

Dear Shareholders:

Banking in the Chicagoland area in 2009 was as bad as being a die hard Cubs fan, all pain and little to show for it. It was a year that had over 100 banks close by the FDIC nationwide, and many more on the bubble as institutions in large metropolitan areas struggled with bad loans and high unemployment. Chicago and Atlanta led the pack with large drops in the value of housing. The Bank's results were reflective of the large drops in real estate values and the extended recession.

The low interest rate environment has been positive for the Bank. The Federal Reserve has kept rates low, as it tries to offset the decline in consumer and business spending. The prime rate is at 3.25%, the same as a year ago.

The low interest rates have also allowed the Bank to reduce our cost of funds. We were able to reduce long term borrowings and our cost of funds reduced from 3.10% at year end December 2008 to 2.01% December 2009. As we are forecasting rates to remain constant over the next 6 – 8 months, this low rate environment will give us the opportunity for further improvement.

How is NSCB responding?

We are conserving capital to maintain our Total Risk Based Capital Ratio to be "well capitalized" and at year end 2009 it was 13.7%, a very strong ratio. Strong capital is important to the Bank's success. There has been much concern about a double dip recession, increased taxes, vacancy rates, unbridled government spending and the sustainability of government programs. NorthSide Community Bank is trying to anticipate the changes on the horizon and our focus continues to be to improve loan quality.

The recession has caused us to re-tool, re-think and revise many processes and policies. We have reviewed all vendor contracts and leases, changed

underwriting, increased monitoring and took expense control to new levels. The results were better underwriting and improved efficiencies throughout the Bank.

Financial Results

For the year in 2009, the Bank continued its strategy to downsize. Assets decreased by 11% to \$494 million, loans decreased by 14% to \$433 million and deposits decreased by 7% to \$409 million.

During the fourth quarter of 2009, we made the decision to charge off a substantial level of loans to recognize two large corporate bankruptcies which occurred with long term borrowers. Non-performing assets were reduced as a percentage of capital to 38.57%. The majority of non-accrual loans which remain are construction loans made during 2006 and vacant land development loans made in the same timeframe. The market is still frozen in terms of buyers for these assets and in some cases, offers are well below "fire sale" appraisals. We will hold these properties long-term if necessary.

Our loan loss provision for the year was \$28 million and our loan loss reserve is at a solid 2.76% of total loans. Charge-offs for 2009 were extremely high at over \$28 million, and in part is a reflection of just how quickly pricing has fallen in Chicago and the suburbs.

The Company was not profitable in 2009 and is reporting a net loss of \$14.1 million. In November 2009, the American Recovery and Reinvestment Act of 2009 allowed eligible small businesses to elect a carry back of net operating losses for 5 years. This gave us the ability to move aggressively and charge off potential losses on non performing assets. Our level of non-performing assets then dropped significantly and we booked a receivable from the Treasury in the amount of \$8.1 million. At the holding company level, book value decreased to \$67 per share at year end 2009, down from \$92 per share the prior year.

Preserving Value

We are very pleased with our existing staff of 50. Our staff is extremely efficient and all efforts continue to focus on minimizing the negative impact of the current business cycle. Their qualifications, experience and productivity will help build the Bank as we move forward. Our goal for 2010 is to return to profitability, conserve capital, continue to build the loan loss reserve, collect our non-accrual loans and liquidate OREO. This will set the foundation for higher earnings, as we are used to, in future years. Our core base of customers continues to enhance our value and we are well prepared to serve their financial needs.

Our shareholders and our Board of Directors have been terrific in their support throughout these difficult economic times. We are certain that with your patience and support, NorthSide will continue to provide the communities it serves with *The Very Best In Banking*.

The attached detailed audited financials give you the details and a year over year comparison. If you have any questions, please contact us at 847-279-1155.

Sincerely,

Patricia A. Clausen
Chairman

James S. Randall
President

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

ASSETS

| | December 31, | |
|--|----------------------|----------------------|
| | 2009 | 2008 |
| Cash and due from banks | \$ 3,298,647 | \$ 17,350,782 |
| Interest bearing deposits in other banks | 17,615,724 | 9,087,144 |
| Investment securities: | | |
| Available-for-sale | 701,829 | 673,039 |
| Held-to-maturity | 4,038,360 | 6,766,412 |
| Federal Home Loan Bank and Federal Reserve Bank stock | 2,778,350 | 2,928,350 |
| Loans | 433,343,111 | 507,698,790 |
| Allowance for loan losses | (11,969,104) | (12,481,407) |
| Premises and equipment | 5,615,922 | 5,977,268 |
| Other real estate owned and repossessed assets | 16,125,239 | 5,179,345 |
| Accrued interest receivable | 1,267,808 | 1,535,310 |
| Deferred income tax benefit | 8,748,549 | 7,663,645 |
| Refundable income taxes | 8,255,198 | - |
| Other assets | 4,606,841 | 4,353,717 |
| | <u>\$494,426,474</u> | <u>\$556,732,395</u> |

LIABILITIES AND SHAREHOLDERS' EQUITY

| | | |
|--|----------------------|----------------------|
| Liabilities: | | |
| Deposits: | | |
| Non-interest bearing | \$ 24,357,985 | \$ 30,352,291 |
| Interest bearing | <u>385,380,164</u> | <u>410,956,492</u> |
| Total deposits | 409,738,149 | 441,308,783 |
| Short-term borrowings | 9 | 310,082 |
| Long-term borrowings | 38,500,000 | 55,000,000 |
| Other liabilities | <u>7,990,171</u> | <u>8,054,434</u> |
| Total liabilities | <u>456,228,329</u> | <u>504,673,299</u> |
| Shareholders' equity: | | |
| Preferred stock, par value \$.01 per share; authorized 25,000 shares | - | - |
| Common stock, par value \$.01 per share; authorized 1,200,000 shares; issued and outstanding 570,266 shares in 2009 and 567,649 shares in 2008 | 5,703 | 5,676 |
| Additional paid-in capital | 19,014,267 | 18,770,913 |
| Retained earnings | 19,191,947 | 33,299,371 |
| Accumulated other comprehensive loss | <u>(13,772)</u> | <u>(16,864)</u> |
| Total shareholders' equity | <u>38,198,145</u> | <u>52,059,096</u> |
| Total liabilities and shareholders' equity | <u>\$494,426,474</u> | <u>\$556,732,395</u> |

