

City National Bank of Florida

*Financial Statements as of and for the Years
Ended December 31, 2006 and 2005, and
Independent Auditors' Report*



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INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholder of
City National Bank of Florida:

We have audited the accompanying balance sheets of City National Bank of Florida (the "Bank") as of December 31, 2006 and 2005, and the related statements of earnings and comprehensive earnings, stockholder's equity, and cash flows for the years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit also 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, such financial statements present fairly, in all material respects, the financial position of the Bank as of December 31, 2006 and 2005, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

A handwritten signature in cursive script that reads "Deloitte & Touche LLP".

March 2, 2007

CITY NATIONAL BANK OF FLORIDA

BALANCE SHEETS

AS OF DECEMBER 31, 2006 AND 2005

(In thousands)

	2006	2005
ASSETS		
INTEREST-EARNING ASSETS:		
Loans	\$ 1,712,427	\$ 1,706,206
Less:		
Deferred loan fees	(4,893)	(5,787)
Allowance for loan losses	<u>(23,798)</u>	<u>(22,586)</u>
Loans—net	1,683,736	1,677,833
Securities available for sale	647,482	557,325
Securities held to maturity (approximate fair values: \$32,853 in 2006 and \$32,294 in 2005)	32,604	32,353
Federal funds sold and securities purchased under agreements to resell	200,000	460,000
Interest-bearing balances with financial institutions	<u>5,693</u>	<u>306</u>
Total interest-earning assets	2,569,515	2,727,817
CASH AND DUE FROM BANKS	110,128	111,386
ACCRUED INTEREST RECEIVABLE	16,144	14,145
BANK PREMISES AND EQUIPMENT—Net	39,980	38,751
OTHER ASSETS	<u>17,705</u>	<u>4,054</u>
TOTAL	<u>\$ 2,753,472</u>	<u>\$ 2,896,153</u>
LIABILITIES AND STOCKHOLDER'S EQUITY		
DEPOSITS AND BORROWINGS:		
Deposits	\$ 2,002,200	\$ 2,351,290
Other borrowings	25,585	35,585
Federal funds purchased and securities sold under agreements to repurchase	<u>438,461</u>	<u>258,257</u>
Total deposits and borrowings	2,466,246	2,645,132
OTHER LIABILITIES	<u>10,544</u>	<u>8,256</u>
Total liabilities	<u>2,476,790</u>	<u>2,653,388</u>
COMMITMENTS AND CONTINGENCIES (Note 9)		
STOCKHOLDER'S EQUITY:		
Common stock, \$10 par value; authorized, issued, and outstanding 1,420,000 shares	14,200	14,200
Capital surplus	14,200	14,200
Retained earnings	250,788	220,357
Accumulated other comprehensive loss	<u>(2,506)</u>	<u>(5,992)</u>
Total stockholder's equity	<u>276,682</u>	<u>242,765</u>
TOTAL	<u>\$ 2,753,472</u>	<u>\$ 2,896,153</u>

See notes to financial statements.

CITY NATIONAL BANK OF FLORIDA

STATEMENTS OF EARNINGS AND COMPREHENSIVE EARNINGS FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005 (In thousands)

	2006	2005
INTEREST INCOME:		
Interest and fees on loans	\$ 135,845	\$ 109,667
Interest and dividends on securities	25,560	20,880
Interest on federal funds sold and securities purchased under agreements to resell	19,074	15,119
Interest on interest-bearing balances with financial institutions	<u>73</u>	<u>51</u>
	<u>180,552</u>	<u>145,717</u>
INTEREST EXPENSE:		
Interest on deposits	45,172	28,289
Interest on borrowings	<u>20,281</u>	<u>12,068</u>
	<u>65,453</u>	<u>40,357</u>
NET INTEREST INCOME	115,099	105,360
PROVISION FOR LOAN LOSSES	<u>1,178</u>	<u>1,500</u>
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	<u>113,921</u>	<u>103,860</u>
OTHER OPERATING INCOME:		
Service charges, commissions, and fees	7,887	8,305
Loss on sales of investment securities—net		(156)
Other	<u>2,847</u>	<u>2,794</u>
	<u>10,734</u>	<u>10,943</u>
OTHER OPERATING EXPENSES:		
Salaries and employee benefits	37,047	33,251
Occupancy expense	8,010	7,429
Equipment expense	1,862	1,765
Other	<u>10,630</u>	<u>10,505</u>
	<u>57,549</u>	<u>52,950</u>
NET EARNINGS	<u>67,106</u>	<u>61,853</u>
OTHER COMPREHENSIVE EARNINGS:		
Unrealized gains/losses on securities available for sale	3,486	(4,992)
Less—reclassification adjustment for gains included in net earnings		<u>156</u>
Total	<u>3,486</u>	<u>(4,836)</u>
COMPREHENSIVE EARNINGS	<u>\$ 70,592</u>	<u>\$ 57,017</u>

See notes to financial statements.

