	13,000	339,000	103,000	6,000
Recoveries of loans charged-off	—	1,000	—	—	5,000	32,000	34,000
Loans charged-off	(22,000)	(163,000)	(20,000)	(50,000)	(391,000)	(42,000)	(179,000)
Balance, ending	$731,000	$1,404,000	$2,720,000	$486,000	$1,152,000	$735,000	$293,000
Ending balance: Individually evaluated for impairment	$223,000	$158,000	$42,000	$—	$—	$—	$22,000
Ending balance: Collectively evaluated for impairment	508,000	1,246,000	2,678,000	486,000	1,152,000	735,000	271,000
Ending balance	$731,000	$1,404,000	$2,720,000	$486,000	$1,152,000	$735,000	$293,000
Loans:							
Ending balance: Impaired loans with a valuation allowance	$4,156,000	$1,395,000	$802,000	$—	$45,000	$—	$34,000
Ending balance: Collectively evaluated for impairment	15,441,000	87,538,000	138,568,000	31,931,000	78,128,000	45,630,000	22,018,000
Ending balance	$19,597,000	$88,933,000	$139,370,000	$31,931,000	$78,173,000	$45,630,000	$22,052,000

Credit Quality Indicators. As part of the on-going monitoring of the credit quality of the Company's loan portfolio, management tracks certain credit quality indicators including trends related to (i) the risk ratings of construction, commercial and agricultural real estate loans and commercial and agricultural operating loans, (ii) the level of classified loans, (iii) net charge-offs, (iv) non-performing loans and (v) the general economic conditions in our market area.

The Company utilizes a risk rating matrix to assign risk ratings to each of its construction, commercial and agricultural loans. Loans are rated on a scale of 1 to 7. A description of the general characteristics of the 7 risk ratings is as follows:

Ratings 1, 2 and 3 - These ratings include loans to average to excellent credit quality borrowers. These borrowers generally have significant capital strength, moderate leverage and stable earnings and growth commensurate to their relative risk rating. These ratings also include performing loans less than $100,000.

Rating 4 - This rating includes loans on management's "watch list" and is intended to be utilized for pass rated borrowers where credit quality has began to show signs of financial weakness that now requires management's heightened attention.

Table of Contents

Rating 5 - This rating is for "Special Mention" in accordance with regulatory guidelines. This rating is intended to be temporary and includes loans to borrowers whose credit quality has clearly deteriorated and are at risk of further decline unless active measures are taken to correct the situation.

Rating 6 - This rating includes "Substandard" loans, in accordance with regulatory guidelines, for which the accrual of interest has not been stopped. By definition under regulatory guidelines, a "Substandard" loan has defined weaknesses which make payment default or principal exposure likely, but not yet certain. Such loans are apt to be dependent upon collateral liquidation, a secondary source of repayment or an event outside of the normal course of business.

Rating 7 - This rating includes "Substandard-Impaired" loans, in accordance with regulatory guidelines, for which the accrual of interest has generally been stopped. This rating includes loans; (i) where interest is more than 90 days past due; (ii) not fully secured; (iii) loans where a specific valuation allowance may be necessary.

The credit risk profile by internally assigned ratings at December 31, 2010, is as follows:

	Construction Real Estate	Commercial Real Estate	Agricultural Real Estate	Commercial Operating	Agricultural Operating	Total
Pass	$6,739,000	$83,235,000	$29,580,000	$64,791,000	$42,941,000	$227,286,000
Special Mention	3,694,000	42,137,000	2,351,000	8,922,000	1,318,000	58,422,000
Substandard	5,008,000	13,196,000	—	4,415,000	1,371,000	23,990,000
Substandard-Impaired	4,156,000	802,000	—	45,000	—	5,003,000
	$19,597,000	$139,370,000	$31,931,000	$78,173,000	$45,630,000	$314,701,000

The credit risk profile based on payment activity at December 31, 2010 is as follows:

	1-4 Family Residential Real Estate	Consumer and Other	Total
Performing	$87,538,000	$22,018,000	$109,556,000
Non-performing	1,395,000	34,000	1,429,000
	$88,933,000	$22,052,000	$110,985,000

Table of Contents

Information concerning impaired loans is as follows:

	December 31, 2010	December 31, 2009
Impaired loans without a valuation allowance	$2,327,000	$4,381,000
Impaired loans with a valuation allowance	4,105,000	5,806,000
Total impaired loans	$6,432,000	$10,187,000
Valuation related to impaired loans	$445,000	$999,000
Total nonaccrual loans	$6,277,000	$10,187,000
Total loans past due ninety days or more and still accruing	$21,000	$121,000

	Years Ended December 31,		
	2010	2009	2008
Average investments in impaired loans	$7,095,000	$8,498,000	$7,590,000
Interest income that would have been recognized on impaired loans	$425,000	$564,000	$478,000
Interest income recorded on impaired loans	$233,000	$32,000	$155,000