The accompanying notes are an integral part of these financial statements.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS

| | For the Year Ended December 31, | |
|---|------------------------------------|---------------|
| | 2009 | 2008 |
| Interest income: | | |
| Interest and fees on loans | \$ 26,598,078 | \$ 33,479,504 |
| Interest on federal funds sold | 56 | 59,781 |
| Interest and dividends on investment securities | 320,738 | 389,207 |
| Interest on deposits in other banks | 60,835 | 82,421 |
| Total interest income | 26,979,707 | 34,010,913 |
| Interest expense: | | |
| Interest on deposits | 10,531,188 | 13,917,422 |
| Interest on short-term borrowings | 2,603 | 102,664 |
| Interest on long-term borrowings | 2,403,468 | 2,940,586 |
| Total interest expense | 12,937,259 | 16,960,672 |
| Net interest income | 14,042,448 | 17,050,241 |
| Provision for loan losses | 28,039,700 | 6,723,000 |
| Net interest income (loss) after provision for loan losses | (13,997,252) | 10,327,241 |
| Other income: | | |
| Fees for customer services | 341,392 | 359,968 |
| Other operating income | 156,191 | 147,553 |
| Total other income | 497,583 | 507,521 |
| Other expenses: | | |
| Salaries and employee benefits | 3,712,056 | 3,869,969 |
| Occupancy and equipment expense | 1,062,330 | 983,566 |
| Other real estate owned and repossessed asset expense | 1,235,475 | 1,502,021 |
| FDIC assessment | 1,047,733 | 384,595 |
| Other | 2,703,394 | 2,495,323 |
| Total other expenses | 9,760,988 | 9,235,474 |
| Income (loss) before income taxes | (23,260,657) | 1,599,288 |
| Income tax expense (benefit) | (9,153,233) | 747,356 |
| Net income (loss) | \$(14,107,424) | \$ 851,932 |

The accompanying notes are an integral part of these financial statements.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
For the Years Ended December 31, 2009 and 2008

| | Common Stock | | Additional Paid-In Capital | Accumulated Other Comprehensive Loss | Retained Earnings | Total |
|---|----------------|-----------------|----------------------------------|---|----------------------|---------------------|
| | Shares | Amount | | | | |
| Balance, January 1, 2008 | 581,682 | \$ 5,817 | \$20,486,295 | \$ (17,007) | \$32,652,354 | <u>\$53,127,459</u> |
| Net income | - | - | - | - | 851,932 | 851,932 |
| Net change in unrealized loss on securities available-for-sale, net of deferred taxes | - | - | - | 143 | - | <u>143</u> |
| Comprehensive income | | | | | | <u>852,075</u> |
| Cash dividend paid - \$0.36 | - | - | - | - | (204,915) | (204,915) |
| Shares acquired | (20,766) | (208) | (2,555,406) | - | - | (2,555,614) |
| Shares sold | <u>6,733</u> | <u>67</u> | <u>840,024</u> | <u>-</u> | <u>-</u> | <u>840,091</u> |
| Balance, December 31, 2008 | 567,649 | 5,676 | 18,770,913 | (16,864) | 33,299,371 | <u>52,059,096</u> |
| Net loss | - | - | - | - | (14,107,424) | (14,107,424) |
| Net change in unrealized loss on securities available-for-sale, net of deferred taxes | - | - | - | 3,092 | - | <u>3,092</u> |
| Comprehensive loss | | | | | | <u>(14,104,332)</u> |
| Shares sold | <u>2,617</u> | <u>27</u> | <u>243,354</u> | <u>-</u> | <u>-</u> | <u>243,381</u> |
| Balance, December 31, 2009 | <u>570,266</u> | <u>\$ 5,703</u> | <u>\$19,014,267</u> | <u>\$ (13,772)</u> | <u>\$19,191,947</u> | <u>\$38,198,145</u> |

The accompanying notes are an integral part of these financial statements.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

| | For the Year Ended | |
|--|--------------------|--------------|
| | December 31, | |
| | 2009 | 2008 |
| Cash flows from operating activities: | | |
| Net income (loss) | \$ (14,107,424) | \$ 851,932 |
| Adjustments to reconcile net income (loss) to cash provided by operating activities: | | |
| Net premium amortization | 1,566 | 5,974 |
| Provision for depreciation | 387,757 | 410,332 |
| Provision for loan losses | 28,039,700 | 6,723,000 |
| Gain on sale of other real estate owned | (265,111) | (22,220) |
| Provision for loss on other real estate owned and repossessed assets | 498,007 | 1,268,818 |
| Provision for deferred income tax benefit | (1,086,866) | (813,787) |
| Decrease in accrued interest receivable | 267,502 | 655,569 |
| Increase in refundable income taxes | (8,255,198) | - |
| Increase in other assets | (46,354) | (69,572) |
| Decrease in other liabilities | (271,033) | (1,141,940) |
| Net cash provided by operating activities | 5,162,546 | 7,868,106 |
| Cash flows from investing activities: | | |
| Proceeds from securities held-to-maturity | 5,726,486 | 15,200,754 |
| Purchase of securities held-to-maturity | (3,000,000) | (4,956,620) |
| Proceeds from maturity of securities available-for-sale | - | 2,000,000 |
| Purchase of securities available-for-sale | (23,736) | (1,024,707) |
| Redemption of Federal Reserve Bank stock | 150,000 | - |
| Net decrease (increase) in loans | 28,057,632 | (1,523,875) |
| Proceeds from sale of other real estate owned | 6,567,254 | 910,390 |
| Capital expenditures | (26,411) | (156,328) |
| Net cash provided by investing activities | 37,451,225 | 10,449,614 |
| Cash flows from financing activities: | | |
| Net decrease in deposits | (31,570,634) | (9,968,662) |
| Net decrease in short-term borrowings | (310,073) | (177,222) |
| Issuance of long-term debt | 11,000,000 | 9,000,000 |
| Payment on long-term debt | (27,500,000) | (8,000,000) |
| Issuance of stock | 243,381 | 840,091 |
| Company stock acquired and retired | - | (2,555,614) |
| Dividend paid | - | (204,915) |
| Net cash used in financing activities | (48,137,326) | (11,066,322) |

The accompanying notes are an integral part of these financial statements.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

| | For the Year Ended | |
|--|----------------------|----------------------|
| | December 31, | |
| | <u>2009</u> | <u>2008</u> |
| Net (decrease) increase in cash and cash equivalents | (5,523,555) | 7,251,398 |
| Cash and cash equivalents at beginning of year | <u>26,437,926</u> | <u>19,186,528</u> |
| Cash and cash equivalents at end of year | <u>\$ 20,914,371</u> | <u>\$ 26,437,926</u> |
| <u>Supplemental schedule of noncash investing</u> | | |
| <u>and financing activities:</u> | | |
| Contribution and net earnings of the 401(k) trusts | <u>\$ 206,770</u> | <u>\$ 217,102</u> |
| Net unrealized gain on investment securities available-for-sale, net of deferred income taxes | <u>\$ 3,092</u> | <u>\$ 143</u> |
| Transfer from loans to other real estate owned and repossessed assets | <u>\$ 17,746,044</u> | <u>\$ 7,336,333</u> |
| <u>Supplemental disclosures of cash flow information:</u> | | |
| Cash payments for: | | |
| Interest on deposits | \$ 11,437,763 | \$ 14,335,893 |
| Interest on borrowings | 1,779,702 | 3,005,991 |
| Income taxes | 215,832 | 1,812,161 |

The accompanying notes are an integral part of these financial statements.

