

2012 ANNUAL REPORT

Everything we do is centered around you.



Central Bank & Trust Co.
Central Bank of Jefferson County
Central Insurance Services
Central Investment Center, Inc.

 **Central Bancshares, Inc.**
Showing you the way.

The mission of Central Bancshares is to be a high-performance financial services company that delivers superior service and value to each customer we serve. We will emphasize employee and customer satisfaction – always mindful that quality people will make the Central difference.

2012 ANNUAL REPORT

CONTENTS

Financial Highlights.....	1
Letter to Employees, Shareholders, Customers and Communities.....	2
Management's Discussion and Analysis	5
Independent Auditor's Report.....	12
Consolidated Balance Sheets.....	13
Consolidated Statements of Income.....	14
Consolidated Statements of Cash Flows.....	15
Consolidated Statements of Changes in Shareholders' Equity.....	16
Consolidated Statements of Comprehensive Income.....	16
Notes to Consolidated Financial Statements.....	16
Boards of Directors.....	43
Officers.....	45
Central Bancshares Locations.....	48
In Memoriam.....	49

For additional copies or information, visit centralbank.com or contact:

Stephen C. Kelly

Central Bank

300 West Vine Street

Lexington, Kentucky 40507

(859) 253-6201

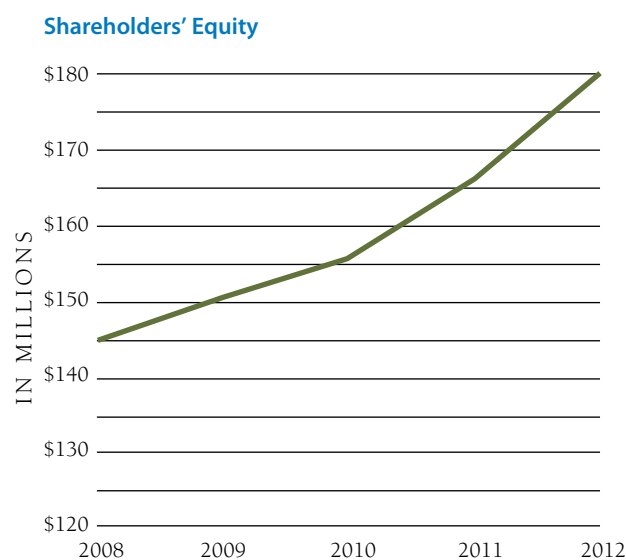
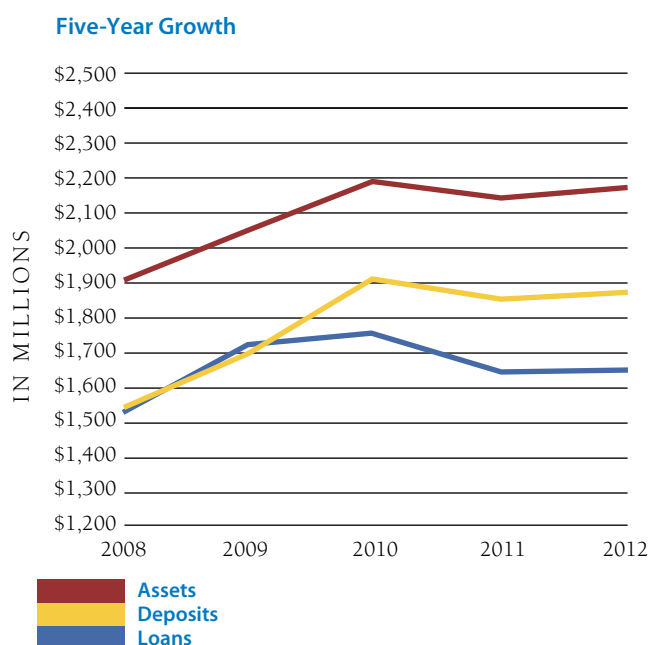
E-mail: skelly@centralbank.com



FINANCIAL HIGHLIGHTS

For twelve months ended December 31

	2012	2011	2010	2009	2008
Results of Operations:					
Net income	\$ 12,880,646	\$ 11,017,235	\$ 6,907,543	\$ 1,768,610	\$ 9,200,145
Net income per share	37.02	31.67	19.85	5.08	26.44
Cash dividends per share	0.00	0.00	0.00	5.00	9.00
Book value per share at year end	518.24	479.72	449.08	433.94	416.03
At December 31					
Assets	\$ 2,175,446,603	\$ 2,145,011,752	\$ 2,192,013,038	\$ 2,053,106,110	\$ 1,910,399,779
Earning assets	2,000,062,125	1,956,857,364	2,019,276,028	1,863,911,997	1,729,851,957
Net loans and leases	1,645,063,290	1,644,350,387	1,747,181,237	1,717,017,748	1,536,559,682
Deposits	1,876,715,151	1,858,076,694	1,903,788,824	1,705,582,952	1,540,141,181
Shareholders' equity	180,307,914	166,906,431	156,243,656	150,978,513	144,747,709
Averages					
Assets	\$ 2,142,605,932	\$ 2,131,379,954	\$ 2,145,488,233	\$ 1,964,115,041	\$ 1,818,243,648
Earning assets	1,970,266,865	1,954,372,859	1,963,138,178	1,793,440,419	1,649,263,780
Net loans and leases	1,626,097,871	1,683,941,150	1,732,507,700	1,602,265,904	1,467,592,067
Deposits	1,852,678,210	1,847,549,623	1,812,588,595	1,623,195,705	1,456,101,126
Shareholders' equity	174,441,375	162,532,252	155,348,975	146,626,780	149,598,387
Performance Ratios:					
Return on average assets	0.60%	0.52%	0.32%	0.09%	0.51%
Return on average shareholders' equity	7.38%	6.78%	4.45%	1.21%	6.15%
Average shareholders' equity					
to average assets	8.14%	7.63%	7.24%	7.47%	8.23%
Dividend payout ratio	0.00%	0.00%	0.00%	98.36%	34.04%
Net charge-offs to average					
loans and leases	0.81%	0.60%	0.93%	0.66%	0.44%
Allowance for credit losses as a percentage					
of year end loans and leases	1.64%	1.72%	1.29%	1.19%	1.40%
Net interest margin (tax equivalent)	3.74%	3.97%	3.85%	3.58%	3.75%



Central Bank is on the move!

Supported by six decades of strength, stability and service to our communities, Central Bank is poised to continue its progress and help our customers, shareholders and communities. Today, the economy is showing some signs of a recovery. If we continue to emphasize service and leadership to forge strong relationships, we can help our customers meet the challenges of the new economy.

We are strengthening our “community banking brand” by delivering a wide array of banking and income-generating services. Those efforts are expanding our customer base and adding new relationships in our markets across the Commonwealth. During a time when the economy has slowed the growth of traditional loan and deposit business, these other lines of business have produced new opportunities for our Company. We are pursuing a multiyear strategy to diversify our balance sheet by focusing on core deposits and relationship-based lending to support growth and prosperity within our Kentucky markets. At the same time, we are strengthening earnings by developing a growing emphasis on income strategies that include insurance, wealth management, mortgage origination and investment services.

Our customers are responding to these initiatives and to the leadership shown by our team of Central Bankers who are delivering truly outstanding service. Again in 2012, our independent measurements of banking service quality place Central Bank at or near the top. We continue to stress service as the key competitive advantage that will sustain our bank through all types of economic conditions and will help us achieve superior financial performance in the days to come.

Financial performance continued to improve in 2012.

2012 Performance

These financial highlights for the Company include Central Bank & Trust Co. and its subsidiaries, Central Investment Center, Inc. and Central Insurance Services; Central Bank of Jefferson County; and Salt Lick Deposit Bank (which was acquired by Peoples Bank of Kentucky on January 1, 2013). We have provided a detailed discussion of our financial results in the Management’s Discussion and Analysis beginning on page 5.

- Net income rose 16.9 percent to \$12,880,646 or \$37.02 per share. For 2011 the result was \$11,017,235 or \$31.67 per share.
- Return on average assets of \$2.14 billion improved to .60 percent from .52 percent in 2011.
- Deposit growth was modest, ending the year with an increase of one percent, \$1.88 billion.
- Loan opportunities were somewhat limited, ending the year at \$1.65 billion, the same level as in 2011.
- Shareholders’ equity grew to \$180.3 million, up \$13.4 million or 8.03 percent.

These results provide a solid basis for future earnings when the credit cycle and economic conditions return to more traditional levels.

Serving our Customers and Communities

Economic recovery is proceeding slowly in Kentucky, and our customers are still cautious about their spending and savings habits. We were extremely encouraged by the strength of the mortgage industry that is leading the way to a more robust economy. Home sales are climbing, along with housing prices, and consumers are using low-interest rates to refinance existing mortgage loans at an unprecedented pace. Our mortgage lending and loan services staff has worked tirelessly to meet those demands while delivering excellent service. In addition, we are encouraged by the acceptance of our new Affordable Housing Loan that serves low-and-moderate-income families in our markets.

Customers have responded to the trusted advisors they know, and our employees have been a tremendous source of strength amid a troubled market. As a result, we used targeted growth strategies to attract and retain core deposits.

With interest rates at historically low levels, our customer relationships and service focus on customer needs were valuable assets. The Bank’s exclusive corporate partnership as the “Official Bank of UK Athletics” continues to expand brand and service awareness, emphasizing insurance, mortgage and wealth management services in 2012.

Deposit gathering entered a new phase with the launch of online deposit accounts. We have expanded our reach

beyond our established markets into the surrounding states. In the months to come, we expect the online channel to serve as a consistent source of new deposits and a convenient way for existing customers to expand their relationships. Other Internet channels, including online and mobile banking, are growing in popularity with convenient access and control of personal and small business finances.

Throughout our existence, our Company has been a driving force for economic development. We are very proud to be providing the lending needed to support growth by individuals and businesses across the state. Despite media reports that “banks were not lending,” we supported our customers and promoted economic development throughout the year. Our lenders assisted a broad range of customers in diverse industries and business segments. Likewise, we moved to serve more of those business customers’ needs with corporate cash management, remote deposit and credit card services.

Other opportunities were created by our financial service professionals who provide private banking, wealth management, insurance and investment services. Our Wealth Management team had a remarkable year, based on its ability to provide a single source of service for people and companies with sophisticated needs. Those customer relationships will serve as a solid foundation for future growth across a wide spectrum of financial services.

Community Sponsorships

Dedicated community service is a vital element for community banks, and it’s the foundation on which we have built our franchise. Our sponsorships and charitable giving supported numerous organizations in the Commonwealth, including American Cancer Society Relay for Life, American Heart Association, Big Brothers/Big Sisters, Bluegrass Tomorrow, Children’s Charities of the Bluegrass, Commerce Lexington, Community Action Council, Downtown Lexington Corporation, Everfi Financial Literacy Program, Greater Louisville Inc., God’s Pantry, Headley-Whitney Museum, Hospice, Junior Achievement, Kentucky Chamber of Commerce, Kincaid Foundation, LexArts, REACH low-income housing program, University of Kentucky,

Kentucky Children’s Hospital, Sanders Brown Center, Tubby’s Klubhouse, United Way, Urban League and YMCA Black Achievers, along with other excellent charitable and civic organizations serving a wide range of our citizens.

Beyond financial investments, our officers and employees are providing leadership and service through their participation on community, charitable and civic boards. Each year the Company recognizes staff members in all markets for Community Service leadership as a means to express its appreciation for their tireless efforts. Our community involvement is a major force in our ability to attract and retain the best talent, which allows Central Bank to have been honored among the Best Places to Work in Kentucky for eight consecutive years.