Table of Contents

Information concerning impaired loans by loan type as of December 31, 2010, is as follows:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no specific reserve recorded:					
Real estate - construction	$1,290,000	$1,290,000	$—	$1,646,000	$99,000
Real estate - 1 to 4 family residential	846,000	846,000	—	715,000	22,000
Real estate - commercial	136,000	136,000	—	102,000	—
Real estate - agricultural	—	—	—	135,000	12,000
Operating - commercial	45,000	45,000	—	384,000	97,000
Operating - agricultural	—	—	—	—	—
Consumer and other	10,000	10,000	—	24,000	1,000
Total loans with no specific reserve:	2,327,000	2,327,000	—	3,006,000	231,000
With an allowance recorded:					
Real estate - construction	2,643,000	2,866,000	223,000	2,944,000	—
Real estate - 1 to 4 family residential	391,000	549,000	158,000	287,000	2,000
Real estate - commercial	624,000	666,000	42,000	624,000	—
Real estate - agricultural	—	—	—	142,000	—
Operating - commercial	—	—	—	85,000	—
Operating - agricultural	—	—	—	—	—
Consumer and other	2,000	24,000	22,000	7,000	—
Total loans with specific reserve:	3,660,000	4,105,000	445,000	4,089,000	2,000
Total					
Real estate - construction	3,933,000	4,156,000	223,000	4,590,000	99,000
Real estate - 1 to 4 family residential	1,237,000	1,395,000	158,000	1,002,000	24,000
Real estate - commercial	760,000	802,000	42,000	726,000	—
Real estate - agricultural	—	—	—	277,000	12,000
Operating - commercial	45,000	45,000	—	469,000	97,000
Operating - agricultural	—	—	—	—	—
Consumer and other	12,000	34,000	22,000	31,000	1,000
	$5,987,000	$6,432,000	$445,000	$7,095,000	$233,000

There are no significant differences between impaired loan balances at December 31, 2010 as compared to non-accrual loans.

Table of Contents

Past due loans as of December 31, 2010, are as follows:

	30-89 Past Due	Greater Than 90 Days	Total Past Due	Current	Total	Greater Than 90 Days Accruing
Real estate - construction	$135,000	$—	$135,000	$19,462,000	$19,597,000	$—
Real estate - 1 to 4 family residential	413,000	684,000	1,097,000	87,836,000	88,933,000	21,000
Real estate - commercial	205,000	136,000	341,000	139,029,000	139,370,000	—
Real estate - agricultural	49,000	—	49,000	31,883,000	31,932,000	—
Operating - commercial	1,399,000	45,000	1,444,000	76,728,000	78,172,000	—
Operating - agricultural	—	—	—	45,630,000	45,630,000	—
Consumer and other	131,000	10,000	141,000	21,911,000	22,052,000	—
	$2,332,000	$875,000	$3,207,000	$422,479,000	$425,686,000	$21,000

There are no other known problem loans that cause management to have serious doubts as to the ability of such borrowers to comply with the present loan repayment terms.

As of December 31, 2010, there were no material commitments to lend additional funds to customers whose loans were classified as impaired.

Loans are made in the normal course of business to certain directors and executive officers of the Company and to their affiliates. The terms of these loans, including interest rates and collateral, are similar to those prevailing for comparable transactions with others and do not involve more than a normal risk of collectability. Loan transactions with related parties were as follows:

	2010	2009
Balance, beginning of year	$8,218,833	$14,191,369
New loans	15,714,078	14,162,381
Repayments	(14,752,962)	(16,241,577)
Change in status	—	(3,893,340)
Balance, end of year	$9,179,949	$8,218,833

Table of Contents

Note 5. Bank Premises and Equipment

The major classes of bank premises and equipment and the total accumulated depreciation are as follows:

	2010	2009
Land	$2,426,383	$2,426,383
Buildings and improvements	14,688,284	14,518,623
Furniture and equipment	5,980,587	6,026,156
	23,095,254	22,971,162
Less accumulated depreciation	11,556,666	11,061,758
	$11,538,588	$11,909,404

Note 6. Other Real Estate Owned

Changes in the other real estate owned are as follows:

	2010	2009
Balance, beginning of year	$10,480,449	$13,333,565
Transfer of loans	1,127,790	2,307,228
Impairment	(14,900)	(3,879,901)
Net proceeds from sale	(1,132,969)	(1,367,578)
Gain on sale	63,959	92,513
Other changes	14,554	(5,378)
Balance, end of year	$10,538,883	$10,480,449

Note 7. Deposits

At December 31, 2010, the maturities of time deposits are as follows:

2011	$139,665,781
2012	54,874,314
2013	22,438,050
2014	10,450,705
2015 and after	10,671,558
	$238,100,408

Table of Contents

Interest expense on deposits is summarized as follows:

	2010	2009	2008
NOW accounts	$449,208	$469,064	$897,544
Savings and money market	919,754	1,181,375	2,759,380
Time, $100,000 and over	1,651,475	2,289,960	3,948,039
Other time	3,076,067	4,487,764	6,602,771
	$6,096,504	$8,428,163	$14,207,734

Deposits held by the Company from related parties at December 31, 2010 and 2009 amounted to approximately $12,000,000 and $10,000,000, respectively.

