McGladrey & Pullen
Certified Public Accountants
Independent Auditor's Report

To the Shareholders and Board of Directors
Independent Bankers Financial Corporation and Subsidiaries
Irving, Texas

We have audited the accompanying consolidated balance sheets of Independent Bankers Financial Corporation and Subsidiaries (the Corporation) as of December 31, 2007 and 2006, and the related consolidated statements of income, changes in shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Independent Bankers Financial Corporation and Subsidiaries as of December 31, 2007 and 2006, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

McGladrey & Pullen, LLP

Dallas, Texas
March 17, 2008

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Independent Bankers Financial Corporation and Subsidiaries

Consolidated Balance Sheets at December 31, 2007 and 2006

(Dollar Amounts in Thousands, except per share amounts)

ASSETS	2007	2006
Cash due from banks (Note 1)	$ 23,453	$ 46,162
Interest-bearing deposits	517	602
Federal funds sold and securities purchased under agreements to resell (Note 1)	720,458	386,352
Total cash equivalents	744,428	433,116
Interest-bearing time deposits	100	300
Securities available for sale (Note 2)	228,261	373,951
Loans held for sale	54,042	23,804
Loans, net (Note 3)	724,070	671,383
Premises and equipment, net (Note 4)	4,864	5,195
Other real estate owned, net (Note 5)	3,460	2,112
Mortgage servicing rights (Note 6)	30,756	32,109
Accrued interest receivable	7,680	8,464
Due from broker	9,789	2,847
Cash surrender value of life insurance	22,462	21,625
Intangible assets, net (Note 11)	3,546	4,795
Other assets	29,571	25,915
Total assets	$ 1,863,029	$ 1,605,616
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits (Note 9):		
Noninterest-bearing	$ 172,756	$ 152,836
Interest-bearing	230,745	213,140
Total deposits	403,501	365,976
Federal funds purchased and securities sold under agreements to repurchase (Note 1)	1,244,708	997,770
Accrued interest payable and other liabilities (Note 14)	35,065	23,762
Other borrowings (Note 10)	50,000	100,000
Junior subordinated debentures (Note 12)	30,928	30,928
Total liabilities	1,764,202	1,518,436
Commitments and contingencies (Note 17)	-	-
Shareholders' equity (Note 19):		
Common stock, par value $10 per share, 5,000,000 shares authorized, 1,091,796 and 1,085,825 shares issued and outstanding in 2007 and 2006	10,918	10,858
Capital surplus	23,391	21,005
Retained earnings	67,953	59,082
Accumulated other comprehensive loss	$ (3,435)	(3,765)
Total shareholders' equity	98,827	87,180
Total liabilities and shareholders' equity	$ 1,863,029	$ 1,605,616

See Notes to Consolidated Financial Statements.

Independent Bankers Financial Corporation and Subsidiaries

Consolidated Statement of Income for the Years Ended December 31, 2007 and 2006

(Dollar Amounts in Thousands)

	2007	2006
Interest income:		
Loans, including fees - taxable	$ 46,887	$ 41,240
Loans , including fees - tax exempt	6,226	4,587
Securities - taxable	11,918	17,427
Federal funds sold and repurchase agreements	35,388	27,010
Other	458	503
Total interest income	100,877	90,767
Interest expense:		
Deposits	13,438	8,036
Federal funds purchased and repurchase agreements	59,860	55,420
Junior subordinated debentures and other borrowings	3,736	5,502
Total interest expense	77,034	68,958
Net interest income	23,843	21,809
Provision for loan losses (Note 3)	2,754	-
Net interest income after provision for loan losses	21,089	21,809
Noninterest income (Note 15)	93,465	70,397
Noninterest expense:		
Salaries and benefits	31,015	28,732
Premises, furniture and equipment	2,965	2,889
Telephone expense	1,283	1,128
Software maintenance	1,303	1,784
Credit card expenses	39,646	28,173
Mortgage operation expense	1,532	1,766
Net loss on derivative transactions	-	448
MSR fair value adjustment	10,146	1,601
Item processing expense	1,774	1,927
Intangible amortization	1,248	898
Professional fees	1,354	1,656
Other operating expenses	8,954	7,983
Total noninterest expense	101,220	78,985
Income before income taxes	13,334	13,221
Federal income taxes (Note 13):		
Current expense	2,246	1,548
Deferred expense	580	1,668
	2,826	3,216
Net income	$ 10,508	$ 10,005

See Notes to Consolidated Financial Statements.

Independent Bankers Financial Corporation and Subsidiaries

Consolidated Statements of Changes in Shareholders' Equity for the Years Ended December 31, 2007 and 2006

(Dollar Amounts in Thousands , except per share amounts)

	Common Stock	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance at December 31, 2005	$ 10,600	$ 19,167	$ 50,598	$ (6,039)	$ 74,326
Comprehensive income:					
Net income	-	-	10,005	-	10,005
Change in fair value of securities available for sale, net of tax effect of $1,333	-	-	-	2,587	2,587
Change in fair value of Fed Funds Swap, net of tax effect of $(162)	-	-	-	(313)	(313)
Total comprehensive income					12,279
Purchase and retirement of common stock (3,673 shares)	(36)	(220)	-	-	(256)
Sale of common stock (29,424 shares)	294	2,058	-	-	2,352
Common stock dividend declared ($1.40 per share)	-	-	(1,521)	-	(1,521)
Balance at December 31, 2006	10,858	21,005	59,082	(3,765)	87,180
Comprehensive income:					
Net income	-	-	10,508	-	10,508
Change in fair value of securities available for sale, net of reclassification adjustment of $47 and tax effect of $1,617	-	-	-	3,138	3,138
Change in fair value of Fed Funds Swap, net of reclassification adjustment of $167 and net of tax effect of $(1,446)	-	-	-	(2,808)	(2,808)
Total comprehensive income					10,838
Purchase and retirement of common stock (34,459 shares)	(344)	(748)	-	-	(1,092)
Sale of common stock (40,430 shares)	404	3,134	-	-	3,538
Common stock dividend declared ($1.50 per share)	-	-	(1,637)	-	(1,637)
Balance at December 31, 2007	**$ 10,918**	**$ 23,391**	**$ 67,953**	**$ (3,435)**	**$ 98,827**

See Notes to Consolidated Financial Statements.