**AliKat Investments, Inc.
and Subsidiary**

**Consolidated Financial Statements
and
Independent Auditor's Report
For the Year Ended
December 31, 2009**

Wolf & Company LLP
Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT

The Board of Directors
AliKat Investments, Inc.
Gurnee, Illinois

We have audited the accompanying consolidated balance sheets of ALIKAT INVESTMENTS, INC. AND SUBSIDIARY as of December 31, 2009 and 2008, and the related consolidated statements of operations, changes in shareholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated 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 consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated 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 consolidated financial position of AliKat Investments, Inc. and Subsidiary as of December 31, 2009 and 2008, 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.

Oak Brook, Illinois
February 19, 2010

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

The accompanying consolidated financial statements have been prepared in conformity with generally accepted accounting principles and conform to practices within the banking industry.

Principles of Consolidation - The consolidated financial statements of AliKat Investments, Inc. include the accounts of the Company and its wholly-owned subsidiary, NorthSide Community Bank. Material intercompany accounts and transactions have been eliminated.

Nature of Operations - The Company is a bank holding company and through its banking subsidiary offers a broad range of financial services to customers in the Illinois counties of Cook and Lake. The financial services offered are principally orientated toward individual consumers and small and medium sized businesses and are typical of those offered by a commercial bank.

Use of Estimates - The preparation of consolidated financial statements in conformity with generally accepted accounting principles 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 income and expenses during the reporting year. Actual results could differ from these estimates.

Statements of Cash Flows - For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks, interest-bearing deposits in other banks and federal funds sold. Generally, federal funds are sold for one day periods.

Interest-bearing Deposits in Other Banks - Interest-bearing deposits in other banks mature within one year and are carried at cost.

Investment Securities - Financial Accounting Standards require that debt and equity securities be classified into one of three reporting categories and accounted for as follows: (1) held-to-maturity securities reported at amortized cost, (2) trading securities reported at fair value with unrealized gains and losses included in earnings, and (3) available-for-sale securities reported at fair value with unrealized gains and losses net of related taxes reported as an increase or decrease in other comprehensive income.

Securities held-to-maturity are securities that the Company has the intent and ability to hold to maturity and are carried at cost adjusted for amortization of premium and accretion of discount, generally computed using the interest method.

Securities available-for-sale are securities that are intended to be held for indefinite periods of time, but which may not be held to maturity. These securities may be used as a part of the Company's asset/liability management strategy and may be sold in response to changes in interest rates, deterioration of issuer's creditworthiness, or due to a desire to increase capital or liquidity.

Realized securities gains and losses are determined on a specific identification basis and are reported in the consolidated statements of income as securities gains and losses.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies (Cont.)

Loans - Loans are stated at the unpaid principal balances, less the allowance for loan losses and net deferred loan fees and unearned discounts.

Unearned discounts on installment loans are recognized as income over the term of the loans using a method that approximates the interest method.

Loan origination and commitment fees, as well as certain direct origination costs, are deferred and amortized as a yield adjustment over the lives of the related loans using the interest method. Amortization of deferred loan fees is discontinued when a loan is placed on nonaccrual status.

The accrual of interest on mortgage and commercial loans is discontinued at the time the loan is 90 days delinquent unless the credit is well secured and in process of collection. Credit card loans and other personal loans are typically charged off no later than 180 days past due. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off 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 Losses - The allowance for loan losses is maintained at a level which, in management's judgment, is adequate to absorb potential losses inherent in the loan portfolio. The amount of the allowance is based on management's evaluation of the collectibility of the loan portfolio, including the nature of the portfolio, credit concentrations, trends in historical loss experience, specific impaired loans, economic conditions and other risks inherent in the portfolio. Allowances for impaired loans are generally determined based on collateral values or the present value of estimated cash flows. Although management uses available information to recognize losses on loans, because of uncertainties associated with local economic conditions, collateral values, and future cash flows on impaired loans, it is reasonably possible that a material change could occur in the allowance for loan losses in the near term. However, the amount of change that is reasonably possible cannot be estimated. The allowance is increased by a provision for loan losses, which is charged to expense and reduced by charge-offs, net of recoveries. Changes in the allowance relating to impaired loans are charged or credited to the provision for loan losses.

Foreclosed Assets - Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets.

Premises and Equipment - Premises and equipment are stated at cost less accumulated depreciation. The provision for depreciation included in operating expenses is computed on the straight-line method based on the estimated useful lives of the assets.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies (Cont.)

Income Taxes - The Company files consolidated income tax returns with its subsidiary, NorthSide Community Bank. Each member of the consolidated group provides for income taxes on a separate return basis and is charged or credited by the Company with the tax or tax benefit shown in a separate return. The provision for income taxes is based on amounts reported in the statements of income adjusted for differences that do not enter into the computation of taxes payable under applicable laws. The Company recognizes deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the financial reporting and tax basis of the Company's assets and liabilities. Measurement of deferred tax assets and liabilities is based upon the provision of enacted tax laws and the effects of future changes in tax laws or rates.

Accounting for Uncertain Tax Positions - In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes*, which was codified into Accounting Standards Codification No. 740, *Income Taxes* (ASC No. 740). FIN 48/ASC No. 740 provides detailed guidance for the financial statement recognition, measurement and disclosure of uncertain tax positions recognized in an entity's financial statements in accordance with Statement of Financial Accounting Standards (SFAS) No. 109, *Accounting for Income Taxes*, which was also codified into ASC No. 740. FIN 48/ASC No. 740 requires an entity to recognize the financial statement impact of a tax position when it is more likely than not that the position will be sustained upon examination. The Company adopted the provisions of this statement in 2009.

Fair Value Measurements - In September 2006, the FASB issued Statement No. 157 (SFAS No. 157), *Fair Value Measurements*, which was codified into Accounting Standards Codification No. 820, *Fair Value Measurements and Disclosures* (ASC No. 820). SFAS No. 157/ASC No. 820 was issued to establish a uniform framework for measuring fair value and expand disclosures about fair value measurements. SFAS No. 157/ASC No. 820 applies whenever other authoritative literature requires or permits fair value measurements, but does not expand the use of fair value.