Note 8. Borrowings

Federal funds purchased are unsecured and mature daily. Securities sold under repurchase agreements are short-term and are secured by investments. Short-term borrowings as of December 31, 2010 and 2009, consisted of Treasury, Tax and Loan option notes secured by investment securities.

At December 31, 2010, FHLB advances and other long-term borrowings consisted of the following:

	Amount	Weighted Average Interest Rate	Features
FHLB advances maturing in:			
2011	$ 1,500,000	4.09 %	
2012	500,000	1.45 %	
2013	2,000,000	2.06 %	
2014	—	0.00 %	
2015	—	0.00 %	
After	12,745,497	2.96 %	Includes $4,500,000 callable in February 2011; $7,000,000 callable in March 2011: $1,245,497 15 year amortizing and puttable in 2015
Total FHLB advances	$ 16,745,497	2.91 %	
Term repurchase agreements maturing in:			
2014	7,000,000	2.99 %	
2018	13,000,000	3.56 %	Callable in 2011
Total term repurchase agreements	$ 20,000,000	3.36 %	
Total FHLB and other long-term borrowings	$ 36,745,497	3.15 %	

Table of Contents

Borrowed funds at December 31, 2009 included borrowings from the FHLB and term repurchase agreements of $36,500,000. Such borrowings carried a weighted-average interest rate of 3.47% with maturities ranging from 2010 through 2018.

Term repurchase agreements are securities sold under agreement to repurchase, have maturity dates greater than one year, and can be called by the issuing financial institution on a quarterly basis.

FHLB borrowings are collateralized by certain 1-4 family residential real estate loans, multifamily real estate loans, commercial real estate loans and agricultural real estate loans. The short-term and term repurchase agreements are collateralized with U.S. government agencies and mortgage-backed securities with a carrying and fair value of $94,211,000 at December 31, 2010. The Banks had available borrowings with the Federal Home Loan Bank of Des Moines, Iowa of $54,208,000 at December 31, 2010.

Note 9. Employee Benefit Plans

The Company has a qualified 401(k) profit-sharing plan. For the year ended December 31, 2010, the Company matched employee contributions up to a maximum of 3% and also contributed an amount equal to 3% of the participating employee's compensation. For the years ended December 31, 2009 and 2008, the Company matched employee contributions up to a maximum of 2% of qualified compensation and also contributed an amount equal to 5% of the participating employee's compensation. For the years ended December 31, 2010, 2009 and 2008, Company contributions to the plan were approximately $545,000, $734,000, and $611,000, respectively. The plan covers substantially all employees.

Note 10. Income Taxes

The components of income tax expense are as follows:

	2010	2009	2008
Federal:			
Current	$3,144,997	$1,710,159	$3,839,793
Deferred	334,114	93,120	(3,370,787)
	3,479,111	1,803,279	469,006
State:			
Current	919,289	532,494	715,645
Deferred	105,652	(42,966)	(339,637)
	1,024,941	489,528	376,008
Income tax expense	$4,504,052	$2,292,807	$845,014

Table of Contents

Total income tax expense differed from the amounts computed by applying the U.S. federal income tax rate of 35% to income before income taxes as a result of the following:

	2010	2009	2008
Income taxes at 35% federal tax rate	$6,114,614	$3,954,508	$2,518,955
Increase (decrease) resulting from:			
Tax-exempt interest and dividends	(2,084,701)	(1,892,872)	(1,984,052)
State taxes, net of federal tax benefit	476,963	404,556	520,100
Other	(2,824)	(173,385)	(209,989)
Total income tax expense	$4,504,052	$2,292,807	$845,014

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred liabilities are as follows:

	2010	2009
Deferred tax assets:		
Allowance for loan losses	$2,411,928	$2,392,936
Other than temporary impairment	880,609	2,063,918
Other real estate owned	1,457,495	1,213,129
Other items	783,463	252,122
	5,533,495	5,922,105
Deferred tax liabilities:		
Net unrealized gains on securities available for sale	(1,953,645)	(1,831,872)
Other	(273,867)	(222,710)
	(2,227,512)	(2,054,582)
Net deferred tax assets	$3,305,983	$3,867,523

Income taxes currently payable of approximately $154,000 are included in accrued expenses and other liabilities as of December 31, 2010. Income taxes currently receivable of approximately $35,000 are included in other assets as of December 31, 2009.