Looking forward to 2013

Central Bank is well-positioned to continue building market share and expanding our reach in the markets we serve. We are challenging our staff to consider best practices that enhance our business processes while improving revenues and reducing expenses. We believe that credit quality is improving which will allow for reduced credit costs in 2013. We plan to focus on commercial loans to qualified business segments and consumer loans on an expanded basis. While we still face significant challenges in the sluggish economy, intense competition and excessive regulation, we believe that moderate growth opportunities still exist.

Our staff members have been constant sources of pride as they strive to provide our markets’ best service. Their experience and expertise are tremendous resources for our Company, our customers and our markets. We continue to invest in training and education to ensure that our advantage endures and that qualified employees are available in every area.

The banking center network is a tremendous resource for gathering and serving customers. Although we are not expanding brick and mortar facilities, we will continue to explore online channels that serve customers when and where they choose. Response to those initiatives has been very encouraging, and we expect further progress to come as we are able to offer expanded transaction capabilities.

Honored for Years of Service

Two Central Bankers retired in 2012 after serving our company with dedication and distinction. I want to offer my sincere appreciation to Olivia Davis, Client Services, and Doug Fritz, Vice President, Wealth Management, who completed their employment with Central Bank & Trust Co. at yearend. We appreciate their long years of support and will miss their leadership and wisdom as vital members of our team.

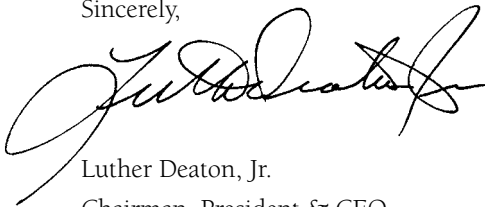
With Appreciation

I appreciate the support and guidance of our directors during the period of economic uncertainty. Their experience and leadership provide an excellent resource and an insightful connection to our local markets. We were deeply saddened by the loss of Board Member Richard Furst, who made tremendous contributions to our success and was a constant source of inspiration and wise counsel. A tribute to him is provided in this report.

It is an honor to serve with our team of dedicated Central Bankers whose energy and enthusiastic service are the cornerstones of our success. I am also thankful for the loyalty of our customers, many of whom have enjoyed relationships with us spanning several decades.

Even though the economy has yet to provide a clear picture of its future direction, Central Bank is well-positioned for the challenges we face. We believe our community banking brand provides the best solutions for the wide variety of business and consumer needs we are in a position to serve. Our commitment to our shareholders, customers and communities is unwavering, for I believe our best days are coming in the years ahead.

Sincerely,



Luther Deaton, Jr.
Chairman, President & CEO
March 15, 2013



“Central Bank is well-positioned to continue building market share and expanding our reach in the markets we serve.”

Central Bancshares, Inc. (the "Company"), a bank holding company located in Lexington, Kentucky, is the parent company of Central Bank & Trust Co.; Central Bank of Jefferson County, Inc.; and Salt Lick Deposit Bank. At December 31, 2012 the Company had 28 full-service banking centers located in Bath, Boone, Clark, Fayette, Jefferson, Jessamine, Kenton, Madison and Scott counties, a full-service brokerage business and a full-service insurance agency. Effective January 1, 2013, the Company sold Salt Lick Deposit Bank. All assets of Salt Lick Deposit Bank were sold, including the two banking centers located in Bath County.

Results of Operations

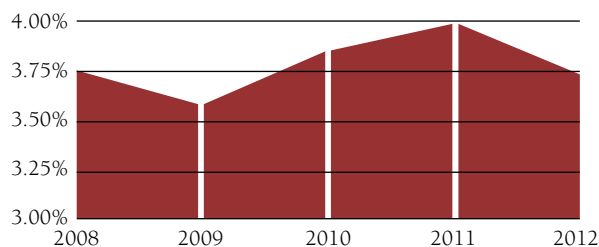
The Company reported net income of \$12,880,646 for 2012, or \$37.02 per share. This compares to \$11,017,235, or \$31.67 per share for 2011, and \$6,907,543, or \$19.85 per share for 2010. During 2012 both the national and local economies showed signs of recovery, and the Company experienced some improvement in terms of real estate foreclosures and past due loans. However, the need to continue working with clients previously impacted by the slow economy continued. During 2012 we had \$7.5 million of additions to foreclosed real estate and experienced net charge-offs on outstanding loans of \$13.5 million. This is a decline of \$3.3 million in additions to foreclosed assets, but an increase of \$3.2 million in net charge-offs. We were also able to dispose of \$9.3 million of real estate assets we had previously foreclosed on. All this activity in other real estate plus market valuation adjustments left us with a net balance of foreclosed real estate assets held at December 31, 2012, of \$21.0 million, a decline of \$4.7 million from December 31, 2011. A full discussion of the performance of the loan portfolio is presented later in this document.

Return on average equity was 7.38 percent and return on average assets was 0.60 percent for 2012, compared with 6.78 percent and 0.52 percent, and 4.45 percent and 0.32 percent, respectively, for 2011 and 2010.

Net Interest Income

Net interest income in 2012 was \$72.5 million compared to \$75.8 million in 2011, a decrease in 2012 of 4.40 percent. The net interest rate spread is the difference between the tax equivalent average rate of interest earned on average earning assets and the average rate of interest expense on average interest bearing liabilities. The net interest margin is the tax equivalent net interest income divided by average earning assets. For computational purposes, non-accrual loans are included in earning assets. On average the net interest spread decreased

Net Interest Margin



22 basis points during 2012, to 3.53 percent, while the net interest margin declined 23 basis points to 3.74 percent for 2012. Every basis point of deterioration in the net interest margin equates to approximately \$200,000 per year in income.

During 2011, the tax equivalent yield on earning assets averaged 4.95 percent; the yield on earning assets averaged 4.51 percent in 2012. Weakness in the economy was demonstrated through lackluster loan demand. With the weak loan demand came increased competition between qualified lenders, causing the interest rates on credit products to decline. The Company was able to control the attrition of its loan portfolio to only 3.12 percent, but saw the tax equivalent yield on those outstanding loans decline from 5.59 percent in 2011 to 5.32 percent in 2012. The increased competition for loans was the primary cause for the reduction in yield on the portfolio.

The investment portfolio averaged \$270.4 million for 2011, and had an average tax equivalent yield of 0.89 percent. The investment portfolio averaged \$344.2 million for 2012, and had an average tax equivalent yield of 0.65 percent. The yield curve was very flat for most of 2012, and the Company held a larger percentage of its assets in very liquid overnight investments as compared to 2011. Management is seeking to find the appropriate balance between the safety of the increased liquidity, and the interest rate risk required to earn a higher yield on the investment portfolio.

While the average yield on earning assets declined 44 basis points from 2011 to 2012, the cost of paying liabilities declined 22 basis points over the same period. Weak loan demand, coupled with increased availability of deposits, led to less competitive pressures in pricing deposits, and made management more reluctant to pay higher prices to attract new deposits. The Company was able to lower its cost on interest bearing deposit accounts from an average of 1.08 percent in 2011 to 0.83 percent in 2012. While there may still be some room left for improvement in the net interest margin from lowering deposit rates, the opportunities for improvement are much less in 2013.

Gross loans outstanding averaged \$1.66 billion for 2012,

decreasing \$53.3 million, or 3.12 percent on average from 2011. The Company was able to increase average deposits by a mere \$5.1 million or 0.28 percent during 2012. Deposits averaged \$1.85 billion during 2012.

The Company averaged a loan to deposit ratio of 89.40 percent during 2012, a decrease of 313 basis points from the 2011 percentage of 92.53 percent. This is the fourth year in a row that the Company's average loan to deposit ratio has declined. Liquidity was a primary emphasis of many financial institutions and bank regulatory agencies during 2012. This reduction in the loan to deposit ratio is a positive reflection of management's attention to liquidity management, and part of an overall strategy to control growth on the balance sheet to improve the Company's capital ratios. However, management is also keenly aware of the tradeoff between liquidity and earnings, and is striving to maintain an appropriate balance.

In March 2009, the Company issued \$22.6 million in Trust Preferred Securities with a fixed rate of interest of 10 percent. The Company still has \$15 million in Trust Preferred Securities outstanding from a previous issue, which have a variable rate of interest equal to the sum of the three month London Interbank Offered Rate (LIBOR) and 1.75 percent, which was 2.06 percent at year end 2012. Interest expense associated with these two debt issues totaled \$2.6 million for 2012, an average rate of 7.05 percent.

The table below reflects the changes in net interest income in 2012 and 2011 due to changes in rates and volumes computed on a tax equivalent basis for all interest-sensitive categories.

Non-Interest Income

Generation of non-interest income has traditionally been a strength of the Company's financial performance, as it was in 2012. Fee income totaled \$36.2 million for 2012, an increase of \$2.1 million, or 6.14 percent over fee income generated in 2011. Management considers this a significant achievement in the Company's financial performance for 2012 considering the adverse impact of consumer protection legislation and other recent regulatory changes on the Company's ability to generate fee income from our traditional sources.

The Company generated \$4.8 million in fees from its trust services during 2012, an increase of \$459,000 from 2011, or 10.49 percent. At year end 2012, total assets under management in the Trust Department stood at \$1.0 billion, an increase of \$96.8 million over December 31, 2011. Personnel in the Trust Department generated \$80.3 million in asset growth from business development efforts, with the remaining \$16.5 million in growth in assets coming from asset appreciation.

Service charges on deposit accounts decreased 12.29 percent, or \$1.3 million during 2012 compared to 2011. The Company's

TAXABLE EQUIVALENT RATE/VOLUME ANALYSIS

(In Thousands)

	Net Change	2012/2011 Increase/Decrease Due To		Net Change	2011/2010 Increase/Decrease Due To	
		Rate	Volume		Rate	Volume
Interest income						
Loans	\$ (7,077)	\$ (4,105)	\$ (2,972)	\$ (4,936)	\$ (2,377)	\$ (2,559)
Investments						
Taxable	(33)	(514)	481	125	(214)	339
Tax exempt	(142)	33	(175)	(114)	128	(242)
Federal funds sold	81	(19)	100	73	23	50
Total interest income	(7,171)	(4,605)	(2,566)	(4,852)	(2,440)	(2,412)
Interest expense						
Deposits						
NOW accounts	(30)	(71)	41	(538)	(484)	(54)
Savings deposits	(9)	(24)	15	(48)	(57)	9
Money market deposits	(311)	(504)	193	(1,815)	(1,891)	76
Time deposits	(3,476)	(1,863)	(1,613)	(3,577)	(3,343)	(234)
Borrowed funds	(12)	162	(174)	(940)	592	(1,532)
Total interest expense	(3,838)	(2,300)	(1,539)	(6,918)	(5,183)	(1,735)
Net interest income	\$ (3,333)	\$ (2,304)	\$ (1,028)	\$ 2,066	\$ 2,743	\$ (677)

Courtesy Coverage product permits a personal transaction account which is maintained in good standing to be overdrawn up to \$800 for the normal insufficient funds check charge. Net revenue of \$6.5 million was generated during 2012 from this product, a decrease of \$1.2 million, or 15.95 percent from 2011. The FDIC issued guidance in late 2010 on how banks are to manage their automated overdraft protection programs. This guidance includes specific instructions on the posting order of items, required counseling with customers who are frequent users of the service, and other specific steps a bank must take to ensure that it is not maximizing fees generated from this product. Management carefully implemented this new guidance in August 2011. It appears that implementation of this guidance has had a negative impact upon income generated from insufficient funds charges. Management recognizes that this product will continue to generate significant income for the Company for years to come, but it is a mature product that is not likely to show significant growth without some change in the regulatory environment, or an increase in the base fee.

Loans originated for sale during 2012 totaled \$286.2 million. At the end of 2012, the Company serviced \$55.6 million in loans for Fannie Mae and Freddie Mac. Approximately 3.78 percent of the loans originated for sale during 2012 were sold service retained.