As required by the pronouncement, the Company adopted the provisions of this statement in 2008 as it related to financial assets and liabilities. The adoption of the provisions of this statement in 2009 as it relates to nonfinancial assets and liabilities resulted in no material impact on the Company's financial position or results of operations.

Stock Incentive Plan - Employee compensation expense under the stock option plan is reported using the intrinsic value method. As such, compensation expense would be recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price.

Comprehensive Income - Comprehensive income consists of net income and unrealized gains and losses on securities available-for-sale and is presented in the consolidated statements of changes in shareholders' equity.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2. Cash and Due From Banks

Included in cash and due from banks is an amount required to be deposited with the Federal Reserve Bank. This reserve balance may vary depending on the level of customer deposits in the subsidiary bank. At December 31, 2009 and 2008, the reserve balance requirements were \$73,000 and \$383,000, respectively.

3. Investment Securities

The amortized cost of securities and their approximate fair values are as follows:

| | <u>Amortized Cost</u> | <u>Gross Unrealized Gains</u> | <u>Gross Unrealized Losses</u> | <u>Fair Value</u> |
|----------------------------------|---------------------------|---------------------------------------|--|-----------------------|
| December 31, 2009: | | | | |
| Available-for-sale: | | | | |
| Equity securities | \$ 75,000 | \$ - | \$ - | \$ 75,000 |
| Mutual funds | <u>649,339</u> | <u>-</u> | <u>22,510</u> | <u>626,829</u> |
| | <u>\$ 724,339</u> | <u>\$ -</u> | <u>\$ 22,510</u> | <u>\$ 701,829</u> |
| Held-to-maturity: | | | | |
| U.S. Government agencies | \$ 2,750,000 | \$ 22,344 | \$ 4,688 | \$ 2,767,656 |
| State and political subdivisions | <u>1,288,360</u> | <u>47,176</u> | <u>-</u> | <u>1,335,536</u> |
| | <u>\$ 4,038,360</u> | <u>\$ 69,520</u> | <u>\$ 4,688</u> | <u>\$ 4,103,192</u> |
| December 31, 2008: | | | | |
| Available-for-sale: | | | | |
| Equity securities | \$ 75,000 | \$ - | \$ - | \$ 75,000 |
| Mutual funds | <u>625,602</u> | <u>-</u> | <u>27,563</u> | <u>598,039</u> |
| | <u>\$ 700,602</u> | <u>\$ -</u> | <u>\$ 27,563</u> | <u>\$ 673,039</u> |
| Held-to-maturity: | | | | |
| U.S. Government agencies | \$ 3,749,689 | \$ 57,577 | \$ 313 | \$ 3,806,953 |
| State and political subdivisions | <u>3,016,723</u> | <u>57,576</u> | <u>1,924</u> | <u>3,072,375</u> |
| | <u>\$ 6,766,412</u> | <u>\$ 115,153</u> | <u>\$ 2,237</u> | <u>\$ 6,879,328</u> |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

3. Investment Securities (Cont.)

The amortized cost and fair value of the securities at December 31, 2009, by contractual maturity, are as follows:

| | Available-for-Sale | | Held-to-Maturity | |
|--|--------------------|-------------------|---------------------|---------------------|
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| Due in one year or less | \$ - | \$ - | \$ 506,842 | \$ 524,224 |
| Due after one year through five years | - | - | 1,823,518 | 1,870,474 |
| Due after five years through ten years | - | - | 1,669,000 | 1,668,601 |
| Due after ten years | - | - | 39,000 | 39,893 |
| Equity securities and mutual funds | <u>724,339</u> | <u>701,829</u> | <u>-</u> | <u>-</u> |
| | <u>\$ 724,339</u> | <u>\$ 701,829</u> | <u>\$ 4,038,360</u> | <u>\$ 4,103,192</u> |

Federal Home Loan Bank and Federal Reserve Bank stock are carried at amortized cost as no market exists for the stock.

Securities with a carrying value of \$1,000,000 and \$499,689 on December 31, 2009 and 2008, respectively, were pledged to secure securities sold under agreement to repurchase and public funds.

4. Loans

The following is a summary of loans outstanding:

| | December 31, | |
|----------------------------|-----------------------|-----------------------|
| | 2009 | 2008 |
| Commercial and industrial | \$ 58,008,186 | \$ 66,351,456 |
| Real estate - construction | 6,675,582 | 66,395,288 |
| Real estate - mortgage | 367,176,537 | 373,259,336 |
| Loans to individuals | 1,525,342 | 1,923,019 |
| Other | <u>21,344</u> | <u>18,832</u> |
| | 433,406,991 | 507,947,931 |
| Unearned income | <u>63,880</u> | <u>249,141</u> |
| | <u>\$ 433,343,111</u> | <u>\$ 507,698,790</u> |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

4. Loans (Cont.)

At December 31, 2009 and 2008, loans with carrying values of \$22,691,999 and \$60,927,875, respectively, were recognized as impaired. The average balance outstanding on these loans was approximately \$22,805,000 and \$58,010,000 for the years ended December 31, 2009 and 2008, respectively. The allowance for loan losses related to impaired loans amounted to approximately \$2,216,000 and \$9,325,000 at December 31, 2009 and 2008, respectively. Interest income on impaired loans of \$1,036,000 and \$1,117,000 was recognized for cash payments received in 2009 and 2008, respectively. The Bank has commitments of \$100,896 to loan additional funds to borrowers whose loans have been modified.

Additional nonperforming loans amounted to \$10,928,905 and \$7,790,522 at December 31, 2009 and 2008, respectively. Interest income based on the original contract terms of these loans would have been approximately \$1,761,000 and \$535,000 at December 31, 2009 and 2008, respectively. Actual interest recognized amounted to \$321,000 and \$26,000 in 2009 and 2008, respectively.

Loans to directors of the Company were made in the ordinary course of business and were made on substantially the same terms, including rates and collateral, as those prevailing at the time for comparable transactions with other persons and did not involve more than the normal risk of collectibility or present other unfavorable features.

As of December 31, 2009 and 2008, loans aggregating \$9,211,769 and \$21,433,701, respectively, were outstanding to directors, executive officers and certain associates. During 2009, new loans aggregating \$1,869,343 and amounts collected of \$1,019,944 were transacted with such parties.