Independent Bankers Financial Corporation and Subsidiaries

Consolidated Statements of Cash Flows for the Years Ended December 31, 2007 and 2006

(Dollar Amounts in Thousands)

	2007	2006
Cash flows from operating activities:		
Net income	$ 10,508	$ 10,005
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization	4,518	4,812
Provision for loan losses	2,754	-
Deferred taxes	580	1,668
Deferred compensation expense	1,461	1,515
Increase in valuation allowance for mortgage servicing rights	10,146	2,099
Net gain on sale of loans	(2,936)	(2,133)
Net (gain) loss on derivative securities	(6,668)	448
Other	(321)	(16)
Increase in cash surrender value of life insurance	(837)	(789)
Changes in operating assets and liabilities, net of effects of acquisition:		
Loans held for sale	(27,472)	(14,082)
Accrued interest receivable	784	(1,476)
Other assets	(7,689)	(1,350)
Accrued interest payable and other liabilities	8,625	2,648
Net cash (used in) provided by operating activities	(6,547)	3,349
Cash flows from investing activities:		
Securities available for sale:		
Purchases	(600)	(19,967)
Proceeds from sales	30,059	-
Proceeds from maturities, calls and principal repayments	119,956	93,341
Maturities of interest bearing time deposits	200	200
Purchases of mortgage servicing rights	(8,398)	(14,285)
Net increase in loans	(58,742)	(114,727)
Proceeds from redemption of junior subordinated debentures	-	620
Purchase of junior subordinated debentures	-	(928)
Proceeds from sales of assets	2,118	530
Purchases of premises and equipment	(1,122)	(1,642)
Acquisitions, net of cash acquired (Note 16)	(1,000)	(3,500)
Net cash provided by (used in) investing activities	82,471	(60,358)
Cash flows from financing activities:		
Net change in deposits	37,525	(85,851)
Net change in federal funds purchased and securities sold under agreements to repurchase	246,938	212,435
Net change in other borrowings	(50,000)	-
Repurchase of junior subordinated debentures	-	(20,620)
Issuance of junior subordinated debentures	-	30,928
Repurchase and retirement of common stock	(1,092)	(256)
Net proceeds from issuance of common stock	3,538	2,352
Dividends paid	(1,521)	(1,378)
Net cash provided by financing activities	235,388	137,610
Net increase in cash equivalents	311,312	80,601
Cash equivalents at beginning of year	433,116	352,515
Cash equivalents at end of year	$ 744,428	$ 433,116
Supplemental cash flow information:		
Cash paid for interest	$ 77,391	$ 68,383
Cash paid for taxes	2,207	3,093
Real estate acquired in foreclosure or in settlement of loans	58	30

See Notes to Consolidated Financial Statements.

Note 1. Summary of Significant Accounting Policies

The consolidated financial statements of Independent Bankers Financial Corporation and Subsidiaries (Corporation) have been prepared in accordance with accounting principles generally accepted in the United States of America. The consolidated financial statements include the accounts of Independent Bankers Financial Corporation (IBFC), IBFC Nevada Corporation, TIB-The Independent BankersBank (Bank), and other nonbanking subsidiaries, including ALX Consulting, Inc., Bankers Bank Card Services Company (BBCS) and TIB Service Company. In addition, the Corporation wholly-owns IBFC Statutory Capital Trust II. See Note 12 for further discussion regarding the Trust. The Bank is an entity which is defined by statute as a "bankers' bank". The statute requires all of the shareholders of the Bank to be depository institutions or holding companies for depository institutions and that the Bank provide services only for depository institutions or at the request of depository institutions. In this context, the Bank provides various banking and banking-related services to financial institutions primarily in Texas, New Mexico, Oklahoma, Arizona, Louisiana and California, many of which are shareholders of the Corporation.

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 requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent 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 these estimates. The allowance for loan losses and fair values of mortgage servicing rights and financial instruments are particularly subject to change.

Cash Flow Reporting

Cash equivalents include cash items, amounts due from banks, deposits with other financial institutions that have an initial maturity under 90 days when acquired by the Corporation, federal funds sold, and securities purchased under agreements to resell. Net cash flows are reported for loans, loans held for sale, deposit transactions and short-term borrowings.

Repurchase/Resell Agreements

The Corporation purchases certain securities under agreements to resell. The amounts advanced under these agreements represent short-term loans and are reflected as assets in the consolidated balance sheet. The securities underlying these agreements are book-entry securities. At December 31, 2007 and 2006, there were no resell agreements outstanding. The Corporation also sells certain securities under agreements to repurchase. The agreements are treated as financings, and the obligations to repurchase securities sold are reflected as a liability in the consolidated balance sheet. The dollar amount of securities underlying the agreements remains in the asset accounts. At December 31, 2007 and 2006, repurchase agreements outstanding were $4,900 and $1,967, respectively, and mature within 90 days.

Securities

Securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Securities are classified as available for sale when they might be sold before maturity. Securities available for sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income. Management determines the appropriate classification of securities at the time of purchase.

Interest income includes amortization of purchase premiums and discounts. Gains and losses on sales of securities are recorded on the trade date and are determined using the specific identification method. Declines in the fair value of held-to-maturity and 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 length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Loans Held for Sale

The Corporation originates mortgage and student loans for portfolio investment or sale in the secondary market. During the period of origination, mortgage loans are designated as held either for sale or investment purposes. Mortgage and student loans held for sale are carried at the lower of cost or market value, determined on a net aggregate basis. Gains or losses recognized upon the sale of loans are determined on a specific identification basis.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding unpaid principal balances adjusted for charge offs and the allowance for loan losses. Interest income is accrued on the unpaid principal balance.

The accrual of interest is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due. All interest accrued but not collected for loans that are placed on non-accrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Loan and Lease Losses

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

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

The allowance consists of specific and general components. The specific component relates to loans that are classified as either doubtful, substandard or special mention. For such loans and leases that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors.