During 2012 the Company sold \$275.4 million in mortgage loans, service released. The interest rate on all loans originated for sale is locked with the buyer and the investor, thus the Company has no interest rate risk associated with these transactions. During 2012 the Company generated \$6.1 million in income from loans sold in the secondary market, an increase of \$3.0 million from 2011, or nearly doubling income from the previous year. While activity in the housing market continues to be depressed, lower interest rates have provided an opportunity for homeowners to refinance. The Mortgage Bankers Association is predicting that mortgage originations in 2013 will decline 20 percent from 2012 levels.

Two residual impacts of the recent economic difficulties are higher levels of past due loans than the Company's normal experience, and higher levels of foreclosed assets consisting primarily of foreclosed real estate. Other real estate owned is property that has been foreclosed upon, or has been taken back in lieu of payment of customer debt. On December 31, 2012, the Company held \$20.1 million in other real estate. Other real estate is recorded at estimated fair market value, less estimated costs to sell the properties. During 2012, the Company either realized losses on the disposal of pieces of other real estate or recorded unrealized losses on properties in establishing valuation reserves in the amount of \$2.9 million, which is roughly equal to the losses experienced in 2011. Despite the fact that the loss experience was roughly equal between 2011 and 2012, management did detect an improvement in the real estate market as more pieces of real estate were sold, and more of those sold at a value close to their appraised value in 2012 than in 2011. Particularly the market for mid priced residential real estate improved; several pieces of property in this price range were sold in 2012. Management is comfortable that the other real estate portfolio is properly recorded at its estimated fair value as of December 31, 2012, but is also aware that in the current economic conditions it is probable that some of these values may continue to decline. The Company is aggressively marketing these properties.

Non-Interest Expense

Non-interest expense for 2012 totaled \$83.6 million, a slight increase of \$263,000, or 0.32 percent from 2011. Several years ago the Company implemented strategies to help control operating expense. In the last three years, the Company has experienced modest growth in operating expenses, less than 2.50 percent per year, despite increased expenses relating to loan collection efforts.

Salaries and benefits are the largest component of non-interest

ANALYSIS OF NON-INTEREST INCOME

	2012	2011	2010	2012/2011		2011/2010	
				CHANGE	%	CHANGE	%
Trust income	\$ 4,837,557	\$ 4,378,124	\$ 3,671,734	\$ 459,433	10.49%	\$ 706,390	19.24%
Service charges on deposit accounts	9,630,467	10,979,706	11,501,419	(1,349,239)	(12.29)%	(521,713)	(4.54)%
Fees on mortgage loan sales and servicing	6,060,758	3,069,097	4,102,469	2,991,661	97.48%	(1,033,372)	(25.19)%
Service charges on revolving credit	4,628,351	4,536,534	3,641,707	91,817	2.02%	894,827	24.57%
Electronic banking fees	4,516,806	4,435,543	4,152,733	81,263	1.83%	282,810	6.81%
Loss or valuation allowances for ORE	(2,853,228)	(2,812,082)	(4,874,879)	(41,146)	1.46%	2,062,797	(42.31)%
Other income	9,342,152	9,485,479	7,769,324	(143,327)	(1.51)%	1,716,155	22.09%
Total non-interest income	\$36,162,863	\$34,072,401	\$29,964,507	\$ 2,090,462	6.14%	\$ 4,107,894	13.71%

expense, totaling \$38.2 million, an increase of \$210,000, or 0.55 percent from 2011. On December 31, 2012, the Company employed 478 full-time equivalent employees compared to 479 full-time equivalent employees at the same date in 2011.

Expenses related to loan collection efforts including legal fees and costs associated with other real estate owned have been unusually high for the past several years. During 2012 legal fees and expenses associated with other real estate owned totaled \$4.1 million. This is a decline of \$763,000, or 15.59 percent from 2011. This is still an unusually high level for these expenses, but management feels that the declining number of properties held, coupled with slowly improving economic conditions, will result in further declines in these expenses in 2013.

Federal Income Tax

The Company had a negative provision for federal income tax of \$55,000 during 2012. The Company's tax planning strategy includes the purchase of municipal securities to increase tax exempt income, and participation in Industrial Revenue Bond lending for non-profit organizations. The Company is also a limited partner in 16 low-income housing projects and two historic renovation projects for which it receives tax credits and is an investor in two Community Development Entities for which it receives New Market Tax Credits. It is the culmination of these various tax exempt income investing activities which generated tax savings and credits in excess of the liability from taxable income.

Management is closely monitoring the Company's income tax position to ensure that it will be able to take advantage of all of its deferred tax assets. The possibility of repositioning the Company's long-term tax planning strategy is under current review. At this time management feels that the deferred tax assets recorded on the Company's books are not impaired.

Financial Condition

On December 31, 2012, total assets of the Company were \$2.18 billion. The Company's assets increased \$30.4 million, or 1.42 percent, from assets at December 31, 2011. During 2012, management continued a strategy of controlled attrition/limited growth in order to strengthen the Company's capital ratios. Earning assets totaled \$2.0 billion on December 31, 2012, or 91.94 percent of total assets. The Company's investment portfolio, including federal funds sold and money market investments, increased \$42.5 million, while its gross loans and leases, including loans held for sale, remained relatively unchanged, with a slight decline of \$590,000 or 0.04 percent.

Earning Assets

Gross loans outstanding totaled \$1.67 billion on December 31, 2012. Loan demand in all areas remained lackluster, at best, during 2012. While the Company did experience a modest increase in Commercial and Mortgage Loans, the Consumer Loan Portfolios declined. Competitive pressures on installment lending, particularly for loans secured by automobiles, produced a rate environment that management did not find attractive. As a result, the Company saw a decline in outstanding installment loans of \$21.9 million or 20.31 percent. We also saw a small decline in Equity Line loans of \$5.1 million, or 4.55 percent.

The Company is mindful of the importance of managing exposure to credit risk. This is accomplished through diversification of the loan portfolio, not only by loan type, but by industry and customer. Diversification by industry and geographic region within the Company's loan portfolio helps to maintain acceptable credit risk exposure. Concentrations of credit are monitored on a monthly basis for compliance with internal and external policies. As a result, there is no undue concentration in any single sector.

ANALYSIS OF NON-INTEREST EXPENSE

	2012	2011	2010	2012/2011		2011/2010	
				CHANGE	%	CHANGE	%
Salaries and benefits	\$ 38,184,558	\$ 37,975,052	\$ 36,184,885	\$ 209,506	0.55%	\$ 1,790,167	4.95%
Occupancy	11,624,372	11,192,099	11,110,995	432,273	3.86%	81,104	0.73%
Furniture and equipment expense	5,584,395	5,797,892	5,928,123	(213,497)	(3.68)%	(130,231)	(2.20)%
Advertising and business development	4,113,871	3,755,161	4,086,753	358,710	9.55%	(331,592)	(8.11)%
Professional services	2,523,676	2,602,890	3,454,486	(79,214)	(3.04)%	(851,596)	(24.65)%
FDIC insurance expense	1,889,628	2,303,052	3,491,092	(413,424)	(17.95)%	(1,188,040)	(34.03)%
Other non-interest expense	19,711,207	19,742,610	17,380,693	(31,403)	(0.16)%	2,361,917	13.59%
Total non-interest expense	\$ 83,631,707	\$ 83,368,756	\$ 81,637,027	\$ 262,951	0.32%	\$ 1,731,729	2.12%

Management has always viewed the investment portfolio as a means by which interest rate risk and liquidity are managed. Management noted that bank examinations and regulatory comments have an increased emphasis regarding on-balance-sheet liquidity. That emphasis, coupled with a very flat yield curve and some asset liability pressure to match immediately repricing deposit liabilities, prompted management to leave a larger than normal percentage of available cash in overnight deposits with the Federal Reserve. On December 31, 2012, the Company was selling \$174.4 million to the Federal Reserve as an overnight investment. On average, this balance was \$178.5 million for 2012. Management continues to look for opportunities to invest in very short term securities that would yield more than the 25 basis points we earn on the overnight funds. For the most part, management is looking for short-term government securities with a maturity of two years or less, and variable rate securities to purchase. Any of these purchased will be classified as available for sale.

Allowance for Credit Losses

At December 31, 2012, the allowance for credit losses was \$27.5 million, or 1.64 percent of gross loans outstanding, compared with \$28.8 million, or 1.72 percent, at December 31, 2011. Net credit losses for 2012 totaled \$13.5 million, or 0.81 percent of gross average outstanding loans and leases. The provision for credit losses during 2012 was \$12.2 million.

Loans delinquent 90 days or more as of December 31, 2012, totaled \$43.8 million, as compared to \$46.3 million on the same date in 2011. Loans in non-accrual status totaled \$52.7 million on December 31, 2012, as compared to \$51.6 million on the same date in 2011. There were \$3.3 million in loans past due at least 90 days and still accruing interest on December 31, 2012, compared to \$922,000 on December 31, 2011.

The performance of the loan portfolio during 2012 reflected the weakness of the economy. Total loans delinquent more than 30 days as a percentage of outstanding loans and leases was 4.37 percent on December 31, 2012. This is a decrease of 60 basis points from December 31, 2011. Management has carefully considered the delinquency in the portfolio as it evaluated the level of allowance for credit losses needed. While no one can say with certainty that the allowance is adequate, management is comfortable that it is adequate.

ASC 310-10-35, "Accounting by Creditors for Impairment of a Loan," requires identification of all impaired loans. A loan is considered to be impaired when it is probable that all principal and interest amounts will not be collected in accordance with the original loan terms. Loans with a carrying value of \$109.5

million or 6.55 percent of gross loans and leases were identified as impaired at December 31, 2012.

Deposits

Total deposits were \$1.88 billion at year end 2012, an increase of \$18.6 million from December 31, 2011. On average, total deposits increased at a rate of 0.28 percent during 2012.

Due to weak loan demand, management concentrated its efforts on maintaining current customer relationships, while reducing the cost of funding particularly in the certificates of deposit. As a result the Company experienced significant growth in demand deposit, NOW and money market balances while experiencing a decline in certificates of deposit. The Company offers fixed-rate certificates of deposit with maturities ranging from seven days to five years. Most of the certificates of deposit purchased by customers have a maturity ranging from six months to 24 months.

Non interest bearing deposits on December 31, 2012, totaled \$420.0 million, which was an increase of \$5.99 million, or 1.45 percent over the \$414.1 million on December 31, 2011.

Short-Term Borrowings

Short-term borrowing sources consist of federal funds purchased from downstream correspondents, repurchase agreements, sweep accounts of commercial customers, and overnight borrowings from Federal Home Loan Bank. The cash management services offered by the Company continue to be a valued service for our commercial deposit customers. The balance in Commercial Sweep Accounts totaled \$60.3 million on December 31, 2012. These accounts are overnight repurchase agreements requiring a direct pledge from our investment portfolio.

Weak loan demand throughout the year, resulted in the Company accumulating large amounts of on-balance-sheet liquidity. As a result, the Company did not utilize any of its short-term borrowing capacity with Federal Home Loan Bank during 2012.