5. Allowance for Loan Losses

Changes in the allowance for loan losses were as follows:

| | For the Year Ended December 31, | |
|----------------------------|------------------------------------|----------------------|
| | 2009 | 2008 |
| Balance, beginning of year | \$ 12,481,407 | \$ 11,747,807 |
| Provision for loan losses | 28,039,700 | 6,723,000 |
| Loan recoveries | 43,689 | 108,716 |
| | <u>40,564,796</u> | <u>18,579,523</u> |
| Loans charged off | <u>28,595,692</u> | <u>6,098,116</u> |
| Balance, end of year | <u>\$ 11,969,104</u> | <u>\$ 12,481,407</u> |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

6. Premises and Equipment

Premises and equipment are summarized as follows:

| | December 31, | |
|---------------------------|--------------|--------------|
| | 2009 | 2008 |
| Land | \$ 1,428,206 | \$ 1,428,206 |
| Building and improvements | 4,927,256 | 4,927,256 |
| Leasehold improvements | 530,737 | 512,826 |
| Equipment | 1,901,561 | 1,931,483 |
| Deposit on equipment | - | 2,577 |
| | 8,787,760 | 8,802,348 |
| Accumulated depreciation | 3,171,838 | 2,825,080 |
| | \$ 5,615,922 | \$ 5,977,268 |

Depreciation charged to operations amounted to \$387,757 in 2009 and \$410,332 in 2008.

7. Deposits

Time certificates of deposit \$100,000 and over included in interest-bearing deposits at December 31, 2009 and 2008 amounted to approximately \$108,088,000 and \$117,233,000, respectively.

The following table sets forth the maturities of the Company's time deposits at December 31, 2009:

| | |
|-----------------------------------|----------------|
| Three months or less | \$ 63,345,958 |
| Over three months to one year | 199,462,384 |
| Over one year through three years | 36,065,846 |
| Over three years | 1,645,720 |
| Total | \$ 300,519,908 |

8. Short-term Borrowings

At December 31, 2009 and 2008 short-term borrowings consisted of the following:

| | 2009 | 2008 |
|---|------|------------|
| Securities sold under agreements to repurchase, maturing in one to five days from date of sale and bear interest at the 90 day U.S. Treasury rate less 10 basis points. | \$ 9 | \$ 310,082 |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

9. Long-term Borrowings

At December 31, 2009 and 2008, long-term borrowings consisted of the following:

| | 2009 | 2008 |
|--|-----------|--------------|
| Arrangement with the Federal Home Loan Bank (FHLB) whereby the FHLB will make advances to the Bank with repayment terms from overnight to five years. The advances to the Bank are collateralized by all qualified one to four family first lien mortgages and multi-family, totaling approximately \$27,873,852 at December 31, 2009. Outstanding advances at December 31, 2009 and 2008 were as follows: | | |
| FHLB advances, 2.66%, interest payable monthly, due January 23, 2009 | \$ - | \$ 1,000,000 |
| FHLB advances, 2.68%, interest payable monthly, due February 9, 2009 | - | 2,000,000 |
| FHLB advances, 2.66%, interest payable monthly, due March 2, 2009 | - | 2,000,000 |
| FHLB advances, 3.06%, interest payable monthly, due July 7, 2009 | - | 2,000,000 |
| FHLB advances, 5.55%, interest payable monthly, due July 20, 2009 | - | 5,000,000 |
| FHLB advances, 5.22%, interest payable monthly, due August 28, 2009 | - | 6,000,000 |
| FHLB advances, 5.55%, interest payable monthly, due July 19, 2010 | 5,000,000 | 5,000,000 |
| FHLB advances, 4.46%, interest payable monthly, due July 22, 2010 | 2,000,000 | 2,000,000 |
| FHLB advances, 5.13%, interest payable monthly, due February 28, 2011 | 3,000,000 | 3,000,000 |
| FHLB advances, 1.53%, interest payable monthly, due July 7, 2011 | 2,000,000 | - |
| FHLB advances, 3.87%, interest payable monthly, due in semi-annual payments with final payment due August 27, 2012 | 1,500,000 | 2,000,000 |
| FHLB advances, 3.12%, interest payable monthly, due July 9, 2014 | 5,000,000 | - |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

9. Long-term Borrowings (Cont.)

| | <u>2009</u> | <u>2008</u> |
|--|----------------------|----------------------|
| Revolving loan agreement at stated interest rates payable quarterly, due February 28, 2009, secured by 100% of Bank subsidiary, total eligible borrowing is \$5,000,000. | - | 5,000,000 |
| Junior Subordinated Debentures due June 24, 2035, interest payable quarterly at 5.91% until June 24, 2012 then at three-month LIBOR rate plus 1.75%. In 2009, the Company exercised its option to suspend payment of interest. | 10,000,000 | 10,000,000 |
| Fixed/Floating Rate Junior Subordinated Deferrable Interest Debenture due September 15, 2037, interest payable quarterly at 6.64% until June 2017 then at three-month LIBOR rate plus 1.57%. In 2009, the Company exercised its option to suspend payment of interest. | <u>10,000,000</u> | <u>10,000,000</u> |
| | <u>\$ 38,500,000</u> | <u>\$ 55,000,000</u> |

Future payments are payable in each of the years as follows:

| | |
|------------|----------------------|
| 2010 | \$ 7,500,000 |
| 2011 | 5,500,000 |
| 2012 | 500,000 |
| 2013 | - |
| 2014 | 5,000,000 |
| Thereafter | <u>20,000,000</u> |
| | <u>\$ 38,500,000</u> |

10. Employee Retirement Benefit Plans

The Company's subsidiary has a Savings and Investment Plan Trust which covers all employees who have completed one year of service and 1,000 hours of service within the plan year. All employees of the Company on July 1, 1997 were immediately eligible to participate in the Plan. Subject to the limitations of the Internal Revenue Code, each eligible employee is allowed to contribute up to 15% of their annual compensation to the Plan. In addition, the Company may make a matching contribution equal to a discretionary percentage, as determined by management, of the participant's eligible salary. The contributions charged to operations amounted to \$0 in 2009 and 2008.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