A loan is considered impaired when, based on current information and events, it is probable that the Corporation will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Corporation does not separately identify such loans for impairment disclosures, unless such loans are the subject of a restructuring agreement.

Premises and Equipment

Land is carried at cost. Building and improvements, and furniture and equipment are carried at cost, less accumulated depreciation computed principally by the straight-line method based on the estimated useful lives of the related properties.

Other Real Estate Owned

Other real estate acquired through or instead of loan foreclosure is initially recorded at fair value when acquired, establishing a new cost basis. Costs after acquisition are expensed. If the fair value of the property declines, a valuation allowance is recorded through expense.

Mortgage Servicing Rights

Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. Generally, purchased servicing rights are capitalized at the cost to acquire the rights. For sales of mortgage loans, a portion of the cost of originating the loan is allocated to the servicing right based on relative fair value. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses.

Mortgage servicing rights are recorded at fair value. Any changes in fair value are included in earnings in the period in which the changes occur.

Servicing fee income is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal or a fixed amount per loan, and are recorded as income when earned.

Long-Lived Assets

Intangible assets, premises and equipment and other long-lived assets are tested for impairment whenever events or changes in circumstances indicate the carrying amount of the assets may not be recoverable from future undiscounted cash flows. If impaired, the assets are recorded at fair value.

Term Federal Funds

The Corporation buys term federal funds as an alternative investment for customer banks. Term federal funds are reflected as a liability on the consolidated balance sheet. At December 31, 2007 and 2006, term federal funds outstanding were $26,100 and $12,400, respectively, and mature within 120 days.

Income Taxes

Deferred taxes are provided on the liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and the tax credit carryforwards, and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between reported amounts of assets and liabilities and their tax basis. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates or the date of enactment.

Federal Funds Transactions as Agent

The Corporation acts as an agent for customer banks to purchase and sell federal funds. The Corporation acts as an intermediary for the receipt and disbursement of funds but is not otherwise obligated by the transactions. These transactions are not reflected in the Corporation's financial statements except for fees earned. At December 31, 2007 and 2006, the Corporation was agent for total federal funds transactions of $1,237,000 and $1,740,000, respectively.

Derivative Financial Instruments

The Corporation's hedging policies permit the use of various derivative financial instruments to manage interest rate risk or to hedge specified assets and liabilities. All derivatives are recorded at fair value on the Corporation's balance sheet. To qualify for hedge accounting, derivatives must be highly effective at reducing the risk associated with the exposure being hedged and must be designated as a hedge at the inception of the derivative contract. If derivative instruments are designated as hedges of fair values, both the change in the fair value of the hedge and the hedged item are included in current earnings. Fair value adjustments related to cash flow hedges are recorded in other comprehensive income and reclassified to earnings when the hedged transaction is reflected in earnings. Ineffective portions of hedges are reflected in earnings as they occur. During the life of the hedge, the Corporation formally assesses whether derivatives designated as hedging instruments continue to be highly effective in offsetting changes in the fair value or cash flows of hedged items. If it is determined that a hedge has ceased to be highly effective, the Corporation will discontinue hedge accounting prospectively.

Fair Values of Financial Instruments

Fair values of financial instruments are estimated using relevant market information and other assumptions. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates. The fair value estimates of existing on- and off-balance sheet financial instruments do not include the value of anticipated future business or the value of assets and liabilities not considered financial instruments.

Loss Contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated.

Dividend Restriction

Banking regulations require the maintenance of certain capital and net income levels that may limit the amount of dividends that may be paid. Approval by regulatory authorities is required if the effect of dividends declared would cause the regulatory capital of the Bank to fall below specified minimum levels. Regulatory capital requirements are more fully disclosed in a separate note.

Restrictions on Cash

The Corporation was required to have $15,029 and $12,713 of cash on hand or on deposit with the Federal Reserve Bank to meet regulatory reserve and clearing requirements at December 31, 2007 and 2006, respectively. Deposits with the Federal Reserve Bank do not earn interest.

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities and fed funds swaps, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income. Gains and losses on available for sale securities 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. Gains and losses on fed funds swaps are reclassified to net income over the remaining contract term if a swap is exited before the termination date.

Reclassifications

Certain reclassifications have been made to the prior year financial statements to conform to the current year presentation. Such reclassifications had no effect on net income or shareholders' equity.

Effect of Newly Issued But Not Yet Effective Accounting Standards

The Financial Accounting Standard Board ("FASB") recently issued the following accounting standards:

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement 109." FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, "Accounting for Income Taxes." FIN 48 prescribes a comprehensive model for recognizing, measuring, presenting and disclosing in the financial statements tax positions taken or expected to be taken on a tax return. If there are changes in net assets as a result of application of FIN 48 these will be accounted for as an adjustment to the opening balance of retained earnings. Additional disclosures about the amounts of such liabilities will be required also. In February 2008, the FASB delayed the effective date of FIN 48 for certain nonpublic enterprises to annual financial statements for fiscal years beginning after December 15, 2007. The Company will be required to adopt FIN 48 in its 2008 annual financial statements. Management is currently assessing the impact of FIN 48.

SFAS No. 141, "Business Combinations (Revised 2007)."SFAS 141R replaces SFAS 141, "Business Combinations", and applies to all transactions and other events in which one entity obtains control over one or more other businesses. SFAS 141R requires an acquirer, upon initially obtaining control of another entity, to recognize the assets, liabilities and any non-controlling interest in the acquiree at fair value as of the acquisition date. Contingent consideration is required to be recognized and measured at fair value on the date of acquisition rather than at a later date when the amount of that consideration may be determinable beyond a reasonable doubt. This fair value approach replaces the cost-allocation process required under SFAS 114 whereby the cost of an acquisition was allocated to the individual assets acquired and liabilities assumed based on their estimated fair value. SFAS 141R requires acquirers to expense acquisition-related costs as incurred rather than allocating such costs to the assets acquired and liabilities assumed, as was previously the case under SFAS 141. Under SFAS 141R, the requirements of SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities", would have to be met in order to accrue for a restructuring plan in purchase accounting. Pre-acquisition contingencies are to be recognized at fair value, unless it is a non-contractual contingency that is not likely to materialize, in which case, nothing should be recognized in purchase accounting and, instead, that contingency would be subject to the probable and estimable recognition criteria of SFAS 5, "Accounting for Contingencies". SFAS 141R is effective for business combinations occurring on or after January 1, 2009.