CITY NATIONAL BANK OF FLORIDA

STATEMENTS OF STOCKHOLDER'S EQUITY FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005 (In thousands)

	Common Stock	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive (Loss) Earnings	Total
BALANCE—December 31, 2004	\$ 14,200	\$ 14,200	\$ 189,904	\$ (1,156)	\$ 217,148
Net earnings			61,853		61,853
Dividends			(31,400)		(31,400)
Change in valuation—securities available for sale				(4,836)	(4,836)
BALANCE—December 31, 2005	14,200	14,200	220,357	(5,992)	242,765
Net earnings			67,106		67,106
Dividends			(36,675)		(36,675)
Change in valuation—securities available for sale				3,486	3,486
BALANCE—December 31, 2006	<u>\$ 14,200</u>	<u>\$ 14,200</u>	<u>\$ 250,788</u>	<u>\$ (2,506)</u>	<u>\$ 276,682</u>

See notes to financial statements.

CITY NATIONAL BANK OF FLORIDA

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005 (In thousands)

	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net earnings	\$ 67,106	\$ 61,853
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	3,040	2,902
Stock appreciation right compensation expense	1,374	978
Provision for loan losses	1,178	1,500
Decrease in provision for off-balance sheet credit losses	(59)	(750)
Gain on sales of equipment—net	(51)	(3)
Loss on sales of securities available for sale—net		156
Origination of loans held for sale	(730)	(7,974)
Proceeds from sales of loans held for sale	746	8,086
Gain on sales of loans held for sale	(16)	(112)
Net accretion on securities held to maturity	(365)	(256)
Net premium amortization on securities available for sale	247	1,785
Accretion of unearned discount on loans	(6,277)	(6,328)
Changes in other assets and liabilities:		
(Increase) decrease in accrued interest receivable	(1,999)	2,131
Decrease in other assets	1,522	2,126
Increase (decrease) in other liabilities	800	(3,622)
Net cash provided by operating activities	<u>66,516</u>	<u>62,472</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Principal repayments and maturities of securities held to maturity	739	3,742
Proceeds from sales of securities available for sale		90,176
Proceeds from calls and maturities of securities available for sale	164,490	40,590
Purchase of securities available for sale	(379,610)	(217,450)
Principal repayment of securities available for sale	112,577	117,134
Net increase in loans	(804)	(140,019)
Increase in interest-bearing balances with financial institutions	(5,387)	(123)
Net increase in customers' acceptance liability	(173)	
Purchases of bank premises and equipment	(4,218)	(1,528)
Proceeds from sales of equipment		3
Net cash used in investing activities	<u>(112,386)</u>	<u>(107,475)</u>

(Continued)

CITY NATIONAL BANK OF FLORIDA

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005 (In thousands)

	2006	2005
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net (decrease) increase in deposits	\$ (349,090)	\$ 175,446
Net increase in federal funds purchased and securities sold under agreements to repurchase	180,204	56,346
Decrease in other borrowings	(10,000)	
Net increase in acceptances outstanding	173	
Dividends paid	<u>(36,675)</u>	<u>(31,400)</u>
Net cash (used in) provided by financing activities	<u>(215,388)</u>	<u>200,392</u>
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(261,258)	155,389
CASH AND CASH EQUIVALENTS—Beginning of year	<u>571,386</u>	<u>415,997</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 310,128</u>	<u>\$ 571,386</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION—Cash paid during the year for interest	<u>\$ 65,375</u>	<u>\$ 39,745</u>
SUPPLEMENTAL DISCLOSURES OF NONCASH ACTIVITIES—There were no foreclosures during 2006 and 2005.		

See notes to financial statements.

(Concluded)

CITY NATIONAL BANK OF FLORIDA

NOTES TO FINANCIAL STATEMENTS

AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

City National Bank of Florida (the “Bank”), a wholly owned subsidiary of City National Bancshares, Inc. (the “Parent”), is engaged in the general commercial banking business and provides a variety of related financial products and services through its branches in Miami-Dade, Broward, and Palm Beach Counties, Florida. The Bank is subject to the regulations of certain federal agencies and undergoes periodic examinations by those regulatory authorities.

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

Cash and Cash Equivalents—Cash and cash equivalents include cash and due from banks with original maturities of 90 days or less and federal funds sold.

Trading Account—Trading account assets are stated at market value. Trading account assets are held in anticipation of short-term market movements. Gains or losses on the sale of trading account assets as well as unrealized market value adjustments are included in other operating income. The Bank did not hold any trading account securities as of December 31, 2006 and 2005.

Securities Available for Sale—Securities to be held for unspecified periods of time, including securities that management intends to use as part of its asset/liabilities strategy, or that may be sold in response to changes in interest rates, changes in prepayment risk, or other similar factors, are classified as available for sale and are carried at fair value. The appreciation or decline in value of these securities is reflected as a separate component of stockholder’s equity and comprises the difference between net earnings and comprehensive earnings.

Commissions and Fees—Commissions and fees on loans are deferred and recognized into income using the straight-line basis, which approximates the level-yield method, over the term of the corresponding loan. Commissions and fees on loans are recorded in other operating income in the accompanying statements of earnings and comprehensive earnings.

Securities Held to Maturity—Investments in debt securities to be held to maturity are carried at amortized cost as the Bank has both the intent and ability to hold these securities to maturity. Premiums and discounts on investment securities are amortized to expense and accreted to income over the life of the securities using a method which approximates the level-yield method.