The Company and its subsidiaries file one income tax return in the U.S. federal jurisdiction and separate tax returns for the state of Iowa. The Company is no longer subject to U.S. federal income and state tax examinations for years before 2007.

Management has determined that the Company has no material uncertain tax positions that would require recognition. The Company had no significant unrecognized tax benefits as of December 31, 2010, that if recognized, would affect the effective tax rate. Management has determined there are no material accrued interests or penalties as of or for the years ended December 31, 2010 and 2009. The Company had no positions for which it deemed that it is reasonably possible that the total amounts of the unrecognized tax benefit will significantly increase or decrease within the 12 months as of December 31, 2010 and 2009.

Table of Contents

Note 11. Commitments, Contingencies and Concentrations of Credit Risk

The Company is party to financial instruments with off-balance-sheet risk in the normal course of business. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheet.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as they do for on-balance-sheet instruments. A summary of the Company's commitments is as follows:

	2010	2009
Commitments to extend credit	$79,757,000	$73,976,000
Standby letters of credit	3,139,000	1,727,000
	$82,896,000	$75,703,000

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. 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 creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Banks upon extension of credit, is based on management's credit evaluation of the party.

Standby letters of credit are conditional commitments issued by the Banks to guarantee the performance of a customer to a third-party. Those guarantees are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Collateral held varies and is required in instances which the Banks deem necessary. In the event the customer does not perform in accordance with the terms of the agreement with the third party, the Banks would be required to fund the commitment. The maximum potential amount of future payments the Banks could be required to make is represented by the contractual amount shown in the summary above. If the commitments were funded, the Banks would be entitled to seek recovery from the customer.

At December 31, 2010 and 2009, the Banks have established liabilities totaling $240,000 and $227,000, respectively to cover estimated credit losses for off-balance-sheet loan commitments and standby letters of credit.

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

Table of Contents

Concentrations of credit risk: The Banks originate real estate, consumer, and commercial loans, primarily in Story, Boone, Hamilton, Polk and Marshall Counties, Iowa, and adjacent counties. Although the Banks have diversified loan portfolios, a substantial portion of their borrowers' ability to repay loans is dependent upon economic conditions in the Banks' market areas.

Note 12. Regulatory Matters

The Company and its 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 possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and Banks' financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Banks must meet specific capital guidelines that involve quantitative measures of their 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. Prompt corrective action provisions are not applicable to bank holding companies. Regulators also have the ability to impose higher limits than those specified by capital adequacy guidelines if they so deem necessary.

Quantitative measures established by regulation to ensure capital adequacy require the Company and each subsidiary bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 2010 and 2009, that the Company and each subsidiary bank met all capital adequacy requirements to which they are subject.

On March 16, 2009, the Office of the Comptroller of the Currency (OCC) informed the Company's lead bank, First National Bank, of the OCC's decision to establish individual minimum capital ratios for First National Bank in excess of the capital ratios that would otherwise be imposed under applicable regulatory standards. The OCC is requiring First National Bank to maintain, on an ongoing basis, Tier 1 Leverage Capital of 9% of Adjusted Total Assets and Total Risk Based Capital of 11% of Risk-Weighted Assets. As of December 31, 2010 and 2009, First National Bank exceeded the 9% Tier 1 and 11% Total Risk Based capital requirements. Failure to maintain the individual minimum capital ratios established by the OCC could result in additional regulatory action against First National Bank.

As of December 31, 2010, the most recent notification from the federal banking regulators categorized the subsidiary banks as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Banks must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the table. Management believes there are no conditions or events since that notification that have changed the institution's category. The Company's and each of the subsidiary bank's actual capital amounts and ratios as of December 31, 2010 and 2009 are also presented in the table.

Table of Contents

	Actual			For Capital Adequacy Purposes			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	$125,515	18.0	%	$55,940	8.0	%	N/A	N/A	
Boone Bank & Trust	13,183	17.4		6,054	8.0		$7,567	10.0	%
First National Bank	53,759	14.0		42,287	11.0		42,287	11.0	
Randall-Story State Bank	9,281	14.6		5,080	8.0		6,351	10.0	
State Bank & Trust	14,976	15.3		7,811	8.0		9,764	10.0	
United Bank & Trust	10,990	17.5		5,034	8.0		6,293	10.0	
Tier 1 capital (to risk-weighted assets):									
Consolidated	$117,666	16.8	%	$27,970	4.0	%	N/A	N/A	
Boone Bank & Trust	12,357	16.3		3,027	4.0		$4,540	6.0	%
First National Bank	50,389	13.1		15,377	4.0		23,065	6.0	
Randall-Story State Bank	8,521	13.4		2,540	4.0		3,810	6.0	
State Bank & Trust	13,755	14.1		3,906	4.0		5,858	6.0	
United Bank & Trust	10,201	16.2		2,517	4.0		3,776	6.0	
Tier 1 capital (to average-weighted assets):									
Consolidated	$117,666	12.5	%	$37,549	4.0	%	N/A	N/A	
Boone Bank & Trust	12,357	11.7		4,238	4.0		$5,297	5.0	%
First National Bank	50,389	10.0		45,207	9.0		45,207	9.0	
Randall-Story State Bank	8,521	10.7		3,183	4.0		3,978	5.0	
State Bank & Trust	13,755	9.9		5,547	4.0		6,933	5.0	
United Bank & Trust	10,201	9.5		4,289	4.0		5,361	5.0	