SFAS No. 160, "Noncontrolling Interest in Consolidated Financial Statements, an amendment of ARB Statement No. 51". SFAS 160 amends Accounting Research Bulletin (ARB) NO. 51, "Consolidated Financial Statements", to establish accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 clarifies that a non-controlling interest in a subsidiary, which is sometimes referred to as minority interest, is an ownership interest in the consolidated entity that should be reported as a component of equity in the consolidated financial statements. Among other requirements, SFAS 160 requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the non-controlling interest. It also requires disclosure, on the face of the consolidated income statement, of the amounts of consolidated net income attributable to the parent and to the non-controlling interest. SFAS 160 is effective for the Corporation on January 1, 2009 and is not expected to have a significant impact on the Corporation's financial statements.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements". This statement defines fair value, establishes a framework for measuring fair value in accordance with United States generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 is effective for the fiscal year that begins after November 15, 2007. The Corporation will adopt this standard beginning in January 2008. Currently, management is evaluating the impact that this new standard will have on the Corporation's financial position, results of operations and cash flows.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities". SFAS No. 159 permits entities to choose to measure many financial assets and financial liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected will be reported in earnings. SFAS No. 159 is optional and effective for fiscal years beginning after November 15, 2007. The Corporation will adopt SFAS No. 159 in 2008. The Corporation does not expect the adoption of SFAS No. 159 to have a material impact on its financial position, results of operations or cash flows.

Note 2. Securities Available for Sale

Securities available for sale consisted of the following:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
December 31, 2007:				
U.S. government agencies	**$ 85,192**	**$ 253**	**$ 192**	**$ 85,253**
Mortgage-backed securities	**142,934**	**419**	**966**	**142,387**
Municipal securities	**600**	**1**	**-**	**601**
Other equity securities	**10**	**10**	**-**	**20**
	$ 228,736	**$ 683**	**$ 1,158**	**$ 228,261**
December 31, 2006:				
U.S. government agencies	$ 200,809	$ 85	$ 2,594	$ 198,300
Mortgage-backed securities	178,364	38	2,780	175,622
Other equity securities	9	20	-	29
	$ 379,182	$ 143	$ 5,374	$ 373,951

Mortgage-backed securities are backed by pools of mortgages that are insured or guaranteed by the Federal Home Loan Mortgage Corporation ("FHLMC"), the Government National Mortgage Corporation ("GNMA") or the Federal National Mortgage Corporation ("FNMA").

At December 31, 2007, there were no holdings of securities of any one issuer, other than the U.S. government and its agencies, in an amount greater than 10% of shareholders' equity.

Unrealized losses, fair value and length of time that individual securities have been in a continuous unrealized loss position as of December 31, 2007 and 2006 are summarized as follows:

	Continuous Unrealized Losses Existing for Less than 12 Months		Continuous Unrealized Losses Existing for Greater than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2007:						
U.S. government agencies	**$ -**	**$ -**	**$ 39,975**	**$ 192**	**$ 39,975**	**$ 192**
Mortgage-backed securities	**2,022**	**16**	**79,381**	**950**	**81,403**	**966**
	$ 2,022	**$ 16**	**$ 119,356**	**$ 1,142**	**$ 121,378**	**$ 1,158**
December 31, 2006:						
U.S. government agencies	$ -	$ -	$ 178,244	$ 2,594	$ 178,244	$ 2,594
Mortgage-backed securities	34,375	159	128,449	2,621	162,824	2,780
	$ 34,375	$ 159	$ 306,693	$ 5,215	$ 341,068	$ 5,374

For those securities with unrealized losses at December 31, 2007 and 2006, the losses are generally due to changes in interest rates and, as such, are considered by management to be temporary.

Securities with estimated fair values of $39,099 and $62,871 at December 31, 2007 and 2006, respectively, were pledged to secure securities sold under agreements to repurchase or lines of credit as permitted by law.

The amortized cost and estimated fair value of securities available for sale at December 31, 2007, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because issuers may have the right to call or repay obligations with or without call or prepayment penalties therefore, a summary of the maturities of these securities is not presented.

	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 40,167	$ 39,975
Due from one year to five years	45,025	45,278
Due in five to fifteen years	600	601
Mortgage-backed securities	142,934	142,387
Equity securities with no contractual maturities	10	20
	$ 228,736	$ 228,261

Sales of securities available for sale were as follows:

	2007	2006
Proceeds from sales	$ 30,059	$ -
Gross realized gains	$ 47	$ -
Gross realized losses	-	-
	$ 47	$ -

Note 3. Loans and Allowance For Loan Losses

Year-end loans consisted of the following:

	2007	2006
Bank stock loans	$ 112,799	$ 81,518
Real estate loans	264,954	286,753
Credit card and personal loans	124,218	97,875
Commercial loans	68,267	75,770
Agricultural loans	3,330	4,384
Leases, net of unearned income	962	2,233
Bank qualified municipal loans	151,527	123,083
Guaranteed student loans	7,698	8,390
	733,755	680,006
Allowance for loan losses	(9,685)	(8,623)
	$ 724,070	$ 671,383

As detailed in the table above, the Corporation has a diversified loan portfolio from customers primarily throughout the states of Texas, New Mexico, Oklahoma, Louisiana, Arizona and California. Accordingly, the ultimate collectibility of a substantial portion of the Corporation's loan portfolio is particularly susceptible to changes in market conditions in these states.

The Corporation's officers, directors and their associates, including companies and firms of which they are officers or in which they and/or their families have an ownership interest, are customers of the Corporation. Loans to officers, directors and their associates totaled $2,364 and $4,732 at December 31, 2007 and 2006, respectively. During 2007, $2,862 of new loans were originated and repayments totaled $2,934. These loans were made on substantially the same terms including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated persons and do not involve more than normal risk of collectibility. In addition, loans to individuals who completed terms as directors in 2007 totaled $2,296.