Bank Premises and Equipment—Bank premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation is computed using the straight-line and accelerated methods over a 5- to 39-year period.

Trust Department Assets—Securities and other property held by the trust department, in agency or other fiduciary capacities for customers, are not included in the accompanying financial statements.

Other Real Estate Owned—Foreclosed assets are carried at the lower of fair value, less estimated costs to sell, or cost. If the fair value of the asset, less the estimated costs to sell, is less than the cost of the asset, the deficiency is charged to income. The Bank did not have any other real estate owned as of December 31, 2006 and 2005.

Income Taxes—The Bank is a “Qualified” Subchapter S subsidiary of City National Bancshares, Inc., an “S Corporation” for income tax reporting purposes. As an S subsidiary, all taxable income and expenses flow directly to the stockholders of City National Bancshares, Inc. and are not taxed at the corporate level. Accordingly, no income tax provision is included in the financial statements.

Provision for Loan Losses—Provisions for loan losses, which increase the allowance for loan losses, are established by charges to income. Such allowances represent the amounts which, in management’s judgment, are adequate to absorb losses on loans which may become uncollectible. The adequacy of the allowance is determined by management’s continuing evaluation of the loan portfolio in light of past loss experience, present economic conditions, and other factors considered relevant by management at the financial statement date. Anticipated changes in economic factors which may influence the level of the allowance are considered in the evaluation by management when the likelihood of the changes can be reasonably determined. In estimating the allowance for loan losses, consideration is given to asset performance, the financial condition of borrowers or guarantors, additional collateral provided, current and anticipated economic conditions, appraisals of collateral, cost of disposal, and holding costs. While management uses the best information available to make such evaluations, future adjustments to the allowance may be necessary, which may be material, if economic conditions differ substantially from the assumptions used in the evaluation. If additions to the original estimate of the allowance for loan losses are deemed necessary, they will be reported in earnings in the period in which they become reasonably estimable.

Pooled loan loss factors are derived from a model that tracks historical loss experience. Pooled loans are loans that are homogeneous in nature, such as consumer installment and residential mortgage loans.

Management believes that the allowance for loan losses is adequate; however, regulatory agencies, as an integral part of their examination process, periodically review the Bank’s allowance for loan losses. Such agencies may require the Bank to recognize additions to the allowance based on their judgment and their evaluation of information available to them at the time of their examination.

Management’s continuing evaluation of its loan portfolio includes the identification of commercial, business, and commercial real estate loans which are considered impaired because it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Individually, identified impaired loans are measured based on the present value of payments expected to be received, using the historical effective loan rate as the discount rate. Alternatively, measurement may also be based on observable market prices or, for loans that are solely dependent on the collateral for repayment, measurement may be based on the fair value of the collateral. Loans that are to be foreclosed are measured based on the fair value of the collateral. If the recorded investment in the impaired loan exceeds the measure of fair value, a valuation is required as a component of the allowance for loan losses. Changes to the valuation allowance are recorded as a component of the provision for loan losses.

Income Recognition—Interest income is recognized over the term of the related loans and investment securities. Accrual of interest is discontinued on nonperforming and impaired loans, and previously accrued interest is reversed, when a loan becomes 90 days past due, or in the opinion of management, such revenue will not be collected. Generally, interest payments received on loans for which the accrual of interest has been discontinued are recorded as a reduction of the respective loan’s principal balance. Premiums and discounts on loans and investment securities are amortized using a method which approximates the level-yield method. Incremental direct loan origination and acquisition fees are deferred and amortized as an adjustment to the yield of the related loan.

New Accounting Pronouncements Affecting the Bank—In July 2006, the Financial Accounting Standards Board (“FASB”) issued Interpretation (“FIN”) No. 48, *Accounting for Uncertainty in Income Taxes—an interpretation of FASB No. 109*. This interpretation establishes guidelines and thresholds that must be met for the recognition and measurement of a tax position taken or expected to be taken in a tax return. The provisions of FIN No. 48 are effective for fiscal years beginning after December 31, 2006. The Bank does not expect the adoption of FIN No. 48 to have a material effect on its results of operations or financial position.

In September 2006, the FASB issued Statement of Financial Accounting Standards (“SFAS”) No. 157, *Fair Value Measurements*. SFAS No. 157 prescribes a single definition of fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The accounting provisions of SFAS No. 157 will be effective for fiscal years beginning after November 15, 2007. The Bank does not believe the adoption of SFAS No. 157 will have a material impact on its financial condition or results of operations.

In September 2006, the FASB issued SFAS No. 158, *Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans*. This statement requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. The accounting provisions of SFAS No. 158 will be effective for fiscal years beginning after June 15, 2007. The Bank is still evaluating the impact of this statement on its financial statements.

In January 2003, the FASB issued FIN No. 46, *Consolidation of Variable Interest Entities*. The FASB revised FIN No. 46 in December 2003 (“FIN 46R”). FIN 46R clarifies the application of Accounting Research Bulletin No. 51, *Consolidated Financial Statements*, to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. The implementation of FIN 46R is required for nonpublic entities at various dates during 2005 and 2006. The adoption of this rule did not have a material impact on the Bank’s results of operations or financial conditions.