Table of Contents

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2009:						
Total capital (to risk-weighted assets):						
Consolidated	$116,366	17.6 %	$52,994	8.0 %	N/A	N/A
Boone Bank & Trust	12,845	17.3	5,925	8.0	$7,407	10.0 %
First National Bank	47,179	13.8	37,656	11.0	37,656	11.0
Randall-Story State Bank	8,936	14.7	4,866	8.0	6,083	10.0
State Bank & Trust	13,740	13.8	7,981	8.0	9,976	10.0
United Bank & Trust	9,497	15.0	5,229	8.0	6,536	10.0
Tier 1 capital (to risk-weighted assets):						
Consolidated	$108,348	16.4 %	$26,497	4.0 %	N/A	N/A
Boone Bank & Trust	12,021	16.2	2,963	4.0	$4,444	6.0 %
First National Bank	43,974	12.9	13,693	4.0	20,539	6.0
Randall-Story State Bank	8,179	13.5	2,433	4.0	3,650	6.0
State Bank & Trust	12,491	12.5	3,990	4.0	5,985	6.0
United Bank & Trust	8,995	13.8	2,614	4.0	3,922	6.0
Tier 1 capital (to average-weighted assets):						
Consolidated	$108,348	12.0 %	$36,187	4.0 %	N/A	N/A
Boone Bank & Trust	12,021	11.5	4,185	4.0	$5,232	5.0 %
First National Bank	43,974	9.5	41,504	9.0	41,504	9.0
Randall-Story State Bank	8,179	10.6	3,085	4.0	3,856	5.0
State Bank & Trust	12,491	9.0	5,563	4.0	6,954	5.0
United Bank & Trust	8,995	8.3	4,347	4.0	5,433	5.0

Federal and state banking regulations place certain restrictions on dividends paid and loans or advances made by the Banks to the Company. Dividends paid by each Bank to the Company would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum capital requirements. Except for the potential effect on the Company's level of dividends, management believes that these restrictions currently do not have a significant impact on the Company.

Table of Contents

Note 13. Fair Value of Financial Instruments

The estimated fair values of the Company's financial instruments (as described in Note 1) are as follows:

	2010		2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and due from banks	$15,478,133	$15,478,000	$18,796,664	$18,797,000
Federal funds sold	3,000,000	3,000,000	—	—
Interest bearing deposits	19,229,814	19,230,000	24,766,088	24,766,000
Securities available-for-sale	469,907,901	469,908,000	418,655,018	418,655,000
Loans receivable, net	418,093,571	415,833,000	415,434,236	411,344,000
Loans held for sale	1,993,108	1,993,000	1,023,200	1,023,000
Accrued income receivable	6,098,535	6,099,000	5,710,226	5,710,000
Financial liabilities:				
Deposits	$743,861,644	$746,401,000	$722,163,949	$725,840,000
Federal funds purchased and securities sold under agreements to repurchase	54,858,701	54,859,000	40,489,505	40,490,000
Other short-term borrowings	2,047,175	2,047,000	138,874	139,000
FHLB and other long-term borrowings	36,745,497	39,303,000	36,500,000	41,504,000
Accrued interest payable	870,455	870,000	1,092,191	1,092,000

Note 14. Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact, and (iv) willing to transact.

Table of Contents

The standards require the use of valuation techniques that are consistent with the market approach, the income approach, and/or the cost approach. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement cost). Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. In that regard, a fair value hierarchy was established for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

Level 1: Inputs to the valuation methodology are quoted prices, unadjusted, for identical assets or liabilities in active markets. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.

Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; inputs to the valuation methodology include quoted prices for identical or similar assets or liabilities in markets that are not active; or inputs to the valuation methodology that are derived principally from or can be corroborated by observable market data by correlation or other means.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement. Level 3 assets and liabilities include financial instruments whose value is determined using discounted cash flow methodologies, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Table of Contents

The following table presents the balances of assets measured at fair value on a recurring basis by level as of December 31, 2010 and 2009:

Description	Total	Quoted Prices in Active markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
2010				
U.S. treasury	$503,000	$503,000	$—	$ —
U.S. government agencies	87,413,000	—	87,413,000	—
U.S. government mortgage-backed securities	127,349,000	—	127,349,000	—
State and political subdivisions	228,373,000	—	228,373,000	—
Corporate bonds	20,372,000	—	20,372,000	—
Equity securities, financial industry common stock	2,814,000	2,814,000	—	—
Equity securities, other	3,084,000	18,000	3,066,000	—
	$469,908,000	$3,335,000	$466,573,000	$ —
2009				
U.S. treasury	$525,000	$525,000	$—	$ —
U.S. government agencies	106,640,000	—	106,640,000	—
U.S. government mortgage-backed securities	101,589,000	—	101,589,000	—
State and political subdivisions	178,052,000	—	178,052,000	—
Corporate bonds	24,300,000	—	24,300,000	—
Equity securities, financial industry common stock	2,347,000	2,347,000	—	—
Equity securities, other	5,202,000	2,023,000	3,179,000	—
	$418,655,000	$4,895,000	$413,760,000	$ —

Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, as well as U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets. Level 2 securities include U.S. government agency securities, mortgage-backed securities (including pools and collateralized mortgage obligations), municipal bonds, and corporate debt securities.

Table of Contents

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 table presents the assets carried on the balance sheet (after specific reserves) by caption and by level with the valuation hierarchy as of December 31, 2010 and 2009:

Description	Total	Quoted Prices in Active markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
2010				
Loans	$3,660,000	$—	$—	$ 3,660,000
Other real estate owned	10,539,000	—	—	10,539,000
Total	$14,199,000	$—	$—	$ 14,199,000
2009				
Loans	$4,807,000	$—	$—	$ 4,807,000
Other real estate owned	10,480,000	—	—	10,480,000
Total	$15,287,000	$—	$—	$ 15,287,000

Loans in the tables above consist of impaired credits held for investment. Impaired loans are valued by management based on collateral values underlying the loans. Management uses original appraised values and adjusts for trends observed in the market to determine the value of impaired loans. Other real estate owned in the table above consists of real estate obtained through foreclosure. Management uses appraised values and adjusts for trends observed in the market and for disposition costs in determining the value of other real estate owned.

Note 15. Subsequent Events

Management evaluated subsequent events through the date the financial statements were issued. There were no significant events or transactions occurring after December 31, 2010, but prior to March 10, 2011, that provided additional evidence about conditions that existed at December 31, 2010. There were no significant events or transactions that provided evidence about conditions that did not exist at December 31, 2010.

Table of Contents

Note 16. Ames National Corporation (Parent Company Only) Financial Statements

Information relative to the Parent Company's balance sheets at December 31, 2010 and 2009, and statements of income and cash flows for each of the years in the three-year period ended December 31, 2010, is as follows:

CONDENSED BALANCE SHEETS
December 31, 2010 and 2009

	2010	2009
ASSETS		
Cash and due from banks	$50,761	$26,797
Interest bearing deposits in banks	7,982,501	1,513,234
Securities available-for-sale	4,320,665	6,336,488
Investment in bank subsidiaries	98,915,881	89,613,176
Loans receivable, net	9,724,213	13,859,423
Premises and equipment, net	573,580	603,571
Accrued income receivable	76,920	104,081
Deferred income taxes	810,516	976,000
Other real estate owned	78,925	197,313
Other assets	15,000	260,955
Total assets	$122,548,962	$113,491,038
LIABILITIES		
Dividends payable	$1,037,621	$943,292
Accrued expenses and other liabilities	148,317	207,858
Total liabilities	1,185,938	1,151,150
STOCKHOLDERS' EQUITY		
Common stock	18,865,830	18,865,830
Additional paid-in capital	22,651,222	22,651,222
Retained earnings	76,519,493	67,703,701
Accumulated other comprehensive income	3,326,479	3,119,135
Total stockholders' equity	121,363,024	112,339,888
Total liabilities and stockholders' equity	$122,548,962	$113,491,038

Table of Contents

CONDENSED STATEMENTS OF INCOME
Years Ended December 31, 2010, 2009 and 2008

	2010	2009	2008
Operating income:			
Equity in net income of bank subsidiaries	$ 13,418,456	$ 9,519,040	$ 5,125,234
Interest	954,867	1,087,714	759,461
Dividends	96,094	181,137	673,506
Rents	114,372	96,765	88,624
Other	30,568	76,005	—
Securities gains (losses), net	(12,152)	(17,163)	3,171,215
Other-than-temporary impairment of investment securities	—	—	(903,600)
	14,602,205	10,943,498	8,914,440
Provision (credit) for loan losses	(50,000)	300,000	327,558
Operating income after provision (credit) for loan losses	14,652,205	10,643,498	8,586,882
Operating expenses	1,992,131	2,099,212	1,934,886
Income before income taxes	12,660,074	8,544,286	6,651,996
Income tax expense (benefit)	(306,200)	(461,500)	300,000
Net income	$ 12,966,274	$ 9,005,786	$ 6,351,996

Table of Contents

CONDENSED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2010, 2009 and 2008