Activity in allowance for loan losses was as follows:

	2007	2006
Balance at beginning of year	$ 8,623	$ 9,905
Provision for losses charged to operations	2,754	-
Provision from acquired loan portfolios	741	79
Charge-offs	(2,730)	(2,428)
Recoveries	297	1,067
Balance at end of year	$ 9,685	$ 8,623

Impaired loans were as follows:

	2007	2006
Year-end impaired loans with a valuation allowance	$ 551	$ 1,483
Valuation allowance related to impaired loans	$ 60	$ 154
Average investment in impaired loans during the year	$ 1,017	$ 1,112

No interest income was recognized on impaired loans in 2007 and 2006.

Loans on which the accrual of interest has been discontinued totaled $551 and $1,483 at December 31, 2007 and 2006, respectively. Loans, contractually delinquent over ninety days, which continued to accrue interest totaled $557 and $1,916 at December 31, 2007 and 2006, respectively.

Note 4. Premises and Equipment

Year-end premises and equipment was as follows:

	2007	2006
Land	$ 582	$ 582
Building	5,142	5,126
Equipment	9,463	9,299
Leasehold and tenant improvements	166	173
	15,353	15,180
Less accumulated depreciation and amortization	(10,489)	(9,985)
	$ 4,864	$ 5,195

Note 5. Other Real Estate Owned

Year-end other real estate owned was as follows:

	2007	2006
Residential property	$ 96	$ 61
Commercial property	3,364	2,051
	$ 3,460	$ 2,112

Recovery of the carrying amount of other real estate owned is particularly susceptible to changes in market conditions in Texas.

Note 6. Mortgage Servicing Rights

Transactions affecting mortgage servicing rights were as follows:

	2007	2006
Balance at beginning of year	$ 32,109	$ 19,923
Purchased mortgage servicing rights	8,398	13,959
Originated mortgage serving rights	395	326
Increase in valuation allowance	(10,146)	(2,099)
Balance at end of year	$ 30,756	$ 32,109

Loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balances of mortgages serviced for others was $2,455,538 and $2,193,000 at December 31, 2007 and 2006, respectively. At such dates, the Corporation held borrowers' escrow balances related to these loans totaling $13,093 and $8,351, respectively.

The Corporation has purchased various 10-year treasury puts, calls and futures contracts with a fair value of $747 and $(1,272) at December 31, 2007 and 2006, respectively, and are included in other asset and other liabilities, respectively. The contracts hedge against changes in fair value for the Corporation's mortgage servicing rights portfolio.

Note 7. Accumulated Other Comprehensive Income (Loss)

	Change in Fair Value of Fed Funds Swap	Change in Fair Value of Securities Available for Sale	Total Accumulated Other Comprehensive Income (Loss)
Balance at December 31, 2005	$ -	$ (6,039)	$ (6,039)
Change in fair value of securities available for sale	-	2,587	2,587
Change in fair value of Fed Funds Swap	(313)	-	(313)
Balance at December 31, 2006	(313)	(3,452)	(3,765)
Change in fair value of securities available for sale	-	3,138	3,138
Change in fair value of Fed Funds Swap	(2,808)	-	(2,808)
Balance at December 31, 2007	**$ (3,121)**	**$ (314)**	**$ (3,435)**

Note 8. Fed Funds Swap

The Corporation maintains an interest-rate risk-management strategy that uses derivative instruments to minimize significant, unanticipated earnings fluctuations caused by interest rate volatility. The Corporation's specific goal is to lower (where possible) the exposure to the volatility within its variable-rate fed funds.

In 2007, the Corporation exited two interest swap contracts with notional amounts of $50,000 and $25,000 by novation. A gain of $186 and loss of $19 on the transactions are recognized in net income over the remaining contract terms of 20 months and 23 months, respectively. In 2007, the amount of net gain recorded in other income was $51.

In 2007, the Corporation entered into one swap contract related to certain forecasted variable-rate fed funds. The swap contracts at December 31, 2007 are summarized as follows (in thousands):

	Effective Date	Termination Date	Fixed Rate	Variable Rate	Notional Amount	Fair Value
Agreement 1	May 24, 2006	May 24, 2010	5.175 %	Fed Funds Daily Rate	$ 25,000	$ (1,009)
Agreement 2	March 16, 2006	March 16, 2010	4.978 %	Fed Funds Daily Rate	25,000	(842)
Agreement 3	February 16, 2006	February 16, 2010	4.905 %	Fed Funds Daily Rate	25,000	(778)
Agreement 4	February 16, 2007	February 16, 2011	4.940 %	Fed Funds Daily Rate	25,000	(2,100)
						$ (4,729)

Note 9. Deposits

Year-end deposits consisted of the following:

	2007		2006	
	Amount	**Percent**	Amount	Percent
Noninterest-bearing demand	**$ 172,756**	**42.8 %**	$ 152,836	41.8 %
NOW and money market accounts	**25,302**	**6.3 %**	47,996	13.1 %
Certificates of deposit:				
Less than $100,000	**163**	**0.0 %**	163	0.0 %
$100,000 and greater	**205,280**	**50.9 %**	164,981	45.1 %
	$ 403,501	**100.0 %**	$ 365,976	100.0 %

At December 31, 2007, all time deposits have scheduled maturities during the year ending December 31, 2008.

Note 10. Other Borrowings

Year-end other borrowings consisted of the following:

	2007	2006
Federal Home Loan Bank advance originated January 14, 2004 Interest rate: 2.54% Maturity date: January 16, 2007	**$ -**	$ 50,000
Federal Home Loan Bank advance originated January 14, 2004 Interest rate: 3.04% Maturity date: January 14, 2008	**50,000**	50,000
	$ 50,000	$ 100,000

Note 11. Intangible Assets

	2007	2006
Purchased credit card relationships	**$ 6,241**	$ 6,241
Less accumulated amortization	**(2,695)**	(1,446)
	$ 3,546	$ 4,795

Purchased credit card relationships are amortized on a straight-line basis over their estimated lives, which is 5 years. Amortization expense of $1,248 and $898 was recorded in 2007 and 2006. The estimated aggregate future amortization expense for purchased credit card relationships remaining as of December 31, 2007 is as follows:

2008	$ 1,248
2009	1,248
2010	700
2011	350
	$ 3,546

Note 12. Junior Subordinated Debentures

On January 25, 2006, IBFC issued $30,928 of Floating Rate Junior Subordinated Debentures through a newly formed wholly owned subsidiary, IBFC Statutory Trust II (Trust II). Trust II then sold Capital Securities of $30,000. IBFC also made an equity contribution of $928 to form Trust II. Interest on the debentures is payable quarterly at LIBOR plus 1.40% (6.47 % at December 31, 2007) and the debentures mature on March 15, 2036.