Long-Term Borrowing

The Company's long-term borrowing consists of advances from Federal Home Loan Bank. On December 31, 2012, the Company had \$5.7 million outstanding in advances from Federal Home Loan Bank with maturities ranging from March 2013 through December 2027. Each advance is payable at its maturity, with a prepayment penalty. The advances are borrowed under a blanket

ANALYSIS OF ALLOWANCE FOR CREDIT LOSSES

	2012	2011	2010	2009	2008
Allowance for Credit Losses					
Balance January 1	\$ 28,782,925	\$ 22,802,975	\$ 20,746,522	\$ 21,753,237	\$ 20,214,651
Provision for credit losses	12,178,741	16,301,304	18,327,054	9,792,367	8,089,824
Less: Net charge-offs	(13,481,546)	(10,321,354)	(16,270,601)	(10,799,082)	(6,551,238)
Balance December 31	\$ 27,480,120	\$ 28,782,925	\$ 22,802,975	\$ 20,746,522	\$ 21,753,237
Average loans and leases, net of unearned income (000's)	\$ 1,656,284	\$ 1,709,584	\$ 1,754,495	\$ 1,624,235	\$ 1,487,745
Loans and leases outstanding at year end, net of unearned income (000's)	\$ 1,672,543	\$ 1,673,133	\$ 1,769,984	\$ 1,737,764	\$ 1,558,313
Nonperforming loans and leases at year end (000's)	\$ 56,041	\$ 52,502	\$ 31,300	\$ 28,147	\$ 15,165
Other real estate owned at year end (000's)	\$ 20,958	\$ 25,624	\$ 24,084	\$ 21,805	\$ 18,856
Ratios:					
Provision for credit losses to average loans and leases	0.74%	0.95%	1.04%	0.60%	0.54%
Net charge-offs to average loans and leases	0.81%	0.60%	0.93%	0.66%	0.44%
Allowance for credit losses to average loans and leases	1.66%	1.68%	1.30%	1.28%	1.46%
Allowance for credit losses to year end loans and leases	1.64%	1.72%	1.29%	1.19%	1.40%
Allowance for credit losses to nonperforming loans and leases	49.04%	54.82%	72.85%	73.71%	143.44%
Nonperforming loans and leases to average loans and leases	3.38%	3.07%	1.78%	1.73%	1.02%
Nonperforming assets to total assets	3.54%	3.64%	2.53%	2.43%	1.78%
Nonperforming assets to equity capital and reserves	37.06%	39.92%	30.93%	29.09%	20.43%
Total delinquency at year end	4.37%	4.97%	3.21%	2.97%	2.61%

lien agreement, and are collateralized by Federal Home Loan Bank stock and first mortgage loans.

In March 2005, Central Bancshares KY Statutory Trust I, a trust formed by the Company, closed a pooled private offering of 15,000 trust preferred securities with a liquidation amount of \$1,000 per security. The Company issued \$15,464,000 of subordinated debentures to the trust in exchange for ownership of all of the common security of the trust and the proceeds of the preferred securities sold by the trust. The Company may redeem the subordinated debentures, in whole or in part, in a principal amount, with integral multiples of \$1,000, on or after June 15, 2010 at 100 percent of the principal amount, plus accrued and unpaid interest. The subordinated debentures mature on June 15, 2035. The subordinated debentures are also redeemable, in whole or in part from time to time, upon the occurrence of specific events defined within the trust indenture. The Company has the option to defer interest payments on the subordinated debentures from time to time for a period not to exceed five consecutive years. The trust preferred securities and subordinated debentures have a variable rate of interest equal to the sum of the three month London Interbank Offered Rate (LIBOR) and 1.75%,

which was 2.06% at year end 2012. The Company's investment in the common stock of the trust was \$464,000.

In March 2009, Central Bancshares KY Statutory Trust III, a trust formed by the Company, closed a private offering of 22,600 trust preferred securities with a liquidation amount of \$1,000 per security. The Company issued \$23,278,000 of subordinated debentures to the trust in exchange for ownership of all of the common security of the trust and the proceeds of the preferred securities sold by the trust. The Company may redeem the subordinated debentures, in whole or in part, in a principal amount, with integral multiples of \$1,000, on or after March 31, 2014 at 100% of the principal amount, plus accrued and unpaid interest. The subordinated debentures mature on March 31, 2039. The subordinated debentures are also redeemable, in whole or in part from time to time, upon the occurrence of specific events defined within the trust indenture. The Company has the option to defer interest payments on the subordinated debentures from time to time for a period not to exceed five consecutive years. The trust preferred securities and subordinated debentures have a 10.00 percent fixed rate of interest. The Company's investment in the common stock of the trust was \$678,000.

AVERAGE EARNING ASSETS & AVERAGE FUNDS AVAILABLE

(in thousands)

	2012	2011	2010	2012/2011		2011/2010	
				Change	%	Change	%
Gross loans	\$ 1,656,284	\$ 1,709,584	\$ 1,754,495	\$ (53,300)	(3.12)%	\$ (44,911)	(2.56)%
Less: Allowance for credit losses	(30,186)	(25,643)	(21,987)	(4,543)	17.72%	(3,656)	16.63%
Total net loans	1,626,098	1,683,941	1,732,508	(57,843)	(3.43)%	(48,567)	(2.80)%
Investment securities	165,710	130,542	110,788	35,168	26.94%	19,754	17.83%
Money market investments	178,459	139,889	118,602	38,570	27.57%	21,287	17.95%
Total investments	344,169	270,431	229,390	73,738	27.27%	41,041	17.89%
Total earning assets	\$1,970,267	\$1,954,372	\$1,961,898	\$ 15,895	0.81%	\$ (7,526)	(0.38)%
Demand deposits	\$ 406,306	\$ 376,280	\$ 329,509	\$ 30,026	7.98%	\$ 46,771	14.19%
Immediately repricing deposits	742,116	671,951	726,424	70,165	10.44%	(54,473)	(7.50)%
Fixed-rate deposits	704,256	799,318	756,656	(95,062)	(11.89)%	42,662	5.64%
Total deposits	1,852,678	1,847,549	1,812,589	5,129	0.28%	34,960	1.93%
Borrowed funds	103,394	109,426	166,393	(6,032)	(5.51)%	(56,967)	(34.24)%
Total funds available	\$1,956,072	\$1,956,975	\$1,978,982	\$ (903)	(0.05)%	\$ (22,007)	(1.11)%

The \$37.6 million in trust preferred securities may be included in Tier 1 capital (with certain limitations applicable) under current regulatory guidelines and interpretations.

Capital

Capital adequacy guidelines of the regulatory agencies make regulatory capital requirements more sensitive to the risk profiles of individual banks, take off-balance-sheet exposure into account in assessing capital adequacy, and minimize disincentives for holding liquid, low risk assets.

In order for a bank holding company to be considered “well capitalized” under prompt corrective action provisions, a company must maintain a Total capital to risk-adjusted assets ratio of 10.0 percent, a Tier I capital to risk-adjusted assets ratio of 6.0 percent, and a Tier I capital to average assets ratio of 5.0 percent. On December 31, 2012, the Company had a Total capital to risk-adjusted assets ratio of 12.4 percent, a Tier I capital to risk-adjusted assets ratio of 11.2 percent, and a Tier I capital to average assets ratio of 9.3 percent. It is generally anticipated within the banking industry that new capital standards and requirements will be released sometime in 2013.

Subsequent Events

As part of the strategic planning process, management and the Board of Directors determined that the future expansion plans for the company did not include deeper penetration into the Eastern

part of Kentucky. As a result, it was determined that our Salt Lick Deposit Bank subsidiary would be sold, an objective completed on January 1, 2013. The Company accepted a cash purchase price of \$8.6 million for Salt Lick Deposit Bank, and recognized a net gain of \$196,000 from the sale.

On December 31, 2012, Salt Lick Deposit Bank had \$72.3 million in total assets, \$52.6 million in gross loans, and \$61.7 million in total deposits. Shareholder’s equity totaled \$8.0 million on December 31, 2012. For 2012 Salt Lick Deposit Bank generated net income of \$669,000.

Preliminary discussions between the Board of Directors and management are that at least part of the cash generated from the sale of Salt Lick Deposit Bank will be used to retire some of the outstanding trust preferred securities within the next 18 months.



Board of Directors and Shareholders
Central Bancshares, Inc.
Lexington, Kentucky

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Central Bancshares, Inc., which comprise the consolidated balance sheets as of December 31, 2012 and 2011, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Central Bancshares, Inc. as of December 31, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Crowe Horwath LLP

Crowe Horwath LLP
Louisville, Kentucky
March 1, 2013

CONSOLIDATED BALANCE SHEETS

	December 31	
	2012	2011
ASSETS		
Cash and due from financial institutions	\$ 46,597,962	\$ 48,651,143
Federal funds sold	<u>174,400,000</u>	<u>142,700,000</u>
<i>Total cash and cash equivalents</i>	<u>220,997,962</u>	<u>191,351,143</u>
Available for sale securities	166,527,755	152,068,423
Held to maturity securities	<u>2,820,945</u>	<u>6,401,139</u>
<i>Total securities</i>	<u>169,348,700</u>	<u>158,469,562</u>
Loans	1,608,012,457	1,604,806,013
Loans held for sale in the secondary market	11,906,207	13,521,673
Allowance for credit losses	<u>(26,839,981)</u>	<u>(27,925,801)</u>
<i>Loans, net</i>	<u>1,593,078,683</u>	<u>1,590,401,885</u>
Premises and equipment, net	37,570,985	40,502,991
Other real estate owned	20,111,669	24,777,686
Interest receivable	5,603,918	5,924,081
Federal Home Loan Bank stock, at cost	7,050,900	7,050,900
Goodwill	14,313,393	14,313,393
Other intangible assets	1,022,972	1,517,560
Other assets	44,612,665	46,298,546
Assets held for sale, Salt Lick Deposit Bank	<u>61,734,756</u>	<u>64,404,005</u>
Total assets	\$ 2,175,446,603	\$ 2,145,011,752
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits		
Non-interest bearing	\$ 412,619,586	\$ 407,283,561
Interest bearing	<u>1,402,364,545</u>	<u>1,390,295,714</u>
<i>Total deposits</i>	<u>1,814,984,131</u>	<u>1,797,579,275</u>
Federal funds purchased and repurchase agreements	60,302,320	52,494,526
Federal Home Loan Bank advances	3,222,343	13,759,676
Subordinated debentures	38,742,000	38,742,000
Interest payable	549,671	687,968
Other liabilities	13,016,614	11,165,803
Liabilities held for sale, Salt Lick Deposit Bank	<u>64,321,610</u>	<u>63,676,073</u>
<i>Total liabilities</i>	<u>1,995,138,689</u>	<u>1,978,105,321</u>
SHAREHOLDERS' EQUITY		
Common stock, \$10 par value, 350,000 shares authorized, 347,922 shares issued	3,479,220	3,479,220
Additional paid-in capital	6,890,468	6,890,468
Retained earnings	173,400,292	160,519,646
Accumulated other comprehensive income (loss)	<u>(3,462,066)</u>	<u>(3,982,903)</u>
<i>Total shareholders' equity</i>	<u>180,307,914</u>	<u>166,906,431</u>
Total liabilities and shareholders' equity	\$ 2,175,446,603	\$ 2,145,011,752

See accompanying notes.