	2010	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$12,966,274	$9,005,786	$6,351,996
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	39,136	46,522	54,970
Provision (credit) for loan losses	(50,000)	300,000	327,558
Amortization and accretion, net	(1,091)	(713)	(18,734)
Provision for deferred income taxes	(83,000)	(164,919)	(123,005)
Securities losses (gains), net	12,152	17,163	(3,171,215)
Other-than-temporary impairment of investment securities	—	—	903,600
Gain on sale of other real estate owned	(30,568)	(47,146)	—
Equity in net income of bank subsidiaries	(13,418,456)	(9,519,040)	(5,125,234)
Dividends received from bank subsidiaries	3,900,000	3,560,000	8,864,000
Decrease in accrued income receivable	27,161	75,330	29,768
Decrease (increase) in other assets	245,955	(17,294)	(176,535)
Decrease in accrued expense payable and other liabilities	(59,541)	(3,723)	(131,592)
Net cash provided by operating activities	3,548,022	3,251,966	7,785,577
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of securities available-for-sale	—	—	(9,303,034)
Proceeds from sale of securities available-for-sale	2,176,341	4,211,087	13,159,215
Proceeds from maturities and calls of securities available-for-sale	500,000	150,000	3,385,000
Decrease (increase) in interest bearing deposits in banks	(6,469,267)	(1,411,257)	9,885,910
Decrease (increase) in loans	4,185,210	3,986,345	(18,746,876)
Proceeds from the sale of other real estate owned	148,956	323,383	—
Purchase of bank premises and equipment	(9,145)	(4,984)	(3,267)
Investment in bank subsidiaries	—	(850,000)	—
Net cash provided by (used in) investing activities	532,095	6,404,574	(1,623,052)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from other borrowings, net	—	—	4,160,000
Payments of other borrowings, net	—	(4,160,000)	—
Dividends paid	(4,056,153)	(5,471,090)	(10,468,702)
Proceeds from issuance of stock	—	—	69,201
Net cash used in financing activities	(4,056,153)	(9,631,090)	(6,239,501)
Net increase (decrease) in cash and cash equivalents	23,964	25,450	(76,976)
CASH AND DUE FROM BANKS			
Beginning	26,797	1,347	78,323
Ending	$50,761	$26,797	$1,347
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Cash payments for interest	$—	$59,432	$29,460

Cash payments (receipts) for income taxes	(393,829)	(276,531)	793,080
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING ACTIVITIES			
Transfer of loans to other real estate owned	$—	$473,550	$—

107

Table of Contents

Note 17. Selected Quarterly Financial Data (Unaudited)

	2010			
	March 31	June 30	September 30	December 31
Total interest income	$9,422,695	$9,353,203	$9,421,463	$9,096,597
Total interest expense	2,065,512	1,965,914	1,907,511	1,836,154
Net interest income	7,357,183	7,387,289	7,513,952	7,260,443
Provision for loan losses	323,798	170,416	74,197	95,387
Net income	3,269,600	3,126,006	3,551,311	3,019,357
Basic and diluted earnings per common share	0.35	0.33	0.38	0.32

	2009			
	March 31	June 30	September 30	December 31
Total interest income	$10,117,472	$9,826,268	$9,522,916	$9,424,651
Total interest expense	2,909,914	2,659,648	2,419,581	2,237,169
Net interest income	7,207,558	7,166,620	7,103,335	7,187,482
Provision for loan losses	229,654	326,670	635,171	366,812
Net income	2,441,140	2,408,905	2,573,567	1,582,174
Basic and diluted earnings per common share	0.26	0.26	0.27	0.17

Table of Contents

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

As of the end of the period covered by this report, an evaluation was performed under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer of the effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)). Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that the Company's current disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms.

Management's annual report on internal control over financial reporting is contained in Item 8 of this Report.

The attestation report of the Company's registered public accounting firm on the Company's internal control over financial reporting is contained in Item 8 of this Report.

There were no changes in the Company's internal control over financial reporting that occurred during the quarter ended December 31, 2010 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERANCE

Directors

Refer to the information under the captions "Corporate Governance" and "Proposals to be Voted on at Meeting – Proposal 1 – Election of Directors" contained in the Company's definitive proxy statement prepared in connection with its Annual Meeting of Shareholders to be held April 27, 2011, as filed with the SEC on March 18, 2011 (the "Proxy Statement"), which information is incorporated herein by this reference.

Executive Officers

The information required by Item 10 regarding the executive officers appears in Item 1 of Part I of this Report under the heading "Executive Officers of the Company and Banks".

Section 16(a) Beneficial Ownership Reporting Compliance

Table of Contents

Refer to the information under the caption "Section 16(a) Beneficial Ownership Reporting Compliance" in the Proxy Statement, which information is incorporated herein by this reference.

Audit Committee

The Company has established an Audit Committee as a standing committee of the Board of Directors. Refer to the information under the caption "Corporate Governance – Board Committees" in the Proxy Statement, which information is incorporated herein by this reference.