In December 2004, the FASB issued SFAS No. 123 (revised 2004) (“SFAS No. 123R”), *Share-Based Payment*, which amends SFAS No. 123. SFAS No. 123R requires all companies to measure compensation cost for all share-based payments (including employee stock options) at fair value and will be effective for nonpublic companies as of the beginning of the first annual reporting period that begins after December 15, 2005. This new standard may be adopted in one of two ways—the modified prospective method or the modified retrospective method. The adoption of SFAS No. 123R did not have a material impact on the Bank’s results of operations or financial condition.

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections*, a replacement of Accounting Principles Board (“APB”) Opinion No. 20 and FASB Statement No. 3. SFAS No. 154 changes the requirements for the accounting and reporting of a change in accounting principle. The statement eliminates the requirement in APB Opinion No. 20 to include the cumulative effect of changes in accounting principle in the income statement in the period of change, and instead requires that changes in accounting principle be retrospectively applied unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. The statement applies to all voluntary changes in accounting principle. SFAS No. 154 is effective for changes made in fiscal years beginning after December 15, 2005. The adoption of SFAS No. 154 did not have a material impact on the Bank’s results of operations or financial condition.

In September 2005, the Emerging Issues Task Force (“EITF”) reached a consensus on EITF 05-06, *Determining the Amortization Period for Leasehold Improvements Purchased after Lease Inception or Acquired in a Business Combination*. EITF Issue No. 05-06 resolves that leasehold improvements that are placed in service significantly after and not contemplated at or near the beginning of the lease term or that are acquired in a business combination should be amortized over the shorter of the useful life of the assets or a term that includes the required lease periods and renewals that are deemed to be reasonably assured as of the date the leasehold improvements are purchased or the date of acquisition, as applicable. EITF Issue No. 05-06 is effective the first reporting period beginning after June 29, 2005. The adoption of EITF 05-06 did not have a material impact on the Bank’s results of operations or financial condition.

In November 2005, the FASB issued FASB Staff Position (“FSP”) FAS 115-1 and FAS 124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* (“FSP 115-1 and 124-1”), which clarifies when an investment is considered impaired, whether the impairment is other-than-temporary, and the measurement of an impairment loss. It also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. FSP 115-1 and 124-1 are effective for all reporting periods beginning after December 15, 2005. The Bank’s management has evaluated the impact of this FSP and has concluded that their disclosures are consistent with the objective of the FSP.

In December 2005, the FASB issued FSP SOP 94-6-1, *Terms of Loan Products That May Give Rise to a Concentration of Credit Risk*. The guidance requires the disclosure of concentrations of loans with certain features that may increase the creditor’s exposure to risk of nonpayment or realization. These loans are often referred to as “non-traditional” loans and include features such as high loan-to-value ratios, terms that permit payments smaller than the interest accruals and loans where the borrower is subject to significant payment increases over the life of the loan. The Bank’s management has evaluated the impact of this FSP and has concluded that their disclosures are consistent with the objectives of the FSP.

Reclassifications—Certain reclassifications have been made to the December 31, 2005, financial statements to conform with the current presentation.

2. SECURITIES AVAILABLE FOR SALE AND SECURITIES HELD TO MATURITY

Debt and equity securities have been classified in the balance sheets according to management's intent. The carrying amount of securities and their approximate fair values at December 31, 2006 and 2005, were as follows:

Securities available for sale at December 31, 2006 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Values
U.S. Treasury	\$ 54,604	\$ 71	\$ (124)	\$ 54,551
U.S. government agencies	190,991	180	(868)	190,303
Collateralized mortgage obligations	290,061	441	(2,123)	288,379
Adjustable rate mortgage securities	56,544	104	(238)	56,410
Obligations of state and political subdivisions	31,003	513	(195)	31,321
Other securities	<u>26,785</u>	<u>29</u>	<u>(296)</u>	<u>26,518</u>
Total	<u>\$ 649,988</u>	<u>\$ 1,338</u>	<u>\$ (3,844)</u>	<u>\$ 647,482</u>

Securities held to maturity at December 31, 2006 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Values
Collateralized mortgage obligations	\$ 29,192	\$ 367	\$ (90)	\$ 29,469
Obligations of state and political subdivisions	1,887			1,887
Other securities	<u>1,525</u>		<u>(28)</u>	<u>1,497</u>
Total	<u>\$ 32,604</u>	<u>\$ 367</u>	<u>\$ (118)</u>	<u>\$ 32,853</u>

Securities available for sale at December 31, 2005 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Values
U.S. Treasury	\$ 129,819	\$ -	\$ (1,165)	\$ 128,654
U.S. government agencies	85,494	79	(1,302)	84,271
Collateralized mortgage obligations	243,396	8	(3,209)	240,195
Adjustable rate mortgage securities	42,219	75	(557)	41,737
Obligations of state and political subdivisions	31,087	631	(171)	31,547
Other securities	<u>31,302</u>		<u>(381)</u>	<u>30,921</u>
Total	<u>\$ 563,317</u>	<u>\$ 793</u>	<u>\$ (6,785)</u>	<u>\$ 557,325</u>