CONSOLIDATED STATEMENTS OF INCOME

	Years Ended December 31	
	2012	2011
INTEREST AND DIVIDEND INCOME		
Loans, including fees	\$ 85,481,727	\$ 92,558,906
Securities:		
U.S. Treasury and government agencies	388,620	535,990
Obligations of states and political subdivisions	124,198	269,802
Mortgage-backed securities	657,656	555,918
Corporate debt bonds	213,090	212,500
Federal funds sold	445,492	364,315
Federal Home Loan Bank stock	353,522	338,216
	<u>87,664,305</u>	<u>94,835,647</u>
INTEREST EXPENSE		
Deposits	12,037,119	15,863,337
Federal funds purchased and repurchase agreements	50,625	55,362
Federal Home Loan Bank advances	454,046	494,771
Subordinated debentures	2,649,311	2,616,021
	<u>15,191,101</u>	<u>19,029,491</u>
Net interest income	72,473,204	75,806,156
Provision for credit losses	<u>12,178,741</u>	<u>16,301,304</u>
Net interest income after provision for credit losses	60,294,463	59,504,852
OTHER INCOME		
Service charges on deposit accounts	9,630,467	10,979,706
Mortgage loan sales and servicing, net	6,060,758	3,069,097
Credit card related fees	4,628,351	4,536,534
Trust fees	4,837,557	4,378,124
Net loss on sales and write-downs of other real estate	(2,853,228)	(2,812,082)
Other fees and income	<u>13,858,958</u>	<u>13,921,022</u>
	<u>36,162,863</u>	<u>34,072,401</u>
OTHER EXPENSES		
Salaries	31,644,833	31,061,073
Employee benefits	6,539,725	6,913,979
Occupancy expense	17,208,767	16,989,991
Other expenses	<u>28,238,382</u>	<u>28,403,713</u>
	<u>83,631,707</u>	<u>83,368,756</u>
Income before income tax benefit	12,825,619	10,208,497
Income tax benefit	<u>(55,027)</u>	<u>(808,738)</u>
NET INCOME	\$ 12,880,646	\$ 11,017,235
Basic earnings per share	\$ 37.02	\$ 31.67
Weighted average number of common shares outstanding	347,922	347,922

See accompanying notes.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31	
	2012	2011
OPERATING ACTIVITIES		
Interest received	\$ 88,487,315	\$ 95,755,812
Fees, commissions and other income received	29,428,543	30,892,057
Interest paid	(15,343,190)	(19,367,262)
Proceeds from loans held for sale	292,288,347	178,474,276
Originations of loans held for sale	(284,927,930)	(180,511,485)
Cash paid to suppliers and employees	(70,388,208)	(69,875,796)
Income tax paid	(923,495)	(516,986)
Net cash from operating activities	38,621,382	34,850,616
INVESTING ACTIVITIES		
Securities available for sale:		
Purchases	(71,354,048)	(329,199,204)
Maturities, calls and return of principal	57,304,977	287,340,493
Securities held to maturity:		
Purchases	(1,199,952)	(1,323,294)
Maturities, calls and return of principal	4,560,223	12,121,874
Investment in low-income housing and historic renovation limited partnerships	-	(4,175,862)
Net change in loans	(21,653,789)	80,680,800
Expenditures for bank premises and equipment	(1,702,171)	(1,176,954)
Proceeds from sale of other real estate owned	9,275,861	6,410,896
Net change in cash equivalent of Salt Lick Deposit Bank	340,678	(1,068,536)
Net cash from investing activities	(24,428,221)	49,610,213
FINANCING ACTIVITIES		
Net change in deposits	18,638,457	(45,712,130)
Net change in federal funds purchased and repurchase agreements	7,807,794	(13,811,036)
Repayment of Federal Home Loan Bank advances	(10,992,593)	(493,543)
Net cash from financing activities	15,453,658	(60,016,709)
Net change in cash and cash equivalents	29,646,819	24,444,120
Cash and cash equivalents, beginning of year	191,351,143	166,907,023
Cash and cash equivalents, end of year	\$ 220,997,962	\$ 191,351,143
RECONCILIATION OF NET INCOME TO NET CASH FROM OPERATING ACTIVITIES		
Net income	\$ 12,880,646	\$ 11,017,235
Adjustments to reconcile net income to net cash from operating activities:		
Provision for credit losses	12,178,741	16,301,304
Depreciation and amortization	8,005,458	7,371,315
Net loss on sales and write-downs of other real estate	2,853,228	2,812,082
Net gain on sale of loans	(5,786,102)	(2,887,503)
Net change in:		
Loans held for sale in the secondary market	7,085,762	(2,037,208)
Interest receivable	345,370	922,412
Prepaid expenses	2,290,155	2,053,007
Interest payable	(152,089)	(337,771)
Income taxes payable	(978,522)	(1,325,724)
Other liabilities	1,731,799	2,690,419
Other, net	(1,833,064)	(1,728,952)
Total adjustments	25,740,736	23,833,381
Net cash from operating activities	\$ 38,621,382	\$ 34,850,616
Supplemental noncash disclosures:		
Transfers from loans to other real estate owned	\$ 7,462,484	\$ 10,773,459
Write-downs of other real estate owned	2,224,208	1,927,398
Transfers from loans to loans held for sale	52,238,090	54,734,775
Transfers from deposits to deposits held for sale	61,731,020	60,497,419

See accompanying notes.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

Years Ended December 31, 2012 and 2011

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balances, January 1, 2011	\$ 3,479,220	\$ 6,890,468	\$ 149,502,411	\$(3,628,443)	\$ 156,243,656
Comprehensive income:					
Net income	-	-	11,017,235	-	11,017,235
Other comprehensive loss	-	-	-	(354,460)	(354,460)
Balances, December 31, 2011	3,479,220	6,890,468	160,519,646	(3,982,903)	166,906,431
Comprehensive income:					
Net income	-	-	12,880,646	-	12,880,646
Other comprehensive income	-	-	-	520,837	520,837
Balances, December 31, 2012	\$ 3,479,220	\$ 6,890,468	\$ 173,400,292	\$(3,462,066)	\$ 180,307,914

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Years Ended December 31	
	2012	2011
Net income	\$ 12,880,646	\$ 11,017,235
Other comprehensive income (loss):		
Unrealized gains/losses on securities:		
Unrealized holding gain (loss) arising during the period	893,380	(745,703)
Tax effect	(312,683)	260,996
Net of tax	580,697	(484,707)
Defined benefit pension plans:		
Net gain (loss) arising during the period	(92,092)	200,380
Tax effect	32,232	(70,133)
Net of tax	(59,860)	130,247
Total other comprehensive income (loss)	520,837	(354,460)
Comprehensive income	\$ 13,401,483	\$ 10,662,775

See accompanying notes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2012 AND 2011

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Nature of Operations: The consolidated financial statements include the accounts of Central Bancshares, Inc. (the "Company"), its wholly-owned Subsidiaries, Central Bank & Trust Co., Central Bank of Jefferson County, Inc., and Salt Lick Deposit Bank (the "Banks"), and Central Bank & Trust Co.'s wholly-owned Subsidiaries, Central Investment Center, Inc., Central Insurance Services, Inc., CB Investment Managers, LLC, Central Bank Title Agency, LLC, and CBT Real Estate Holdings, LLC. The Company merged the operations of Central Bank, FSB, into Central Bank & Trust Co. on January 18, 2011. On October 29, 2012, the Company agreed to sell Salt Lick Deposit Bank to a non-related third party financial institution. Salt Lick Deposit Bank's assets and liabilities are presented as assets and liabilities held for sale on the consolidated balance sheets as of December 31, 2012 and 2011. The sale transaction closed on January 1, 2013. All significant intercompany balances and transactions have been eliminated in consolidation.

The Banks grant commercial, consumer and residential loans to customers primarily located in Fayette, Boone, Kenton, Clark, Jessamine, Madison, Scott, Jefferson, Bath and surrounding counties in Kentucky. The Banks provide full banking services, including trust services. Although the Banks have diversified loan portfolios, a substantial portion of their debtors' ability to honor their contracts is dependent upon the local economy. Substantially all loans are secured by specific items of collateral including business assets, consumer assets and real estate. Other financial instruments, which potentially represent concentrations of credit risk, include cash and cash equivalents held in other financial institutions. Central Investment Center, Inc. offers non-deposit investment products, including mutual funds, annuities, and certain debt and equity securities. Central Insurance Services, Inc. is a licensed agent for life, health, title, and property and casualty insurance. CBT Real Estate Holdings, LLC holds and disposes of real estate acquired in settlement of loans.

Subsequent Events: The Company has evaluated subsequent events for recognition and disclosure through March 1, 2013, which is the date the financial statements were available to be issued.

Estimates in the Financial Statements: 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, 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 allowance for credit losses, other real estate valuation allowance, fair values of financial instruments, impairment of securities, mortgage servicing rights, pension obligation and contingent liabilities are particularly subject to change.

Cash Flows: Cash and cash equivalents include cash on hand, amounts due from financial institutions, securities purchased under resale agreements, money market investments and federal funds sold with maturities under 90 days. Net cash flows are reported for customer loan and deposit transactions, interest bearing deposits in other financial institutions, and federal funds purchased and repurchase agreements.

Securities: The Banks classify their security portfolios into two categories: available for sale and held to maturity. Securities are classified as available for sale when they might be sold before maturity. Securities are classified as held to maturity when management has the positive intent and ability to hold them to maturity. The Banks have no trading securities.

Securities available for sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income, net of tax. Securities held to maturity are stated at amortized cost.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized on the level-yield method without anticipating prepayments except for mortgage-backed securities where prepayments are anticipated. Gains and losses on dispositions are recorded on the trade date and based on the net proceeds and the adjusted carrying amount of the securities sold, using the specific identification method.

Management evaluates securities for other-than-temporary impairment (“OTTI”) at least on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis.

Loans: Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, net of deferred loan fees and costs, and an allowance for credit losses. Loan origination fees, net of certain direct origination costs, are deferred and the net amount is amortized as a yield adjustment over the life of the related loans.

Interest income is accrued on the principal balance. Classes of commercial and real estate loans are placed on nonaccrual, with interest income discontinued, at the time the loan is 90 days delinquent unless the loan is well-secured and in process of collection. Classes of consumer loans may be placed on nonaccrual if sufficient collateral exists, but are typically charged off no later than 120 days past due. All interest accrued but not received on loans placed on nonaccrual is reversed against interest income. Nonaccrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

For all loan classes, payments received on nonaccrual loans are applied to principal only using the cost recovery method if the Company estimates that collection of all principal is not reasonably assured. If all principal is reasonably assured, payments on nonaccrual loans may be applied to interest income on the cash basis. Loans of all classes are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

For all loan classes, past due status is based on the contractual terms of the loan.

Allowance for Credit Losses: The allowance for credit losses is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management’s judgment, should be charged off.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired. Loans of all classes are considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired.

Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Nonaccrual loans of certain classes are individually evaluated for impairment. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Interest income on impaired loans is recognized on the cash basis unless the loan is a troubled debt restructured loan performing under its modified terms. Large groups of smaller balance homogeneous loans, such as consumer loans, are collectively evaluated for impairment, and accordingly, they are not separately identified for impairment disclosures. If such loans are part of a borrowing relationship in which other types of loans have been individually evaluated for impairment, they also are individually evaluated.

Troubled debt restructurings are separately identified for impairment disclosures and are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a troubled debt restructuring is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral. For troubled debt restructurings that subsequently default, the Company determines the amount of reserve in accordance with the accounting policy for the allowance for credit losses.

The general component covers non-impaired loans and is based on historical loss experience adjusted for current factors. The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the most recent three years. This actual loss experience is supplemented with other economic factors based on the risks present for each portfolio segment. These economic factors include consideration of the following: levels of and trends in delinquencies and impaired loans; levels of and trends in charge-offs and recoveries; trends in volume and terms of loans; aggregate indebtedness of significant borrowing relationships; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures, and practices; experience, ability, and depth of lending management and other relevant staff; local economic trends and conditions; industry conditions; and effects of changes in credit concentrations. The following portfolio segments and their associated risks have been identified:

- Commercial loans are dependent on the strength of the industries of the related borrowers and the success of their businesses. Commercial loans are advanced for equipment purchases or to provide working capital or meet other financing needs of business enterprises. These loans may be secured by accounts receivable, inventory, equipment or other business assets. Financial information is obtained from the borrowers and guarantors to evaluate ability to repay the loans.
- Commercial real estate loans are dependent on the industries tied to these loans as well as the local commercial real estate market. Commercial real estate loans include completed projects as well as construction loans. The loans are secured by the real estate, and appraisals are obtained to support the loan amount. Financial information is obtained from the borrower(s) and guarantor(s) and/or an evaluation of the project's cash flows is performed to evaluate the borrower's ability to repay the loan.
- Residential real estate loans are affected by the local residential real estate market and the local economy. The Bank evaluates the borrower's repayment ability through a review of financial information obtained from the borrower. Appraisals or evaluations are obtained to support the loan amount.
- Consumer loans, including installment loans and credit card receivables, are dependent on local economies. Consumer loans are generally secured by consumer assets, but may be unsecured. The Bank evaluates the borrower's repayment ability through a review of financial information obtained from the borrower.