IBFC's obligations under the Capital Securities and Junior Subordinated Debentures are unsecured and rank junior in priority to any existing and future indebtedness of IBFC. IBFC may, at any time, dissolve Trust II and distribute the Junior Subordinated Debentures to holders of the Capital Securities in exchange for the Capital Securities.

The Corporation accounts for the Trust in accordance with Financial Accounting Standards Board Interpretation No. 46(R), "Consolidation of Variable Interest Entities, an Interpretation of Accounting Research Bulletin No. 51" ("FIN 46(R)").FIN 46(R) establishes accounting guidance for consolidation of variable interest entities ("VIEs") that function to support the activities of the primary beneficiary. The primary beneficiary of a VIE is the entity that absorbs a majority of the VIE's expected losses, receives a majority of the VIE's expected residual returns, or both, as a result of ownership, controlling interest, contractual relationship, or other business relationship with the VIE. Prior to the implementation of FIN 46(R), VIEs were generally consolidated by an enterprise when the enterprise had a controlling financial interest through ownership of a majority of voting interest in the entity. FIN 46(R) requires the Corporation to deconsolidate its investment in trust subsidiaries because the Corporation is not the primary beneficiary.

Note 13. Federal Income Taxes

Actual income tax expense differed from the amounts computed by applying the U.S. federal income tax rate of 34% to pretax accounting income as follows:

	2007	2006
Income tax expense computed at statutory rate	**$ 4,534**	$ 4,495
Increase in cash value of life insurance	**(285)**	(268)
Tax-exempt interest	**(2,124)**	(1,559)
Other	**701**	548
Actual income tax expense	**$ 2,826**	$ 3,216

Year-end deferred taxes were as follows:

	2007	2006
Deferred tax assets:		
Loans	**$ 3,039**	$ 2,427
Accrued expense and other liabilities	**2,546**	2,409
Securities available for sale	**162**	1,778
Other real estate owned	**108**	130
Federal fund swap	**1,608**	162
Other	**114**	514
Total deferred tax assets	**7,577**	7,420
Deferred tax liabilities:		
Premises and equipment	**127**	208
Mortgage servicing rights	**7,560**	6,539
FHLB stock	**177**	210
Total deferred tax liabilities	**7,864**	6,957
Net deferred tax (liability) asset	**$ (287)**	$ 463

Note 14. Employee Benefits

The Corporation maintains a savings plan for its employees. Employees are eligible to participate immediately upon hire subject to next enrollment date. Maximum employer and employee contributions to the plan are limited to $45 or 100% of an employee's gross earnings, whichever is less. The savings plan vests equally over five years. The Corporation may make contributions in an amount necessary to match up to a maximum of 5% of the employee's annual compensation. The Corporation's contributions were $879 and $789 in 2007 and 2006, respectively.

The Corporation has nonqualified deferred compensation plans which provide death and retirement benefits to certain officers. Benefits under the plans are payable over a 15 year period following death or retirement. Deferred compensation expense of $672 and $690 was recorded in 2007 and 2006, respectively. Deferred compensation payable totaled $4,952 and $4,649 at December 31, 2007 and 2006, respectively. The Corporation has purchased life insurance policies to fund future plan obligations. These policies had an aggregate cash surrender value of $22,462 and $21,625 at December 31, 2007 and 2006, respectively.

During 2002, the Corporation adopted a Phantom Stock Ownership and Long-Term Incentive Plan under which eligible employees may be granted phantom shares from an initial pool of 108,000 shares and such shares generally vest over five years. Holders of the phantom shares have no rights as a shareholder of the Corporation, but may redeem vested phantom shares held for cash in an amount equal to the increase in the book value of the Corporation's common stock subsequent to their grant date.

Information regarding phantom shares is as follows:

	2007	2006
Phantom shares outstanding at beginning of year	**68,015**	75,067
Redeemed	**(24,530)**	(7,052)
Phantom shares outstanding at end of year	**43,485**	68,015
Available for grant at end of year	**27,039**	27,039
Exercisable at end of year	**37,587**	56,630

In 2006, the Corporation adopted a Stock Appreciation Right Plan (SAR) under which eligible employees are awarded the right to receive a lump sum cash payment in an amount equal to the increase in the fair market value of the Corporation's stock on an established date, after the vesting period of generally five years, over the grant date price of the SAR.

In 2007 and 2006, respectively, 10,150 and 6,000 awards were granted.

Compensation expense related to phantom shares and stock appreciation rights is accrued over the vesting period of the award; however, the ultimate measurement of the aggregate compensation is based on the value of the award on the date of exercise. Accrued compensation payable under the Plans totaled $1,848 and $2,414 at December 31, 2007 and 2006, respectively. Compensation expense recognized under the Plans totaled $789 in 2007 and $825 in 2006. At December 31, 2007, the aggregate value of unvested shares was approximately $180 and will be recognized as the shares vest over the next three years.

Note 15. Noninterest Income

Noninterest income consisted of the following for the years ended December 31, 2007 and 2006:

	2007	2006
Credit card fees	**$ 60,236**	$ 46,163
Item processing fees	**2,391**	2,300
Mortgage loan servicing fees	**4,846**	4,296
Customer security transaction fees	**2,591**	2,341
Audit and loan review fees	**1,396**	2,368
Gain on sales of loans	**2,936**	2,133
Gain on sale of securities, net	**47**	-
Federal fund agency fees	**1,536**	1,290
Gain on sale of other investment	**2,061**	-
Net gain on derivative transactions	**6,668**	-
Other	**8,757**	9,506
	$ 93,465	$ 70,397

Note 16. Acquisitions

Effective June 30, 2006, the Bank purchased 100% of the assets of Western States BankCard Association, a mutual benefit corporation under California law, for a total cash purchase price of approximately $3,500. The acquisition of Western States BankCard Association will significantly increase the Bank's card processing volumes, in turn creating economies that will allow the Bank to provide improved efficiencies, service levels and product offerings for customer banks across the country. The acquired entity will be a division of BBCS and will be known as Western States Card Services (WSCS).