10. Employee Retirement Benefit Plans (Cont.)

The Company has a stock incentive plan under which options to purchase up to 50,000 shares of AliKat Investments, Inc.'s common stock are granted to certain directors and employees. Options may be awarded over a period of time through the year ending 2009. The option price as determined by the Board of Directors may not be less than the fair value of the shares at the date of the grant, except for those options, which do not vest until such time when certain specified conditions are met within a seven and one-half year period, were granted at \$1.00 per share. All options expire ten years from date of grant. The following summarizes stock option activities for the years ended December 31, 2009 and 2008:

| | <u>\$25.00</u> <u>Per Share</u> | <u>\$35.00</u> <u>Per Share</u> | <u>\$41.00</u> <u>Per Share</u> | <u>\$61.00</u> <u>Per Share</u> | <u>\$70.00</u> <u>Per Share</u> | <u>\$82.00</u> <u>Per Share</u> | <u>\$98.00</u> <u>Per Share</u> | <u>\$115.00</u> <u>Per Share</u> | <u>Total</u> |
|------------------------------|------------------------------------|------------------------------------|------------------------------------|------------------------------------|------------------------------------|------------------------------------|------------------------------------|-------------------------------------|--------------|
| Balance at January 1, 2008 | 370 | 2,682 | 3,998 | 882 | 1,239 | 981 | 750 | 3,508 | 14,410 |
| Granted in 2008 | - | - | - | - | - | - | - | - | - |
| Exercised in 2008 | (170) | (2,322) | (890) | (686) | - | - | - | - | (4,068) |
| Cancelled in 2008 | (200) | - | - | - | - | - | - | - | (200) |
| Balance at December 31, 2008 | - | 360 | 3,108 | 196 | 1,239 | 981 | 750 | 3,508 | 10,142 |
| Granted in 2009 | - | - | - | - | - | - | - | - | - |
| Exercised in 2009 | - | - | - | - | - | - | - | - | - |
| Expired in 2009 | - | (120) | (125) | - | (118) | - | - | (125) | (488) |
| Balance at December 31, 2009 | <u>-</u> | <u>240</u> | <u>2,983</u> | <u>196</u> | <u>1,121</u> | <u>981</u> | <u>750</u> | <u>3,383</u> | <u>9,654</u> |

Aggregate value of AliKat Investments, Inc. stock at December 31, 2009 is \$67 per share.

As of December 31, 2009, 36,883 options have been exercised.

The Company has two Phantom Stock Appreciation Rights Plans. The two plans were established in January 2007 for the benefit of management personnel and employees. Under the 2007 Plans a combined total of 4,500 shares of common stock has been reserved. The following summarizes stock appreciation rights activities for the years ended December 31, 2009 and 2008:

| | <u>Plan A</u> | | | | <u>Plan B</u> | | | |
|----------------------------|---------------------------------|---------------------------------|---------------------------------|--------------|---------------------------------|---------------------------------|---------------------------------|--------------|
| | <u>\$83</u> <u>Per Share</u> | <u>\$84</u> <u>Per Share</u> | <u>\$91</u> <u>Per Share</u> | <u>Total</u> | <u>\$83</u> <u>Per Share</u> | <u>\$84</u> <u>Per Share</u> | <u>\$89</u> <u>Per Share</u> | <u>Total</u> |
| Balance, January 1, 2008 | 2,450 | - | - | 2,450 | 1,375 | - | 75 | 1,450 |
| Granted in 2008 | - | - | 400 | 400 | - | - | - | - |
| Expired in 2008 | - | - | - | - | - | - | - | - |
| Exercised in 2008 | - | - | - | - | - | - | - | - |
| Balance, December 31, 2008 | 2,450 | - | 400 | 2,850 | 1,375 | - | 75 | 1,450 |
| Granted in 2009 | - | 5,235 | - | 5,235 | - | 946 | - | 946 |
| Expired in 2009 | (700) | - | - | (700) | - | - | (75) | (75) |
| Exercised in 2009 | - | - | - | - | - | - | - | - |
| Balance, December 31, 2009 | <u>1,750</u> | <u>5,235</u> | <u>400</u> | <u>7,385</u> | <u>1,375</u> | <u>946</u> | <u>-</u> | <u>2,321</u> |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

10. Employee Retirement Benefit Plans (Cont.)

Plan A has a five-year vesting period and Plan B has a five-year vesting period and then additional benefits occur. As of December 31, 2009, no grants have been exercised.

The Company has nonqualified retirement plans (AliKat Investments, Inc. 401(k) Rabbi Trust and NorthSide Community Bank 401(k) Rabbi Trust) to permit certain directors and key officers to defer current compensation in order to provide retirement and other benefits for such individuals. A participant's deferral is fully vested at all times. The Plan is administered by an outside trustee appointed by the Board of Directors. Plan assets and the corresponding liability to plan participants are included in other assets and other liabilities in the accompanying consolidated balance sheets. Total deferred compensation accumulated under these plans at December 31, 2009 and 2008 amounted to \$4,355,182 and \$4,148,412, respectively.

11. Income Taxes

Income tax expense (benefit) is comprised of the following:

| | <u>2009</u> | <u>2008</u> |
|--|-----------------------|-------------------|
| Current income tax expense (benefit): | | |
| Federal | \$ (8,077,537) | \$ 1,271,662 |
| State | <u>11,170</u> | <u>289,481</u> |
| | <u>(8,066,367)</u> | <u>1,561,143</u> |
| Deferred income tax benefit (expense): | | |
| Federal | (618,186) | 659,046 |
| State | <u>1,705,052</u> | <u>154,741</u> |
| | <u>1,086,866</u> | <u>813,787</u> |
| Total income tax expense (benefit) | <u>\$ (9,153,233)</u> | <u>\$ 747,356</u> |

The reason for the difference between the actual income tax expense (benefit) and the amount computed at the applicable statutory federal tax rate of 34 percent follows:

| | <u>2009</u> | <u>2008</u> |
|---|-----------------------|-------------------|
| Federal income tax expense (benefit) at statutory rate | \$ (7,908,623) | \$ 543,758 |
| Nondeductible expenditures and other items | (9,879) | 12,541 |
| State income tax (benefit), net of federal income tax benefit | <u>(1,234,731)</u> | <u>191,057</u> |
| Income tax expense (benefit) | <u>\$ (9,153,233)</u> | <u>\$ 747,356</u> |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

11. Income Taxes (Cont.)

The deferred tax assets and liabilities are as follows:

| | <u>December 31,</u> | |
|--|---------------------|---------------------|
| | <u>2009</u> | <u>2008</u> |
| Deferred tax assets: | | |
| Deferred compensation | \$ 1,959,638 | \$ 1,980,985 |
| Loan loss deduction | 4,646,167 | 4,845,033 |
| Deferred loan origination fees | 24,797 | 96,710 |
| Depreciation | 173,830 | 92,554 |
| Nonaccrued interest | 233,073 | 830,645 |
| Other real estate owned | 24,482 | - |
| State net operating loss carryforward | 1,870,805 | - |
| Investment securities available-for-sale | <u>8,738</u> | <u>10,699</u> |
| | 8,941,530 | 7,856,626 |
| Deferred tax liability: | | |
| FHLB stock dividend | <u>192,981</u> | <u>192,981</u> |
| Net deferred tax assets | <u>\$ 8,748,549</u> | <u>\$ 7,663,645</u> |

The Company is no longer subject to federal or state income tax audits before the 2006 tax year.