Mortgage Banking Activities: Mortgage loans originated and intended for sale in the secondary market are classified as held for sale and carried at the lower of aggregate cost or fair value as determined by outstanding commitments from investors. Gains on sales generated from mortgage banking activities are based on the difference between the selling price and the carrying value of the related loan sold.

The Company enters into commitments to originate certain mortgage loans whereby the interest rate on the loans is determined prior to funding (rate lock commitments). Rate lock commitments on mortgage loans that are intended to be sold are considered to be derivatives. The period of time between issuance of a loan commitment, loan closing and the sale of the loan generally ranges from 30 to 90 days. The Company protects itself from changes in interest rates through the use of best efforts forward delivery contracts, whereby the Company commits to sell a loan at the time the borrower commits to an interest rate with the intent that the buyer has assumed interest rate risk on the loan. If the underlying loan does not close, there is no obligation on the Company's part to deliver the loan to the investor. As a result, the Company is not exposed to losses nor will it realize significant gains related to its rate lock commitments due to changes in interest rates. The correlation between the rate lock commitments and the best efforts contracts is very high due to their similarity. Because of this high correlation, no gain or loss occurs on the rate lock commitments.

As the Company sells loans servicing released and retained, servicing rights are recognized as assets for the allocated value of retained servicing rights on loans sold. Servicing rights are initially recorded at fair value based on market prices for comparable mortgage servicing contracts. Servicing rights are expensed in proportion to, and over the period of, estimated net servicing revenues. Impairment is evaluated based on the fair value of the rights, using groupings of the underlying loans as to interest rates. Any impairment of a grouping is reported as a valuation allowance.

Servicing fee income is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal or a fixed amount per loan and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income. Servicing fee income, gains on sales of mortgage loans held for sale and amortization of mortgage servicing rights are reported on the income statement as mortgage loan sales and servicing, net.

Premises and Equipment: Land is carried at cost. Premises are stated at cost less accumulated depreciation computed on the straight-line method over the estimated useful lives of the assets. Furniture, fixtures and equipment are depreciated using an accelerated method. Leasehold improvements are amortized on the straight-line method over the shorter of the estimated useful lives of the improvements or the terms of the related leases.

Income Taxes: Deferred income tax assets and liabilities are computed annually for differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized. Income tax expense is the tax payable or refundable for the period plus or minus the change during the period in deferred tax assets and liabilities.

The Company recognizes a tax benefit only if it is more likely than not that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50 percent likely of being realized on examination. For tax positions not meeting the more-likely-than-not test, no tax benefit is recorded. The Company recognizes interest and/or penalties related to income tax matters in income tax expense.

Federal Home Loan Bank (FHLB) Stock: The Banks are members of the FHLB system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. FHLB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income.

Transfers of Financial Assets: Transfers of financial assets are accounted for as sales when control over the assets has been relinquished. Control over transferred assets is deemed to be surrendered when the assets have been isolated from the Company, the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Foreclosed Assets: Assets acquired through or instead of loan foreclosure are initially recorded at fair value, less selling costs, when acquired, establishing a new cost basis. If fair value declines subsequent to acquisition, a valuation allowance is recorded through expense. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Operating costs incurred after acquisition are expensed.

Goodwill and Other Intangible Assets: Goodwill results from business acquisitions and represents the excess of the purchase price over the fair value of acquired tangible assets and liabilities and identifiable intangible assets. Goodwill and other intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but tested for impairment at least annually or more frequently if events and circumstances exist that indicate a goodwill impairment test should be performed. The Company has selected December 31 as the date to perform the annual impairment test. Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Goodwill is the only intangible asset with an indefinite life on the Company's balance sheet.

Other intangible assets consist of customer relationship intangibles arising from acquisitions. They are initially measured at fair value and then are amortized on the straight-line method over their estimated useful lives, which is between 8 and 10 years.

Trust Department: Revenues from trust department services are recorded on the cash basis, which approximates the accrual basis, in accordance with customary banking practice. Securities and other properties, except cash deposits, held by the trust department in a fiduciary or agency capacity are not included in the consolidated financial statements since such items are not assets of the Company.

Investment in Limited Partnerships: Central Bank & Trust Co. is a limited equity partner in 16 low-income housing projects and two historic renovation projects. The investments are accounted for using the equity method and are included in other assets.

Benefit Plans: Pension expense is the net of interest cost, return on plan assets, and amortization of gains and losses not immediately recognized. Employee stock ownership and 401(k) plan expense is the amount contributed determined by Board decision. Deferred compensation plan expense is allocated over years of service.

All ESOP shares are allocated to participants as of the end of each fiscal year. Compensation expense is based on the price paid for the shares acquired by the plan during the year. Since all ESOP shares are allocated to participants, all dividends reduce retained earnings.

Loan Commitments and Related Financial Instruments: Financial instruments include off-balance-sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

Fair Value of Financial Instruments: Fair values of financial instruments, as more fully disclosed in Note 10, are estimated using relevant market information and other assumptions. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Earnings per Share: Basic earnings per share is net income divided by the weighted average number of shares outstanding during the period. The Company has no instruments outstanding which are potentially dilutive.

Comprehensive Income (Loss): Comprehensive income (loss) consists of net income and other comprehensive income (loss). Other comprehensive income (loss) includes unrealized gains and losses on securities available for sale, net of related income tax, and changes in the funded status of the defined benefit pension plan, net of related income tax. Accumulated other comprehensive income (loss) is recognized as a separate component of equity.

Loss Contingencies: Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe that there now are such matters that will have a material effect on the consolidated financial statements.

Dividend Restriction: Banking regulations require maintaining certain capital levels and may limit the dividends paid by the Banks to the holding company or by the holding company to shareholders.

Restrictions on Cash: Included in cash and due from financial institutions are certain deposits that are held at the Federal Reserve or maintained in vault cash in accordance with average balance requirements specified by the Federal Reserve Board of Governors. The average balance requirement was \$27,159,000 and \$28,047,000 at December 31, 2012 and 2011. These funds earn interest at an interest rate determined by the Federal Reserve.

Reclassifications: Some items in the prior year financial statements were reclassified to conform to the current year presentation. Reclassifications had no effect on prior year net income or shareholders' equity.

NOTE 2. SECURITIES

The fair value of securities available for sale and the related gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
2012				
U.S. government agency securities	\$ 82,458,382	\$ 111,915	\$ (45,009)	\$ 82,525,288
Obligations of states and political subdivisions	1,229,830	30,116	(2,899)	1,257,047
Agency mortgage-backed securities: Residential	79,971,660	608,253	-	80,579,913
Corporate bond	5,000,000	-	(111,500)	4,888,500
Total	<u>168,659,872</u>	<u>750,284</u>	<u>(159,408)</u>	<u>169,250,748</u>
Less: available for sale securities, held for sale	<u>(2,721,686)</u>	<u>(4,206)</u>	<u>(2,899)</u>	<u>(2,722,993)</u>
	\$165,938,186	\$ 746,078	\$ (156,509)	\$166,527,755
2011				
U.S. government agency securities	\$ 79,565,229	\$ 87,697	\$ (19,183)	\$ 79,633,743
Obligations of states and political subdivisions	1,297,970	42,923	(8,390)	1,332,503
Agency mortgage-backed securities: Residential	69,094,249	520,992	(62,565)	69,552,676
Corporate bond	5,000,000	-	(862,500)	4,137,500
Total	<u>154,957,448</u>	<u>651,612</u>	<u>(952,638)</u>	<u>154,656,422</u>
Less: available for sale securities, held for sale	<u>(2,588,140)</u>	<u>(8,262)</u>	<u>(8,403)</u>	<u>(2,587,999)</u>
	\$152,369,308	\$ 643,350	\$ (944,235)	\$152,068,423

The carrying amount, unrecognized gains and losses, and fair value of securities held to maturity are as follows:

	Carrying Amount	Gross Unrecognized Gains	Gross Unrecognized Losses	Fair Value
2012				
U.S. Treasury securities	\$ 325,570	\$ 430	\$ -	\$ 326,000
Obligations of states and political subdivisions	526,697	44,303	-	571,000
Agency mortgage-backed securities: Residential	1,956,432	88,568	-	2,045,000
Other	500,000	-	-	500,000
Total	\$ 3,308,699	133,301	-	3,442,000
Less: held to maturity securities, held for sale	(487,754)	(1,246)	-	(489,000)
	\$ 2,820,945	\$ 132,055	\$ -	\$ 2,953,000
2011				
U.S. Treasury securities	\$ 326,377	\$ 1,623	\$ -	\$ 328,000
U.S. government agency securities	1,001,457	18,543	-	1,020,000
Obligations of states and political subdivisions	1,488,143	80,857	-	1,569,000
Agency mortgage-backed securities: Residential	3,795,190	83,810	-	3,879,000
Other	500,000	-	-	500,000
Total	\$ 7,111,167	\$ 184,833	\$ -	\$ 7,296,000
Less: held to maturity securities, held for sale	(710,028)	(1,972)	-	(712,000)
	\$ 6,401,139	\$ 182,861	\$ -	\$ 6,584,000

The amortized cost and fair value of debt securities at December 31, 2012 are shown below by contractual maturity. The table includes securities owned by Salt Lick Deposit Bank. Mortgage-backed securities are shown separately because they are not due at a single maturity. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

	Held to Maturity		Available for sale	
	Carrying Amount	Fair Value	Fair Value	Amortized Cost
Due in one year or less	\$ 325,570	\$ 326,000	\$ 2,665,918	\$ 2,653,087
Due from one to five years	526,697	571,000	73,856,068	73,810,481
Due from five to ten years	500,000	500,000	5,515,623	5,612,629
Due after ten years	-	-	6,633,226	6,612,015
Agency mortgage-backed securities: Residential	1,956,432	2,045,000	80,579,913	79,971,660
Total	\$ 3,308,699	\$ 3,442,000	\$169,250,748	\$ 168,659,872

Securities with a carrying amount of approximately \$98,012,000 and \$80,930,000 at December 31, 2012 and 2011, were pledged to secure public deposits, repurchase agreements, trust deposits, and for other purposes as required or permitted by law. Included in these amounts were securities with a carrying amount of approximately \$2,625,000 and \$2,132,000 that were pledged by Salt Lick Deposit Bank at December 31, 2012 and 2011.

At December 31, 2012 and 2011, there were no holdings of securities of any one issuer, other than the U.S. government and its agencies, in an amount greater than 10 percent of shareholders' equity.

Securities with unrealized losses at year end 2012 and 2011, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, are shown below. The tables include securities owned by Salt Lick Deposit Bank.

Description of Securities	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
2012						
Available for Sale						
U.S. government agency securities	\$ 13,300,736	\$ (44,725)	\$ 68,553	\$ (284)	\$ 13,369,289	\$ (45,009)
Obligations of states and political subdivisions	-	-	174,296	(2,899)	174,296	(2,899)
Corporate bond	-	-	4,888,500	(111,500)	4,888,500	(111,500)
Total available for sale	\$ 13,300,736	\$ (44,725)	\$ 5,131,349	\$ (114,683)	\$ 18,432,085	\$ (159,408)

There were no securities held to maturity in an unrealized loss position at December 31, 2012.

Description of Securities	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
2011						
Available for Sale						
U.S. government agency securities	\$ 30,481,386	\$ (18,612)	\$ 128,990	\$ (571)	\$ 30,610,376	\$ (19,183)
Obligations of states and political subdivisions	211,867	(8,390)	-	-	211,867	(8,390)
Agency mortgage-backed securities: Residential	52,043,820	(62,565)	-	-	52,043,820	(62,565)
Corporate bond	4,137,500	(862,500)	-	-	4,137,500	(862,500)
Total available for sale	\$ 86,874,573	\$ (952,067)	\$ 128,990	\$ (571)	\$ 87,003,563	\$ (952,638)

There were no securities held to maturity in an unrealized loss position at December 31, 2011.