Audit Committee Financial Expert

The Board of Directors of the Company has determined that Warren R. Madden, a member of the Audit Committee, qualifies as an "audit committee financial expert" under applicable SEC rules. The Board of Directors has further determined that Mr. Madden qualifies as an "independent" director under applicable SEC rules and the corporate governance rules of the NASDAQ stock market. The Board's affirmative determination was based, among other things, upon Mr. Madden's experience as Vice President of Finance and Business of Iowa State University, a position in which he functions as the principal financial officer of the University.

Code of Ethics

The Company has adopted an Ethics and Confidentiality Policy that applies to all directors, officers and employees of the Company, including the Chief Executive Officer and the Chief Financial Officer of the Company. A copy of this policy is posted on the Company's website at www.amesnational.com. In the event that the Company makes any amendments to, or grants any waivers of, a provision of the Ethics and Confidentiality Policy that requires disclosure under applicable SEC rules, the Company intends to disclose such amendments or waiver and the reasons therefor on its website.

ITEM 11. EXECUTIVE COMPENSATION

Refer to the information under the caption "Executive Compensation" in the Proxy Statement, which information is incorporated herein by this reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED SHAREHOLDER MATTERS

Refer to the information under the caption "Security Ownership of Management and Certain Beneficial Owners" in the Proxy Statement, which information is incorporated herein by this reference. The Company does not maintain any equity compensation plans covering its directors, officers or employees or the directors, officers or employees of the Banks.

ITEM 13. CERTAIN RELATIONSHIPS, RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

Refer to the information under the captions "Loans to Directors and Executive Officers and Related Party Transactions" and "Corporate Governance – Director Independence" in the Proxy Statement, which information is incorporated herein by this reference.

Table of Contents

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Refer to the information under the caption "Relationship with Registered Public Accounting Firm" in the Proxy Statement, which information is incorporated herein by this reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) List of Financial Statements and Schedules.

1. Financial Statements

Reports of Clifton Gunderson LLP, Independent Registered Public Accounting Firm	68
Consolidated Balance Sheets, December 31, 2010 and 2009	71
Consolidated Statements of Income for the Years ended December 31, 2010, 2009 and 2008	72
Consolidated Statements of Stockholders' Equity for the Years ended December 31, 2010, 2009 and 2008	73
Consolidated Statements of Cash Flows for the Years ended December 31, 2010, 2009 and 2008	74
Notes to Consolidated Financial Statements	76

2. Financial Statement Schedules

All schedules are omitted because they are not applicable or not required, or because the required information is included in the consolidated financial statements or notes thereto.

(b) List of Exhibits.

3.1	-	Restated Articles of Incorporation of the Company, as amended (incorporated by reference to Exhibit 3.1 to Form 8-K as filed June 16, 2005)
3.2	-	Bylaws of the Company, as amended (incorporated by reference to Exhibit 3.2 to Form 8-K as filed February 19, 2008)
10.1	-	Management Incentive Compensation Plan (incorporated by reference to Exhibit 10 filed with the Company's Annual Report on Form 10K for the year ended December 31, 2002)*
21	-	Subsidiaries of the Registrant
23	-	Consent of Independent Registered Public Accounting Firm
31.1	-	Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	-	Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	-	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350
32.2	-	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350
	*	Indicates a management compensatory plan or arrangement.

Table of Contents

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

	AMES NATIONAL CORPORATION	
March 10, 2011	By:	/s/ Thomas H. Pohlman Thomas H. Pohlman, President

Table of Contents

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated and on March 10, 2011.

/s/ Thomas H. Pohlman
Thomas H. Pohlman, President
(Principal Executive Officer)

/s/ John P. Nelson
John P. Nelson, Vice President
(Principal Financial and Accounting Officer)

/s/ Betty A. Baudler Horras
Betty A. Baudler Horras, Director

/s/ Robert L. Cramer
Robert L. Cramer, Director

/s/ Douglas C. Gustafson
Douglas C. Gustafson, Director

/s/ Charles D. Jons
Charles D. Jons, Director

/s/ Steven D. Forth
Steven D. Forth, Director

/s/ James R. Larson II
James R. Larson II, Director

/s/ Warren R. Madden
Warren R. Madden, Director

/s/ Larry A. Raymon
Larry A. Raymon, Director

/s/ Fred C. Samuelson
Fred C. Samuelson, Director

/s/ Marvin J. Walter
Marvin J. Walter, Director

Table of Contents

EXHIBIT INDEX

The following exhibits are filed herewith:

Exhibit No.	Description
21	-Subsidiaries of the Registrant
23	-Consent of Independent Registered Public Accounting Firm.
31.1	-Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002
31.2	-Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002
32.1	-Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350
32.2	-Certification of Principal Financial Officer pursuant to 18 U.S.C. Section 1350