12. Commitments, Contingent Liabilities and Credit Risk

Financial Instruments with Off-Balance-Sheet Risk - The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet financing needs of its customers. These financial instruments include commitments to extend credit and letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets.

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

At December 31, 2009 and 2008, financial instruments whose contract amounts represent credit risk were:

| | <u>2009</u> | <u>2008</u> |
|------------------------------|---------------|---------------|
| Commitments to extend credit | \$ 25,961,000 | \$ 38,120,000 |
| Letters of credit | 1,221,000 | 1,447,000 |

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. 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

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

12. Commitments, Contingent Liabilities and Credit Risk (Cont.)

Financial Instruments with Off-Balance-Sheet Risk (cont.) -

represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the counterparty. Collateral held varies but may include certificates of deposit, accounts receivable, inventory, property and equipment, income-producing commercial properties and real estate.

Letters of credit are conditional commitments issued by the Company to guarantee 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. The Company holds various types of collateral supporting those commitments. At December 31, 2009, those commitments were 100 percent collateralized.

Concentration of Credit Risk - The Company and the Bank make commercial, consumer and residential loans to their customers throughout northern Illinois. The majority of loans made are secured by specific collateral. Collateral held varies but may include deposits held in financial institutions; U.S. treasury securities; other marketable securities; income-producing commercial properties; accounts receivable; and property, plant and equipment.

Contingencies - Due to the nature of their business activities, the Company and the Bank are at times subject to legal action which arises in the normal course of business. In the opinion of management, the ultimate resolution of these matters is not expected to have a material effect on the financial position or results of operations of the Company or the Bank.

Interest Rate Risk - The Bank assumes interest rate risk (the risk that general interest rate levels will change) as a result of its normal operations. As a result, fair values of the Bank's financial instruments will change when interest rate levels change, and that change may be either favorable or unfavorable to the Bank. Management attempts to match maturities of assets and liabilities to the extent believed necessary to minimize interest rate risk. However, borrowers with fixed rate obligations are less likely to prepay in a rising rate environment and more likely to prepay in a falling rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by adjusting terms of new loans and deposits and by investing in securities with terms that mitigate the Bank's overall interest rate risk.

13. Restrictions on Dividends

The Company's primary source of cash is dividends received from the Bank. By regulation the Bank is restricted on the amount of dividends it can pay without prior regulatory approval. As a practical matter, dividends distributed by the Bank are restricted to amounts that allow the Bank to maintain prudent capital levels.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

14. Disclosures About Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practical to estimate that value:

Cash and Cash Equivalents - The carrying amounts of cash and short-term instruments approximate fair values.

Interest-Bearing Deposits in Banks - The carrying amounts of interest-bearing deposits maturing within ninety days approximate their fair values. Fair values of other interest-bearing deposits are estimated using discounted cash flow analyses based on current rates for similar types of deposits.

Investment Securities - For investment securities, 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. The carrying value of Federal Home Loan Bank and Federal Reserve Bank stock approximates fair value based on the redemption provisions of the Federal Home Loan Bank and Federal Reserve Bank.

Loans - The fair value of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

Deposits - The fair value of demand deposits, savings accounts, NOW and money market accounts 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.

Short-Term and Long-Term Borrowings - The fair value of short-term and long-term borrowings is estimated by discounting the future cash flows using the current interest rates at which similar borrowings could be made for the same maturities.

Commitments to Extend Credit and Letters of Credit - The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

14. Disclosures About Fair Value of Financial Instruments

The estimated carrying amount and fair value of the Company's financial instruments at December 31, 2009 is as follows:

| | <u>Carrying Amount</u> | <u>Fair Value</u> |
|--|----------------------------|-----------------------|
| Financial assets: | | |
| Cash and due from banks | \$ 3,298,647 | \$ 3,298,647 |
| Interest-bearing deposits with banks | 17,615,724 | 17,615,724 |
| Investment securities: | | |
| Available-for-sale | 701,829 | 701,829 |
| Held-to-maturity | 4,038,360 | 4,103,192 |
| Federal Home Loan Bank and Federal Reserve Bank stock | 2,778,350 | 2,778,350 |
| Loans | 433,343,111 | 422,943,280 |
| Less allowance for possible loan losses | (11,969,104) | - |
| Financial liabilities: | | |
| Deposits | 409,738,149 | 409,246,998 |
| Short-term borrowings | 9 | 9 |
| Long-term borrowings | 38,500,000 | 39,705,027 |
| Off-balance sheet items: | | |
| Commitments to extend credit | - | - |
| Letters of credit | - | - |

15. Fair Value Measurements

Financial Accounting Standards define fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. These standards also establish a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standards describe three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) or identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, and other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

15. Fair Value Measurements (Cont.)

The Company used the following methods and significant assumptions to estimate fair value:

Securities Available-for-Sale - Investment securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices for similar assets, if available. If quoted prices are not available, fair values are measured using matrix pricing models, or other model-based valuation techniques requiring observable inputs other than quoted prices such as yield curves, prepayment speeds, and default rates. Recurring Level 1 securities would include U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets. Recurring Level 2 securities include U.S. government agency securities, U.S. government sponsored agency securities, mortgage-backed securities, collateralized mortgage obligations and municipal bonds. Where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. Changes in fair market value are recorded in other comprehensive income as the securities are available for sale.

Impaired Loans - The Company does not record loans at fair value on a recurring basis. However, on occasion, a loan is considered impaired and an allowance for loan loss is established. A loan is considered impaired when it is probable that all of the principal and interest due under the original terms of the loan may not be collected. Once a loan is identified as individually impaired, management measures impairment. The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. In accordance with standards, impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3.

Other Real Estate Owned and Repossessed Assets - The Company does not record other real estate owned and repossessed assets at fair value on a recurring basis. Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at the lower of the carrying amount or fair value less cost to sell. When the fair value is estimated based on an observable market price or current appraised value, the Company records the asset as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the asset is further impaired below the appraised value and there is no observable market price, the Company records the asset as nonrecurring Level 3.