Unrealized losses on debt securities have not been recognized into income because the issued bonds are of high credit quality (rated AA or higher), management does not intend to sell and it is likely that management will not be required to sell the securities prior to their anticipated recovery, and the decline in fair value is largely due to changes in interest rates and other market conditions. The fair value is expected to recover as the bonds approach maturity.

NOTE 3. LOANS

Loans at December 31 were as follows:

	2012	2011
Commercial	\$ 345,250,182	\$ 359,247,491
Commercial real estate	750,385,561	658,691,318
Residential real estate	460,975,939	513,157,192
Installment	96,714,555	121,016,826
Credit card receivables	7,912,687	8,583,485
Loans held for sale in the secondary market, including Salt Lick Deposit Bank	12,292,863	13,592,523
	<u>1,673,531,787</u>	<u>1,674,288,835</u>
Unearned income	(988,377)	(1,155,524)
Allowance for credit losses	(27,480,120)	(28,782,925)
Loans, net	<u>1,645,063,290</u>	<u>1,644,350,386</u>
Less: loans held for sale	(52,624,746)	(54,805,625)
Less: allowance for credit losses associated with loans held for sale	640,139	857,124
	<u>\$ 1,593,078,683</u>	<u>\$ 1,590,401,885</u>

The Banks have entered into loan transactions with their directors, executive officers, significant shareholders and their affiliates (related parties). The aggregate amount of loans to such related parties was approximately \$2,106,000 and \$782,000 at December 31, 2012 and 2011. These amounts include approximately \$291,000 and \$301,000 in loans at Salt Lick Deposit Bank.

The following table presents the activity in the allowance for credit losses by segment of loans for the years ended December 31, 2012 and 2011:

	Commercial	Commercial Real Estate	Residential Real Estate	Installment	Credit Card Receivables	Unallocated	Total
2012							
Allowance for credit losses:							
Beginning balance	\$ 6,102,247	\$ 8,995,142	\$ 7,517,186	\$ 2,961,504	\$ 320,343	\$ 2,886,503	\$ 28,782,925
Provision for credit losses	6,130,486	6,660,335	(2,392,291)	376,185	389,714	1,014,312	12,178,741
Loans charged off	(6,498,771)	(3,066,646)	(2,456,384)	(2,706,762)	(255,345)	-	(14,983,908)
Recoveries	69,139	97,593	272,651	1,014,484	48,495	-	1,502,362
Total ending allowance balance	5,803,101	12,686,424	2,941,162	1,645,411	503,207	3,900,815	27,480,120
Less: allowance for credit losses associated with loans held for sale	(121,588)	(264,403)	(213,783)	(40,365)	-	-	(640,139)
	\$ 5,681,513	\$ 12,422,021	\$ 2,727,379	\$ 1,605,046	\$ 503,207	\$ 3,900,815	\$ 26,839,981
2011							
Allowance for credit losses:							
Beginning balance	\$ 2,810,473	\$ 6,730,769	\$ 6,919,254	\$ 4,011,371	\$ 343,634	\$ 1,987,474	\$ 22,802,975
Provision for credit losses	4,283,798	5,640,342	3,897,437	1,169,030	411,668	899,029	16,301,304
Loans charged off	(1,110,928)	(3,718,555)	(3,451,354)	(3,001,622)	(517,650)	-	(11,800,109)
Recoveries	118,904	342,586	151,849	782,725	82,691	-	1,478,755
Total ending allowance balance	6,102,247	8,995,142	7,517,186	2,961,504	320,343	2,886,503	28,782,925
Less: allowance for credit losses associated with loans held for sale	(197,958)	(367,637)	(217,261)	(50,636)	-	(23,632)	(857,124)
	\$ 5,904,289	\$ 8,627,505	\$ 7,299,925	\$ 2,910,868	\$ 320,343	\$ 2,862,871	\$ 27,925,801

The following table presents the balance in the allowance for credit losses and the recorded investment in loans by segment of loans and based on impairment method as of December 31, 2012 and 2011 (includes Salt Lick Deposit Bank balances):

	Commercial	Commercial Real Estate	Residential Real Estate	Installment	Credit Card Receivables	Unallocated	Total
2012							
Allowance for credit losses:							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	\$ 1,609,408	\$ 7,060,399	\$ 2,744,492	\$ 35,391	\$ -	\$ -	\$ 11,449,690
Collectively evaluated for impairment	<u>4,193,693</u>	<u>5,626,025</u>	<u>196,670</u>	<u>1,610,020</u>	<u>503,207</u>	<u>3,900,815</u>	<u>16,030,430</u>
Total ending allowance balance	\$ 5,803,101	\$ 12,686,424	\$ 2,941,162	\$ 1,645,411	\$ 503,207	\$ 3,900,815	\$ 27,480,120
Loans:							
Individually evaluated for impairment	\$ 16,405,703	\$ 68,008,554	\$ 25,023,325	\$ 63,869	\$ -	\$ -	\$ 109,501,451
Collectively evaluated for impairment	<u>328,931,255</u>	<u>682,377,007</u>	<u>447,189,223</u>	<u>96,650,686</u>	<u>7,893,788</u>	<u>-</u>	<u>1,563,041,959</u>
	\$ 345,336,958	\$ 750,385,561	\$ 472,212,548	\$ 96,714,555	\$ 7,893,788	\$ -	\$ 1,672,543,410
2011							
Allowance for credit losses:							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	\$ 4,157,268	\$ 5,462,497	\$ 4,214,814	\$ 49,163	\$ -	\$ -	\$ 13,883,742
Collectively evaluated for impairment	<u>1,944,979</u>	<u>3,532,645</u>	<u>3,302,372</u>	<u>2,912,341</u>	<u>320,343</u>	<u>2,886,503</u>	<u>14,899,183</u>
Total ending allowance balance	\$ 6,102,247	\$ 8,995,142	\$ 7,517,186	\$ 2,961,504	\$ 320,343	\$ 2,886,503	\$ 28,782,925
Loans:							
Individually evaluated for impairment	\$ 30,160,401	\$ 45,007,820	\$ 26,976,315	\$ 253,647	\$ -	\$ -	\$ 102,398,183
Collectively evaluated for impairment	<u>329,001,248</u>	<u>613,683,498</u>	<u>498,723,188</u>	<u>120,763,179</u>	<u>8,564,015</u>	<u>-</u>	<u>1,570,735,128</u>
	\$ 359,161,649	\$ 658,691,318	\$ 525,699,503	\$ 121,016,826	\$ 8,564,015	\$ -	\$ 1,673,133,311

The following table presents information related to impaired loans by segment of loans as of and for the years ended December 31, 2012 and 2011 (includes information for Salt Lick Deposit Bank):

	Unpaid Principal Balance	Recorded Investment	Allowance for Credit Losses Allocated	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
December 31, 2012						
With no related allowance recorded:						
Commercial	\$ 14,316,801	\$ 12,376,857	\$ -	\$ 14,096,730	\$ 709,891	\$ 709,891
Commercial real estate	50,047,210	48,560,322	-	47,231,457	1,533,205	1,533,205
Residential real estate	17,927,305	15,945,224	-	18,556,515	370,313	370,313
Installment	323,242	20,534	-	356,406	1,227	1,227
Subtotal	82,614,558	76,902,937	-	80,241,108	2,614,636	2,614,636
With an allowance recorded:						
Commercial	8,729,409	4,028,846	1,609,408	6,755,979	28,569	28,569
Commercial real estate	21,028,727	19,448,232	7,060,399	18,451,911	166,725	166,725
Residential real estate	9,146,664	9,078,101	2,744,492	7,725,455	284,613	284,613
Installment	43,335	43,335	35,391	46,556	4,227	4,227
Subtotal	38,948,135	32,598,514	11,449,690	32,979,901	484,134	484,134
Total	\$ 121,562,693	\$ 109,501,451	\$ 11,449,690	\$ 113,221,009	\$ 3,098,770	\$ 3,098,770
December 31, 2011						
With no related allowance recorded:						
Commercial	\$ 22,762,646	\$ 20,373,310	\$ -	\$ 20,100,583	\$ 905,837	\$ 905,837
Commercial real estate	29,424,716	27,172,659	-	24,918,947	868,260	868,260
Residential real estate	19,282,443	18,930,816	-	19,673,454	677,634	677,634
Installment	498,939	160,660	-	174,878	2,401	2,401
Subtotal	71,968,744	66,637,445	-	64,867,862	2,454,132	2,454,132
With an allowance recorded:						
Commercial	9,882,218	9,787,091	4,157,268	2,863,821	111,511	111,511
Commercial real estate	18,666,310	17,835,161	5,462,497	15,231,993	301,925	301,925
Residential real estate	8,230,554	8,045,499	4,214,814	9,273,711	242,782	242,782
Installment	331,961	92,987	49,163	106,322	156	156
Subtotal	37,111,043	35,760,738	13,883,742	27,475,847	656,374	656,374
Total	\$ 109,079,787	\$ 102,398,183	\$ 13,883,742	\$ 92,343,709	\$ 3,110,506	\$ 3,110,506

The recorded investment in loans excludes accrued interest receivable and loan origination fees, net due to immateriality. For purposes of this disclosure, the unpaid principal balance is not reduced for net charge-offs.

Nonaccrual loans and loans past due over 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

The following table presents the recorded investment in nonaccrual loans and loans past due over 90 days still on accrual by segment of loans as of December 31, 2012 and 2011:

	Nonaccrual		Loans Past Due Over 90 Days Still Accruing	
	2012	2011	2012	2011
Commercial	\$ 6,782,915	\$ 7,319,206	\$ 224,657	\$ 8,143
Commercial real estate	31,965,413	30,140,983	2,265,166	496,381
Residential real estate	13,538,470	13,066,439	815,550	370,024
Installment	411,674	1,036,412	7,390	18,301
Credit card receivables	23,904	17,155	6,215	29,447
Total	<u>52,722,376</u>	<u>51,580,195</u>	<u>3,318,978</u>	<u>922,296</u>
Less: loans held for sale, Salt Lick Deposit Bank	<u>1,126,935</u>	<u>1,099,896</u>	<u>40,500</u>	<u>38,128</u>
	\$ <u>51,595,441</u>	\$ <u>50,480,299</u>	\$ <u>3,278,478</u>	\$ <u>884,168</u>

The following table presents the aging of the recorded investment in past due loans as of December 31, 2012 and 2011 by segment of loans, including loans of Salt Lick Deposit Bank:

	30-89 Days Past Due	Greater than 89 Days Past Due	Total Past Due	Loans Not Past Due	Total
December 31, 2012					
Commercial	\$ 1,549,270	\$ 6,568,911	\$ 8,118,181	\$ 337,218,777	\$ 345,336,958
Commercial real estate	6,819,611	25,267,540	32,087,151	718,298,410	750,385,561
Residential real estate	7,407,193	11,728,388	19,135,581	453,076,967	472,212,548
Installment	2,411,984	209,547	2,621,531	94,093,024	96,714,555
Credit card receivables	164,906	14,330	179,236	7,714,552	7,893,788
Total	<u>\$ 18,352,964</u>	<u>\$ 43,788,716</u>	<u>\$ 62,141,680</u>	<u>\$ 1,610,401,730</u>	<u>\$ 1,672,543,410</u>
December 31, 2011					
Commercial	\$ 11,768,184	\$ 7,101,429	\$ 18,869,613	\$ 340,292,036	\$ 359,161,649
Commercial real estate	9,183,030	27,555,562	36,738,592	621,952,726	658,691,318
Residential real estate	7,731,144	10,750,235	18,481,379	507,218,124	525,699,503
Installment	2,920,557	843,033	3,763,590	117,253,236	121,016,826
Credit card receivables	119,840	46,602	166,442	8,397,573	8,564,015
Total	<u>\$ 31,722,755</u>	<u>\$ 46,296,861</u>	<u>\$ 78,019,616</u>	<u>\$ 1,595,113,695</u>	<u>\$ 1,673,133,311</u>

Troubled Debt Restructurings: The Company has allocated \$7,937,589 and \$8,385,193 of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as of December 31, 2012 and 2011. The Company has committed to lend additional amounts totaling up to \$251,670 and \$65,967 as of December 31, 2012 and 2011 to customers with outstanding loans that are classified as troubled debt restructurings.