Securities held to maturity at December 31, 2005 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Values
Collateralized mortgage obligations	\$ 29,177	\$ 183	\$ (242)	\$ 29,118
Obligations of state and political subdivisions	2,176			2,176
Other securities	<u>1,000</u>	<u> </u>	<u> </u>	<u>1,000</u>
Total	<u>\$ 32,353</u>	<u>\$ 183</u>	<u>\$ (242)</u>	<u>\$ 32,294</u>

Securities available for sale and held to maturity with unrealized losses at December 31, 2006, were as follows (in thousands):

	<u>Less than 12 months</u>		<u>12 months or Longer</u>		<u>Total</u>	
	Market Value	Unrealized Losses	Market Value	Unrealized Losses	Market Value	Unrealized Losses
Available for Sale						
U.S. treasury	\$ -	\$ -	\$ 19,842	\$ (124)	\$ 19,842	\$ (124)
U.S. government agencies	45,734	(63)	51,008	(805)	96,742	(868)
Collateralized mortgage obligations	90,715	(148)	140,443	(1,975)	231,158	(2,123)
Adjustable rate mortgage securities	4,151	(13)	18,019	(225)	22,170	(238)
Obligation of state and political subdivisions	6,727	(33)	10,295	(162)	17,022	(195)
Other securities	<u> </u>	<u> </u>	<u>15,736</u>	<u>(296)</u>	<u>15,736</u>	<u>(296)</u>
	<u>\$ 147,327</u>	<u>\$ (257)</u>	<u>\$ 255,343</u>	<u>\$ (3,587)</u>	<u>\$ 402,670</u>	<u>\$ (3,844)</u>
Held for Maturity						
Collateralized mortgage obligations	\$ 6,114	\$ (89)	\$ 16	\$ (1)	\$ 6,130	\$ (90)
Other securities	<u>639</u>	<u>(11)</u>	<u>858</u>	<u>(17)</u>	<u>1,497</u>	<u>(28)</u>
	<u>\$ 6,753</u>	<u>\$ (100)</u>	<u>\$ 874</u>	<u>\$ (18)</u>	<u>\$ 7,627</u>	<u>\$ (118)</u>

Securities available for sale and held to maturity with unrealized losses at December 31, 2005, were as follows (in thousands):

	<u>Less than 12 months</u>		<u>12 months or Longer</u>		<u>Total</u>	
	<u>Market Value</u>	<u>Unrealized Losses</u>	<u>Market Value</u>	<u>Unrealized Losses</u>	<u>Market Value</u>	<u>Unrealized Losses</u>
Available for Sale						
U.S. treasury	\$ 24,761	\$ (149)	\$ 103,893	\$ (1,016)	\$ 128,654	\$ (1,165)
U.S. government agencies	44,604	(764)	35,419	(538)	80,023	(1,302)
Collateralized mortgage obligations	110,034	(1,269)	120,533	(1,940)	230,567	(3,209)
Adjustable rate mortgage securities	17,253	(72)	19,452	(485)	36,705	(557)
Obligation of state and political subdivisions	8,318	(78)	7,108	(93)	15,426	(171)
Other securities	<u>10,491</u>	<u>(139)</u>	<u>9,758</u>	<u>(242)</u>	<u>20,249</u>	<u>(381)</u>
	<u>\$ 215,461</u>	<u>\$(2,471)</u>	<u>\$ 296,163</u>	<u>\$ (4,314)</u>	<u>\$ 511,624</u>	<u>\$(6,785)</u>
Held for Maturity						
Collateralized mortgage obligations	\$ 19,763	\$ (242)	\$ -	\$ -	\$ 19,763	\$ (242)

Management of the Bank anticipates that the market values of its investments which have unrealized losses for 12 months or longer at December 31, 2006 and 2005, will increase to at least the cost of the investment to the Bank. The investments with indicated losses above include debt securities whose market values have declined due to interest rate fluctuations. In determining that the investment is not other-than-temporarily impaired the Bank considered reports of financial specialists and the volatility of the investment's fair value.

The unrealized losses on the Bank's investments in U.S. treasury obligations, U.S. government agencies, collateralized mortgage obligations, adjustable rate mortgage securities, obligations of state and political subdivisions, and other securities were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. Because the Bank has the ability and intent to hold those investments until a recovery of fair value, which may be maturity, the Bank does not consider those investments to be other-than-temporarily impaired at December 31, 2006 and 2005, respectively.