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

15. Fair Value Measurements (Cont.)

Fair values of assets and liabilities measured on a recurring basis at December 31, 2009 and 2008 are as follows:

| | Fair Value | Fair Value Measurements at Reporting Date Using | | |
|-------------------------------|------------|---|---|--|
| | | Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| December 31, 2009: | | | | |
| Securities available-for-sale | \$ 701,829 | \$ - | \$ 701,829 | \$ - |
| December 31, 2008: | | | | |
| Securities available-for-sale | \$ 673,039 | \$ - | \$ 673,039 | \$ - |

Fair values of assets and liabilities measured on a nonrecurring basis at December 31, 2009 and 2008 are as follows:

| | Fair Value | Fair Value Measurements Using | | | |
|---|---------------|---|---|--|----------------------------|
| | | Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total Gains (Losses) |
| December 31, 2009: | | | | | |
| Impaired loans | \$ 20,475,626 | \$ - | \$ 20,475,626 | \$ - | \$ (182,673) |
| Other real estate owned and repossessed assets | 16,125,239 | - | 16,125,239 | - | <u>(459,781)</u> |
| | | | | | <u>\$ (642,454)</u> |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

15. Fair Value Measurements (Cont.)

The following represent impairment charges recognized during the period.

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral-dependent loans, had a carrying amount of \$22,691,999, with a valuation allowance of \$2,216,373, resulting in an allocation of loan losses of \$182,673 for the period.

Other real estate owned and repossessed assets, which are valued using the fair value less costs to sell, had a carrying amount of \$16,585,020. The carrying amount of the assets were written down to their fair value of \$16,125,239, resulting in a loss of \$459,781, which was charged to earnings for the year.

16. Parent Company Statements

Presented below are the balance sheets and the statements of income and cash flows for the Parent Company:

BALANCE SHEETS

ASSETS

| | December 31, | |
|--|---------------|---------------|
| | 2009 | 2008 |
| Cash | \$ 277,885 | \$ 70,477 |
| Investment in subsidiary | 58,152,567 | 76,541,336 |
| Investment security available-for-sale | 75,000 | 75,000 |
| Investment in Alikat Capital Trusts | 620,000 | 620,000 |
| Other assets | 1,331,330 | 1,331,330 |
| Total assets | \$ 60,456,782 | \$ 78,638,143 |

LIABILITIES AND SHAREHOLDERS' EQUITY

| | | |
|--|---------------|---------------|
| Other liabilities | \$ 1,638,637 | \$ 959,047 |
| Long-term debt | 20,620,000 | 25,620,000 |
| Total liabilities | 22,258,637 | 26,579,047 |
| Shareholders' equity | 38,198,145 | 52,059,096 |
| Total liabilities and shareholders' equity | \$ 60,456,782 | \$ 78,638,143 |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

16. Parent Company Statements (Cont.)

STATEMENTS OF OPERATIONS

| | For the Year Ended December 31, | |
|---|------------------------------------|--------------|
| | 2009 | 2008 |
| Operating income: | | |
| Dividend income from subsidiary | \$ 5,625,388 | \$ 3,083,785 |
| Interest income | 3,878 | 4,061 |
| Total operating income | 5,629,266 | 3,087,846 |
| Operating expense: | | |
| Interest expense | 1,304,978 | 1,433,785 |
| Other | 39,851 | 34,190 |
| Total operating expense | 1,344,829 | 1,467,975 |
| Income before equity in undistributed income of subsidiary | 4,284,437 | 1,619,871 |
| Dividend in excess of income of subsidiary | (18,391,861) | (767,939) |
| Income (loss) before income taxes | (14,107,424) | 851,932 |
| Applicable income tax expense | - | - |
| Net income (loss) | \$ (14,107,424) | \$ 851,932 |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

16. Parent Company Statements (Cont.)

STATEMENTS OF CASH FLOWS

| | For the Year Ended December 31, | |
|---|------------------------------------|--------------|
| | 2009 | 2008 |
| Cash flows from operating activities: | | |
| Net income (loss) | \$(14,107,424) | \$ 851,932 |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | |
| Increase (decrease) in other liabilities | 679,590 | (24,600) |
| Dividend in excess of income of subsidiary | 18,391,861 | 767,939 |
| Net cash provided by operating activities | 4,964,027 | 1,595,271 |
| Cash flows from financing activities: | | |
| Payment of long-term debt | (5,000,000) | - |
| Proceeds from issuance of stock | 243,381 | 840,091 |
| Company stock acquired and retired | - | (2,555,614) |
| Dividend paid | - | (204,915) |
| Net cash provided by (used in) financing activities | (4,756,619) | (1,920,438) |
| Net increase (decrease) in cash | 207,408 | (325,167) |
| Cash at beginning of year | 70,477 | 395,644 |
| Cash at end of year | \$ 277,885 | \$ 70,477 |
| <u>Supplemental disclosures of cash flow information:</u> | | |
| Cash payment for interest on borrowings | \$ 625,388 | \$ 1,433,785 |
| <u>Supplemental schedule of noncash investing and financing activities:</u> | | |
| Net unrealized gain from subsidiary's available-for-sale securities | \$ 3,092 | \$ 143 |

ALIKAT INVESTMENTS, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

17. Regulatory Matters

The Company is subject to various regulatory capital requirements administered by federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company must meet specific capital guidelines that involve quantitative measures of the Company's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Company'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 regulation to ensure capital adequacy require the Company to maintain minimum amounts and ratios (set forth in the table below) of total capital and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and Tier 1 capital (as defined) to adjusted total assets (as defined). Management believes, as of December 31, 2009, that the Company meets all capital adequacy requirements to which it is subject.

As of December 31, 2009, the most recent notification from the Federal Reserve Bank categorized the Company as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized the Company must maintain total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the Company's category.

The Company's 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 |
| As of December 31, 2009: | | | | | | |
| Total Capital | | | | | | |
| (to Risk-Weighted Assets) | \$ 62,078,000 | 13.7% | \$ 36,310,000 | 8.0% | \$ 45,387,000 | 10.0% |
| Tier 1 Capital | | | | | | |
| (to Risk-Weighted Assets) | 49,058,000 | 10.8% | 18,155,000 | 4.0% | 27,232,000 | 6.0% |
| Tier 1 Capital | | | | | | |
| (to Adjusted Total Assets) | 49,058,000 | 9.9% | 19,813,000 | 4.0% | 24,767,000 | 5.0% |
| As of December 31, 2008: | | | | | | |
| Total Capital | | | | | | |
| (to Risk-Weighted Assets) | \$ 78,563,000 | 15.3% | \$ 41,147,000 | 8.0% | \$ 51,434,000 | 10.0% |
| Tier 1 Capital | | | | | | |
| (to Risk-Weighted Assets) | 69,410,000 | 13.5% | 20,574,000 | 4.0% | 30,860,000 | 6.0% |
| Tier 1 Capital | | | | | | |
| (to Adjusted Total Assets) | 69,410,000 | 12.6% | 22,094,000 | 4.0% | 27,617,000 | 5.0% |