The entire purchase price of Western States BankCard Association was allocated to customer contracts with terms of three to five years and will be amortized over five years.

In June 2007, the Bank purchased an existing California bank national charter for a total cash purchase price of $1,000. The newly purchased charter was merged into the Bank's Texas state bank charter. The purchase changed the loan production office in California to a full branch of the Bank, provided the Bank with lending authority in the state of California and enabled the Bank to provide a wider range of services to banks in California. The entire purchase price of the charter was allocated to goodwill.

Note 17. Commitments and Contingencies

Financial Instruments With Off-Balance Sheet Risk

The Corporation is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, credit card line commitments and standby letters of credit and involve, to varying degrees, elements of credit risk and interest rate risk in excess of the amount recognized in the consolidated balance sheet. The contract or notional amounts of those instruments reflect the extent of involvement the Corporation has in particular classes of financial instruments.

The Corporation's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit, credit card line commitments and standby letters of credit is represented by the contractual amount of those instruments. The Corporation uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. At December 31, 2007 and 2006, the amounts of these financial instruments were as follows:

	2007	2006
Commitments to extend credit	**$ 219,058**	$ 201,031
Standby letters of credit	**5,345**	6,483
Credit card lines	**693,995**	464,887
	$ 918,398	$ 672,401

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. Such commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Corporation evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Corporation upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, single and multi-family residences, property and equipment and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the Corporation to guarantee the performance of a customer to a third party. The Corporation's policies generally require that letter of credit arrangements contain security and debt covenants similar to those contained in loan arrangements. The amount of collateral obtained, if deemed necessary by the Corporation upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, single and multi-family residences, property and equipment and income-producing commercial properties. In the event the customer does not perform in accordance with the terms of the agreement with the third party, the Corporation would be required to fund the commitment. The maximum potential amount of future payments the Corporation could be required to make is represented by the contractual amount shown in the table above. If the commitment is funded, the Corporation would be entitled to seek recovery from the customer. As of December 31, 2007 and 2006, no amounts have been recorded as liabilities for the Corporation's potential obligations under these guarantees.

Credit card commitments are unsecured.

The Corporation has a revolving line of credit payable with a third party. During 2007 and 2006, the note had a maximum advanceable amount of $15,000. The line of credit accrues interest at the Wall Street Journal prime interest rate, contains certain financial covenants and is secured by the stock of the Bank. There was no balance outstanding at any time during 2007 or 2006.

Lease Commitments

The Corporation leases certain office facilities and office equipment under operating leases that expire at various dates through 2013. The Corporation has renewal options for most of its operating leases. Rent expense for all operating leases totaled $953 in 2007 and $876 in 2006. Total rents paid under escalating lease agreements are expensed over the life of the lease on a straight-line basis. The rental payments on operating leases are based on a minimum rental plus a percentage of operating costs, some of which are restricted as to the maximum annual increase.

Future minimum lease payments under all noncancelable operating leases as of December 31, 2007 are as follows:

2008	$	808
2009		657
2010		162
2011		77
2012		55
2013		19
	$	1,778

Contingencies

Various other contingent liabilities are not reflected in the financial statements, including claims and legal actions arising in the ordinary course of business. In the opinion of management, after consultation with legal counsel, the ultimate disposition of these matters is not expected to have a material effect on the Corporation's financial condition, results of operations or cash flows.

Note 18. Fair Value of Financial Instruments

The estimated fair value approximates carrying value for financial instruments except those described below:

Securities and Derivatives

Fair values for securities and derivatives are based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar instruments.

Loans Held for Sale

Fair values are based on quoted market prices of similar loans sold on the secondary market.

Loans

The fair value of fixed-rate loans and variable-rate loans which reprice on an infrequent basis is estimated by discounting future cash flows using the current interest rates at which similar loans with similar terms would be made to borrowers of similar credit quality. Credit card receivables were valued based on the estimated premium to book value the Corporation would expect to obtain for a sale of the entire portfolio given its size, terms and other characteristics.

Deposits

The fair value of fixed-rate deposit liabilities with defined maturities is estimated by discounting future cash flows using the interest rates currently offered for deposits of similar remaining maturities.

Other Borrowings

The fair value of fixed rate borrowings is estimated based on the present value of expected cash flows using current interest rates for similar financial instruments.

Off-Balance Sheet Instruments

The fair values of these items are not material and are therefore not included on the following schedule.

The estimated fair values of the Corporation's financial instruments as of December 31, 2007 and 2006 were as follows:

	2007		2006	
	Carrying Amount	**Estimated Fair Value**	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash equivalents	**$ 744,428**	**$ 744,428**	$ 433,116	$ 433,116
Interest-bearing time deposits	**100**	**98**	300	300
Securities	**228,261**	**228,261**	373,951	373,951
Loans held for sale	**54,042**	**54,042**	23,804	23,804
Loans, net	**724,070**	**741,582**	671,383	686,672
Mortgage servicing rights	**30,756**	**30,756**	32,109	32,109
Accrued interest receivable	**7,680**	**7,680**	8,464	8,464
Due from broker	**9,789**	**9,789**	2,847	2,847
Financial liabilities:				
Deposits	**403,501**	**403,675**	365,976	366,161
Federal funds purchased and securities sold under agreements to repurchase	**$ 1,224,708**	**1,244,656**	997,770	997,770
Other borrowings	**50,000**	**50,000**	100,000	97,166
Junior subordinated debentures	**30,928**	**30,928**	30,928	30,928
Derivatives	**4,729**	**4,729**	1,747	1,747
Accrued interest payable	**968**	**968**	1,325	1,325

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Corporation's entire holdings of a particular financial instrument. These estimates are subjective in nature and require considerable judgment to interpret market data. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Corporation could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts. The fair value estimates presented herein are based on pertinent information available to management as of the respective balance sheet date. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued since the presentation dates, and therefore, estimates of fair value after the balance sheet date may differ significantly from the amounts presented herein.