Expected maturities of some securities will differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call prepayment penalties. The scheduled maturities of securities available for sale and securities held to maturity at December 31, 2006, are shown below (in thousands):

	<u>Securities Available for Sale</u>		<u>Securities Held to Maturity</u>	
	<u>Amortized Cost</u>	<u>Approximate Fair Values</u>	<u>Amortized Cost</u>	<u>Approximate Fair Values</u>
Due in 1 year or less	\$ 31,341	\$ 30,987	\$ -	\$ -
Due after 1 year through 5 years	199,222	198,779	1,525	1,497
Due after 5 years through 10 years	18,118	18,303		
Due after 10 years	<u>37,917</u>	<u>37,845</u>	<u>1,887</u>	<u>1,887</u>
	286,598	285,914	3,412	3,384
Collateralized mortgage obligations	290,061	288,379	29,192	29,469
Adjustable rate mortgage securities	56,544	56,410		
Other	<u>16,785</u>	<u>16,779</u>		
Total	<u>\$ 649,988</u>	<u>\$ 647,482</u>	<u>\$ 32,604</u>	<u>\$ 32,853</u>

There were no proceeds from sales of securities available for sale during the year ended December 31, 2006. Proceeds from sales of securities available for sale during the year ended December 31, 2005, amounted to approximately \$90,176,000. Gross gains amounted to approximately \$2,000 for the year ended December 31, 2005. Gross losses amounted to approximately \$158,000 for the year ended December 31, 2005. Securities valued at approximately \$401,209,000 and \$310,561,000 at December 31, 2006 and 2005, respectively, were pledged as collateral to secure certain public deposits, repurchase agreements, or for other purposes.

3. LOANS

Loans classified by type, at December 31, 2006 and 2005, are summarized as follows (in thousands):

	2006	2005
Real estate:		
Adjustable	\$ 939,080	\$ 1,024,105
Fixed	406,846	321,269
Commercial and business:		
Adjustable	182,495	163,167
Fixed	62,524	106,298
Consumer:		
Adjustable	14,867	11,215
Fixed	5,890	4,459
Other	<u>100,725</u>	<u>75,693</u>
Total	<u>\$ 1,712,427</u>	<u>\$ 1,706,206</u>

At December 31, 2006 and 2005, there were no loans whose terms had been modified primarily to restructure the payment terms. Nonaccrual loans at December 31, 2006 and 2005, amounted to approximately \$146,000 and \$330,000, respectively. Interest income that would have been recorded on restructured and nonaccrual loans, if such loans were performing in accordance with their original terms, for the years ended December 31, 2006 and 2005, was not significant to net earnings.

At December 31, 2006 and 2005, the recorded investment in loans that are considered impaired was approximately \$146,000 and \$330,000, respectively. These impaired loans had no related allowance for loan losses at December 31, 2006. At December 31, 2005, these impaired loans had a related allowance of approximately \$96,000. The average recorded investment in impaired loans during the years ended December 31, 2006 and 2005, was approximately \$226,000 and \$581,000, respectively. For the years ended December 31, 2006 and 2005, the Bank recognized interest income on these impaired loans of approximately \$26,000 and \$36,000, respectively.

At December 31, 2006 and 2005, the Bank had approximately \$32,940,000 and \$30,000,000, respectively, of interest-only loans where the borrower may be subject to payment increase.

The Bank makes loans to its directors, officers, employees, and other affiliated parties on substantially the same terms, including interest rate and collateral requirements, as those prevailing at the time of the loan origination for comparable transactions with nonaffiliated persons. The aggregate amount of direct loans to directors, executive officers, and principal stockholders amounted to approximately \$12,490,000 and \$6,600,000 at December 31, 2006 and 2005, respectively. The amount of indirect loans to directors, executive officers, and principal stockholders amounted to approximately \$23,923,000 and \$3,000,000 at December 31, 2006 and 2005, respectively. At December 31, 2006, the Bank had no loan participations sold to related parties. At December 31, 2005, the Bank had loan participations sold to related parties in the amount of \$21,000,000.

Loans carried at approximately \$172,594,000 and \$223,743,000 at December 31, 2006 and 2005, respectively, were pledged as collateral to secure borrowings from the Federal Home Loan Bank of Atlanta ("FHLB").

Loans carried at approximately \$127,277,000 and \$57,974,000 at December 31, 2006 and 2005, respectively, were pledged as collateral to secure borrowings from the Federal Reserve Bank of Atlanta for contingency purposes.

4. ALLOWANCE FOR LOAN LOSSES

Transactions affecting the allowance for loan losses, at December 31, 2006 and 2005, are summarized as follows (in thousands):

	2006	2005
Balance—beginning of year	\$ 22,586	\$ 21,245
Provision for loan losses	1,178	1,500
Recoveries	187	248
Loans charged off	<u>(153)</u>	<u>(407)</u>
Balance—end of year	<u>\$ 23,798</u>	<u>\$ 22,586</u>

5. BANK PREMISES AND EQUIPMENT

Bank premises and equipment, at December 31, 2006 and 2005, are summarized as follows (in thousands):

	2006	2005
Land	\$ 6,908	\$ 6,908
Buildings and leasehold improvements	61,317	59,376
Furniture and equipment	<u>22,612</u>	<u>20,592</u>
	90,837	86,876
Less accumulated depreciation	<u>(50,857)</u>	<u>(48,125)</u>
Bank premises and equipment—net	<u>\$ 39,980</u>	<u>\$ 38,751</u>

During January 2007 the Bank sold a building for approximately \$10.5 million and recognized a gain on sale of building of approximately \$6.5 million.

6. DEPOSITS

Deposit accounts, at December 31, 2006 and 2005, consist of the following (in thousands):

	2006	2005
Demand	\$ 689,912	\$ 800,047
Interest checking	211,506	229,416
Savings	118,054	181,703
Money market savings	728,513	906,693
Time deposits	<u>254,215</u>	<u>233,431</u>
Total	<u>\$2,002,200</u>	<u>\$2,351,290</u>

Time deposits at December 31, 2006, mature as follows (in thousands):

Maturing in six months or less	\$ 166,614
Maturing between six months and one year	55,535
Maturing between one and three years	28,321
Maturing beyond three years	<u>3,745</u>
Total	<u>\$ 254,215</u>

Time certificates of deposit, issued in denominations of \$100,000 or more, amounted to approximately \$177,432,000 and \$138,047,000 at December 31, 2006 and 2005, respectively. Interest on deposits includes the following (in thousands):

	2006	2005
Interest checking	\$ 4,759	\$ 2,824
Savings	4,118	3,721
Money market savings	28,402	15,471
Time deposits in denominations of \$100,000 or more	5,157	3,908
Time deposits	<u>2,736</u>	<u>2,365</u>
Total	<u>\$45,172</u>	<u>\$28,289</u>

7. OTHER BORROWINGS

The Bank had outstanding FHLB advances, at December 31, 2006 and 2005, as follows (in thousands):

Fixed Interest Rate	Maturity Date	Callable	2006	2005
5.49 %	July 7, 2008	Continuous	\$ -	\$ 10,000
4.95	December 15, 2010	Continuous	25,000	25,000
0.00	June 15, 2017	N/A	234	234
0.00	June 28, 2017	N/A	<u>351</u>	<u>351</u>
Total			<u>\$ 25,585</u>	<u>\$ 35,585</u>

8. FEDERAL FUNDS PURCHASED AND SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

Certain information pertaining to short-term borrowings, at December 31, 2006 and 2005, is set forth in the following tables (in thousands):

	2006	2005
Federal funds purchased:		
Balances outstanding	<u>\$ 15,200</u>	<u>\$ 200</u>
Largest amount outstanding at any month-end	<u>15,200</u>	<u>3,600</u>
Average balance outstanding during the year	<u>945</u>	<u>2,873</u>
Weighted-average interest rate for the year	<u>4.94 %</u>	<u>3.05 %</u>
Securities sold under agreements to repurchase:		
Balances outstanding	<u>\$423,261</u>	<u>\$258,057</u>
Largest amount outstanding at any month-end	<u>451,130</u>	<u>438,860</u>
Average balance outstanding during the year	<u>420,299</u>	<u>356,688</u>
Weighted-average interest rate for the year	<u>4.46 %</u>	<u>2.85 %</u>

9. COMMITMENTS AND CONTINGENCIES

In the normal course of business, various commitments and contingent liabilities are outstanding that are not reflected in the financial statements. A summary of these commitments and contingent liabilities at December 31, 2006 and 2005, is as follows (in thousands):

	2006	2005
Standby letters of credit	\$ 60,301	\$ 58,536
Commitments to extend credit	773,986	760,895

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. At December 31, 2006 and 2005, standby letters of credit amounting to approximately \$17,469,000 and \$21,934,000, respectively, were secured by cash collateral or marketable securities. The liability recorded by the Bank related to the fair value of standby letters of credit outstanding at December 31, 2006 and 2005, was \$196,000 and \$199,000, respectively, and is included in other liabilities in the accompanying balance sheets.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary, is based on management's credit evaluation.

The Bank is a defendant in various lawsuits, and in the opinion of management, based on consultation with legal counsel, the outcome of these lawsuits will not have a material effect on the results of operations or financial position of the Bank.

The Bank has entered into a number of noncancelable operating lease agreements for premises and equipment. The minimum annual rental commitments under these leases at December 31, 2006, are summarized as follows (in thousands):

Years Ending December 31	Amount
2007	\$ 1,994
2008	1,862
2009	1,433
2010	1,119
2011	908
Thereafter	<u>12,640</u>
Total	<u>\$19,956</u>

Rent expense under all leases having initial noncancelable terms of more than one year was approximately \$2,191,000 and \$2,134,000 in 2006 and 2005, respectively.

10. EMPLOYEE BENEFIT PLAN

During 1987, the Bank adopted a Retirement Savings Trust and Retirement Savings Plan (the “Plan”), a defined contribution 401(k) plan. The Plan covers all employees who are 21 years of age with more than 90 days of service as of the Plan entry dates of January 1 and July 1. Employees qualify for benefits upon reaching the age of 65 or upon permanent disability. Beginning January 1, 2001, the Plan was amended allowing employees to be 100% vested in the employer matching contributions made starting that date and thereafter. Employer contributions made prior to that date are subject to the vesting schedule that was in effect: vesting began at 20% after two years of service, increasing by 20% per year until full vesting occurs. Participants receive a 100% employer matching contribution up to 5% of their pretax compensation. In addition, the Bank may make a discretionary contribution from current or accumulated profits. During 2006 and 2005, the Bank contributed approximately \$860,000 and \$851,000, respectively, to the Plan.