Note 19. Shareholders' Equity

The Corporation has 1,000,000 authorized shares of $1 par value convertible preferred stock (Series B, C and D) with a liquidation value of $20 per share. No shares were outstanding at December 31, 2007 or 2006.

The Corporation maintains a Dividend Reinvestment and Share Purchase Plan whereby shareholders may elect to:(1) reinvest common stock dividends in the common stock of the Corporation, and (2) make optional cash payments to purchase additional common stock of the Corporation. The purchase price of common shares issued under the Plan is the book value of the stock (excluding other comprehensive income) as of the month ended immediately preceding the reinvestment date. During 2007 and 2006, 5,261 and 4,971 shares of common stock were issued under the Plan with an average issue price of $83.76 and $75.81 per share, respectively.

Note 20. Regulatory Matters

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

Quantitative measures established by regulations to ensure capital adequacy require the maintaining of minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined).

As of December 31, 2007 and 2006, the Bank met the level of capital necessary to be categorized as "well capitalized" under prompt corrective action regulations. To be categorized as "well capitalized," the Bank must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the table.

As of December 31, 2007 and 2006, the Corporation met all capital requirements under the regulatory framework specified by the Federal Reserve Board. Management is not aware of any conditions subsequent to December 31, 2007 that would change the Corporation's or the Bank's capital category.

The Corporation's and the Bank's actual capital amounts and ratios are presented in the following table.

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2007:						
Total capital to risk weighted assets:						
Consolidated	**$ 133,696**	**12.0 %**	**$ 89,047**	**8.0 %**	**N/A**	**N/A**
Bank only	**130,147**	**11.7 %**	**88,808**	**8.0 %**	**$ 111,009**	**10.0 %**
Tier I capital to risk weighted assets:						
Consolidated	**124,006**	**11.1 %**	**44,523**	**4.0 %**	**N/A**	**N/A**
Bank only	**120,457**	**10.9 %**	**44,404**	**4.0 %**	**66,606**	**6.0 %**
Tier I capital to average assets:						
Consolidated	**126,006**	**6.8 %**	**73,281**	**4.0 %**	**N/A**	**N/A**
Bank only	**120,457**	**6.6 %**	**73,242**	**4.0 %**	**91,553**	**5.0 %**
December 31, 2006:						
Total capital to risk weighted assets:						
Consolidated	$ 121,378	12.7 %	$ 76,558	8.0 %	N/A	N/A
Bank only	119,187	12.5 %	76,306	8.0 %	$ 95,382	10.0 %
Tier I capital to risk weighted assets:						
Consolidated	110,328	11.5 %	38,279	4.0 %	N/A	N/A
Bank only	110,555	11.6 %	38,153	4.0 %	57,229	6.0 %
Tier I capital to average assets:						
Consolidated	110,328	6.2 %	71,463	4.0 %	N/A	N/A
Bank only	110,555	6.2 %	71,336	4.0 %	89,169	5.0 %

Note 21. Parent Company Only Financial Statements

Balance Sheets

	December 31,	
ASSETS	**2007**	2006
Cash due from subsidiary bank	**$ 4,433**	$ 4,003
Investment in subsidiaries	**126,206**	115,918
Other assets	**2,694**	2,231
Total assets	**$ 133,333**	$ 122,152
LIABILITIES AND SHAREHOLDERS' EQUITY		
Dividends payable	**$ 1,637**	$ 1,521
Junior subordinated debentures	**30,928**	30,928
Other liabilities	**1,941**	2,523
Total liabilities	**34,506**	34,972
Commitments and contingencies	**-**	-
Shareholders' equity:		
Common stock, par value $10 per share, 5,000,000 shares authorized; 1,091,796 and 1,085,825 shares issued and outstanding in 2007 and 2006	**10,918**	10,858
Capital surplus	**23,391**	21,005
Retained earnings	**67,953**	59,082
Accumulated other comprehensive loss	**(3,435)**	(3,765)
Total shareholders' equity	**98,827**	87,180
Total liabilities and shareholders' equity	**$ 133,333**	$ 122,152

Statements of Income

	Year Ended December 31, 2007	Year Ended December 31, 2006
Dividend income	$ 2,500	$ -
Interest income	65	59
Interest expense	(2,166)	(2,066)
	399	(2,007)
Other Income	-	218
Other expenses	(854)	(1,014)
Loss before income taxes and equity in undistributed income of subsidiaries	(455)	(2,803)
Federal:		
Federal income taxes - current benefit	1,005	947
Income (loss) before equity in undistributed income of subsidiaries	550	(1,856)
Equity in undistributed income of subsidiaries	9,958	11,861
Net income	$ 10,508	$ 10,005

Statements of Cash Flows

	Year Ended December 31, 2007	Year Ended December 31, 2006
Cash flows from operating activities:		
Net income	$ 10,508	$ 10,005
Adjustments to reconcile net income to net cash used in operating activities:		
Equity in undistributed income of subsidiaries	(9,958)	(11,861)
Deferred compensation expense	789	825
Changes in operating assets and liabilities:		
Other assets	(463)	542
Other liabilities	(1,371)	(156)
Net cash used in operating activities	(495)	(645)
Cash flows from investing:		
Payments to and investments in subsidiaries	-	(8,928)
Sales of investments in subsidiaries	-	644
Net cash used in financing activities	-	(8,284)
Cash flows from financing activities:		
Change in junior subordinated debentures	-	10,308
Purchase and retirement of common stock	(1,092)	(256)
Net proceeds from issuance of common stock	3,538	2,352
Cash dividends paid on common stock	(1,521)	(1,378)
Net cash provided by financing activities	925	11,026
Net increase in cash equivalents	430	2,097
Cash equivalents at beginning of year	4,003	1,906
Cash equivalents at end of year	$ 4,433	$ 4,003
Supplemental cash flow information:		
Cash paid during the year for interest	$ 2,182	$ 1,966
Cash paid during the year for taxes	2,207	3,093