11. STOCK APPRECIATION RIGHTS

On January 1, 1998, the Parent created a Management Stock Appreciation Rights Plan with up to 200,000 shares available for grants to employees. Vesting of these stock appreciation rights (“SARs”) begins at 10% one year after the anniversary date of the grant and continues at 10% per year until full vesting occurs after 10 years. There were no SARs granted during 2006. During 2005, there were 10,000 SARs granted to employees at the Parent’s book value price per share. There were 4,750 SARs forfeited during 2006 and no SARs exercised. There were 3,750 SARs forfeited during 2005 and no SARs exercised. The Bank recognized \$1,374,000 and \$978,000 in compensation expense relating to these grants during the years ended December 31, 2006 and 2005, respectively.

12. REGULATORY MATTERS

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 2006, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2006 and 2005, the most recent notification from the Office of the Comptroller of the Currency categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. 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. There are no conditions or events since that notification that management believes have changed the institution’s category.

The Bank's actual capital amounts and ratios are also presented in the table below:

	<u>Actual</u>		<u>Required for Capital Adequacy Purposes</u>		<u>Required to be Categorized as Well Capitalized Under Prompt Corrective Action Provisions</u>	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2006:						
Total capital (to risk-weighted assets)	\$303,715,000	14.8 %	\$164,052,000	8.0 %	\$205,065,000	10.0 %
Tier I capital (to to risk-weighted assets)	278,926,000	13.6	82,026,000	4.0	123,039,000	6.0
Tier I capital (to average assets)	278,926,000	10.1	110,726,000	4.0	138,408,000	5.0
As of December 31, 2005:						
Total capital (to risk-weighted assets)	\$272,152,000	13.2 %	\$165,000,000	8.0 %	\$206,000,000	10.0 %
Tier I capital (to to risk-weighted assets)	248,515,000	12.1	82,000,000	4.0	123,000,000	6.0
Tier I capital (to average assets)	248,515,000	8.7	114,000,000	4.0	142,000,000	5.0

Banking regulations limit the amount of dividends that may be paid without prior approval of the federal banking regulators. Retained earnings from which dividends may be paid by the Bank without prior approval of the federal banking regulators amounted to approximately \$82,415,000 at December 31, 2006.

13. FAIR VALUE OF FINANCIAL INSTRUMENTS

The following tables set forth information pertaining to the estimated fair value of the Bank's financial instruments as of December 31, 2006 and 2005. The estimated fair value amounts have been determined using available market information and appropriate valuation methodologies. However, considerable judgment is necessarily required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Bank 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. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since December 31, 2006, and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

	December 31, 2006		December 31, 2005	
	Carrying Amount (In Thousands)	Fair Value (In Thousands)	Carrying Amount (In Thousands)	Fair Value (In Thousands)
Assets:				
Cash and cash equivalents	\$ 310,128	\$ 310,128	\$ 571,386	\$ 571,386
Interest-bearing balances with financial institutions	5,693	5,693	306	306
Securities held to maturity	32,604	32,853	32,353	32,294
Securities available for sale	647,482	647,482	557,325	557,325
Loans	1,712,427	1,694,387	1,706,206	1,692,991
Liabilities:				
Demand deposits, interest checking accounts, savings accounts, and money market deposits	\$ 1,747,985	\$ 1,747,985	\$ 2,117,859	\$ 2,117,859
Time deposits	254,215	254,173	233,431	232,905
Other borrowings	25,585	25,522	35,585	35,619
Federal funds purchased and securities sold under agreement to repurchase	438,461	438,461	258,257	258,257

Cash and Cash Equivalents—The carrying amount of cash and due from banks and federal funds sold is a reasonable estimate of fair value due to the relatively short period to maturity of these instruments.

Interest-Bearing Balances With Financial Institutions—The fair value of time deposits with other banks is estimated using the rates currently offered for deposits of similar maturities and taking into account the creditworthiness of the other bank.

Securities—For securities available for sale, fair values are based on quoted market prices or dealer quotes. For securities held to maturity, fair value equals quoted market price, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Federal Funds and Securities Purchased Under Agreements to Resell—The carrying values for federal funds sold and securities purchased under agreements to resell approximate fair value due to the relatively short period to maturity of these instruments.

Loans—The Bank has determined that the carrying value of variable rate loans with good credit risk and variable rate loans repricing in the near future approximates fair values. The fair value of other types of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

Demand Deposits and Time Deposits—The fair value of demand deposits, interest checking accounts, savings accounts, and certain money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities.

Other Borrowings—The fair value of other borrowings is estimated using the rates currently offered for borrowings of similar maturities.

Federal Funds Purchased and Securities Sold Under Agreements to Repurchase—The carrying values for federal funds purchased and securities sold under agreements to repurchase approximate fair value due to the relatively short period to maturity of these instruments.

Off-Balance Sheet Instruments—The fair values of standby letters of credit, commitments to extend credit, forward contracts, and commitments to purchase securities approximate carrying value due to the insignificant differences between the stated rates and the current market rates. The fair value of the off-balance sheet instruments at December 31, 2006 and 2005 were not material.

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