During the years ended December 31, 2012 and 2011, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; or a permanent reduction of the recorded investment in the loan.

Modifications involving a reduction of the stated interest rate of the loan were for periods ranging from one month to 10 years. Modifications involving an extension of the maturity date were for periods ranging from one months to six years.

The following table presents loans by segment modified as troubled debt restructurings that occurred during the years ended December 31, 2012 and 2011 and includes troubled debt restructurings of Salt Lick Deposit Bank:

	<u>Number of Loans</u>	<u>Pre-Modification Outstanding Recorded Investment</u>	<u>Post-Modification Outstanding Recorded Investment</u>
December 31, 2012			
Troubled debt restructurings:			
Commercial	13	\$ 4,639,242	\$ 4,616,780
Commercial real estate	15	23,860,041	24,240,512
Residential real estate	22	4,081,395	3,994,636
Installment	1	5,348	5,537
Credit card receivables	0	-	-
Total	<u>51</u>	<u>\$ 32,586,026</u>	<u>\$ 32,857,465</u>
December 31, 2011			
Troubled debt restructurings:			
Commercial	5	\$ 6,312,940	\$ 6,442,446
Commercial real estate	10	19,446,831	19,758,226
Residential real estate	13	3,724,283	3,702,952
Installment	1	13,494	11,613
Credit card receivables	0	-	-
Total	<u>29</u>	<u>\$ 29,497,548</u>	<u>\$ 29,915,237</u>

The troubled debt restructurings described above increased the allowance for credit losses by \$1,179,380 and resulted in charge-offs of \$35,902 during the year ended December 31, 2012. The troubled debt restructurings described above increased the allowance for credit losses by \$4,264,460 and resulted in charge-offs of \$143,785 during the year ended December 31, 2011. The troubled debt restructurings described above which are presented as loans held for sale in the Salt Lick Deposit Bank transaction total \$0 and \$59,335 for the years ended December 31, 2012 and 2011.

The following table presents loans by segment modified as troubled debt restructurings for which there was a payment default within 12 months following the modification during the years ended December 31, 2012 and 2011 and includes troubled debt restructurings of Salt Lick Deposit Bank:

	<u>Number of Loans</u>	<u>Recorded Investment</u>
December 31, 2012		
Troubled debt restructurings that subsequently defaulted:		
Commercial	3	\$ 212,547
Commercial real estate	5	1,469,159
Residential real estate	9	1,950,628
Installment	0	-
Credit card receivables	0	-
Total	<u>17</u>	<u>\$ 3,632,334</u>
December 31, 2011		
Troubled debt restructurings that subsequently defaulted:		
Commercial	4	\$ 6,382,514
Commercial real estate	7	17,688,550
Residential real estate	5	1,275,195
Installment	0	-
Credit card receivables	0	-
Total	<u>16</u>	<u>\$ 25,346,259</u>

A loan is considered to be in payment default once it is 30 days contractually past due under the modified terms.

The troubled debt restructurings that subsequently defaulted described above increased the allowance for credit losses by \$103,820 and resulted in charge-offs of \$6,884 during the year ended December 31, 2012. The troubled debt restructurings that subsequently defaulted described above increased the allowance for credit losses by \$4,173,610 and resulted in charge-offs of \$143,785 during the year ended December 31, 2011. The troubled debt restructurings that subsequently defaulted during the years ended December 31, 2012 and 2011 reported as loans held for sale in the Salt Lick Deposit Bank transaction total \$0 and \$45,402, respectively.

The terms of certain other loans were modified during the year ended December 31, 2012 that did not meet the definition of a troubled debt restructuring. These loans have a total recorded investment as of December 31, 2012 of \$178,755,568. The modification of these loans involved either a modification of the terms of a loan to borrowers who were not experiencing financial difficulties or a delay in a payment that was considered to be insignificant. The terms of certain other loans were modified during the year ended December 31, 2011 that did not meet the definition of a troubled debt restructuring. These loans have a total recorded investment as of December 31, 2011 of \$36,862,000. The modification of these loans involved either a modification of the terms of a loan to borrowers who were not experiencing financial difficulties or a delay in a payment that was considered to be insignificant.

In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Company's internal underwriting policy.

Certain loans which were modified during the year ended December 31, 2012 and did not meet the definition of a troubled debt restructuring as the modification was a delay in a payment that was considered to be insignificant, had delays in payment ranging from 30 days to three months.

Credit Quality Indicators: The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis includes loans with an outstanding balance greater than \$25,000 and non-homogeneous loans, such as commercial, commercial real estate and residential real estate loans, and homogeneous loans that are part of a borrowing relationship. This analysis is performed on a monthly basis. The Company uses the following definitions for risk ratings:

Special Mention. Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

Substandard. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. Loans listed as not rated are included in groups of homogeneous loans, such as installment loans and credit card receivables. Credit quality indicators similar to those described above, including delinquency and other performance indicators, are used for loans that are not rated.

Based on the most recent analysis performed, the risk category of loans by segment of loans, including loans of Salt Lick Deposit Bank, is as follows:

	Pass	Special Mention	Substandard	Doubtful	Not Rated	Total
December 31, 2012						
Commercial	\$ 325,037,922	\$ 3,918,642	\$ 16,293,618	\$ -	\$ -	\$ 345,250,182
Commercial real estate	664,216,250	27,462,727	58,626,229	80,355	-	750,385,561
Residential real estate	430,520,190	5,769,460	24,560,561	125,728	-	460,975,939
Installment	-	-	-	-	96,714,555	96,714,555
Credit card receivables	-	-	-	-	7,912,687	7,912,687
Loans held for sale in the secondary market	-	-	-	-	12,292,863	12,292,863
	<u>\$ 1,419,774,362</u>	<u>\$ 37,150,829</u>	<u>\$ 99,480,408</u>	<u>\$ 206,083</u>	<u>\$ 116,920,105</u>	<u>\$ 1,673,531,787</u>
December 31, 2011						
Commercial	\$ 324,463,041	\$ 5,162,154	\$ 29,428,924	\$ 161,831	\$ 31,541	\$ 359,247,491
Commercial real estate	589,030,844	22,220,121	47,440,353	-	-	658,691,318
Residential real estate	481,591,522	4,881,259	25,911,859	772,552	-	513,157,192
Installment	-	-	-	-	121,016,826	121,016,826
Credit card receivables	-	-	-	-	8,583,485	8,583,485
Loans held for sale in the secondary market	-	-	-	-	13,592,523	13,592,523
	<u>\$ 1,395,085,407</u>	<u>\$ 32,263,534</u>	<u>\$ 102,781,136</u>	<u>\$ 934,383</u>	<u>\$ 143,224,375</u>	<u>\$ 1,674,288,835</u>

NOTE 4. MORTGAGE BANKING ACTIVITIES

Loans originated for sale in the secondary market and subsequently sold totaled approximately \$286,227,000 and \$175,587,000 during 2012 and 2011. The Company had commitments to originate \$31,027,237 in loans at December 31, 2012, which it intends to sell after the loans are closed. The Company had \$12,292,863 and \$13,592,523 in loans held for sale at December 31, 2012 and 2011; these totals included \$386,656 and \$70,850 held for sale by Salt Lick Deposit Bank.

Loans serviced for others, which are not reported as assets, totaled approximately \$55,554,000 and \$60,370,000 at December 31, 2012 and 2011.

Activity for capitalized mortgage servicing rights included in other assets during 2012 and 2011 was as follows:

	2012	2011
Servicing rights		
Beginning of year	\$ 227,087	\$ 228,999
Originated	81,159	55,978
Amortized to expense	<u>(61,934)</u>	<u>(57,890)</u>
End of year	\$ 246,312	\$ 227,087

No valuation allowance for impaired servicing rights is considered necessary. The fair value of capitalized mortgage servicing rights was estimated to be approximately \$283,000 and \$261,000 at year end 2012 and 2011.

On April 1, 2011, the Company entered into a settlement with a mortgage investor which had been demanding repayment on three mortgage loans that the Company had sold to the investor. Compliance with loan origination guidelines was at issue. The Company made a \$325,000 payment to the investor in return for release from any further buy back demands or potential penalties on all loans sold by the Company to the investor on or before December 31, 2008. The payment resulted in additional expense of approximately \$250,000 in 2011, which is included in other expenses.

NOTE 5. OTHER REAL ESTATE OWNED

Activity in other real estate owned was as follows:

	2012	2011
Other real estate owned, beginning of year	\$ 25,624,246	\$ 24,083,659
Acquisition and improvement of other real estate, net	7,462,484	10,763,565
Proceeds from sales of other real estate	(9,275,861)	(6,410,896)
Provision for valuation allowance of other real estate	(2,224,208)	(2,126,738)
Net loss on sales and direct write-downs	<u>(629,020)</u>	<u>(685,344)</u>
Other real estate owned, end of year	20,957,641	25,624,246
Less: other real estate owned, held for sale	<u>(845,972)</u>	<u>(846,560)</u>
	\$ 20,111,669	\$ 24,777,686

Activity in the valuation allowance was as follows:

	2012	2011
Beginning of year	\$ 7,545,922	\$ 5,618,524
Additions charged to expense	2,224,208	2,126,738
Direct write-downs	<u>(1,129,295)</u>	<u>(199,340)</u>
End of year	8,640,835	7,545,922
Less: valuation allowance, held for sale	<u>(12,500)</u>	<u>-</u>
	\$ 8,628,335	\$ 7,545,922

Expenses related to foreclosed assets include:

	2012	2011
Net loss (gain) on sales and direct write-downs	\$ 629,020	\$ 685,344
Provision for valuation allowance	2,224,208	2,126,738
Operating expenses, net of rental income	<u>1,809,361</u>	<u>2,948,724</u>
	\$ 4,662,589	\$ 5,760,806

NOTE 6. PREMISES AND EQUIPMENT

Premises and equipment at December 31 are as follows:

	2012	2011
Land	\$ 3,580,756	\$ 3,580,756
Buildings and improvements	24,060,048	24,027,298
Leasehold improvements	26,493,124	26,487,431
Furniture, fixtures and equipment	38,880,829	37,583,151
Construction in progress	382,506	162,913
Accumulated depreciation	<u>(52,986,617)</u>	<u>(48,357,514)</u>
	40,410,646	43,484,035
Less: premises and equipment held for sale, net	<u>(2,839,661)</u>	<u>(2,981,044)</u>
Total	\$ 37,570,985	\$ 40,502,991

Depreciation and amortization expense amounted to \$4,775,559 and \$5,056,754 in 2012 and 2011.

Operating Leases: The Company leases its main office, 12 banking center locations and its mortgage and insurance center in addition to its land leases for three banking centers. The Company currently subleases a portion of its space to eight tenants. Salt Lick Deposit Bank had no leases as of December 31, 2012. Rent expense for the Company was approximately \$5,150,000 and \$4,880,000 in 2012 and 2011. Rent commitments under noncancelable operating leases, and certain renewal provisions, net of subleases, are as follows:

2013	\$ 5,019,467
2014	5,103,431
2015	5,329,867
2016	5,610,919
2017	5,614,672
Thereafter	<u>32,832,641</u>
	\$ 59,510,997

NOTE 7. GOODWILL AND INTANGIBLE ASSETS

Goodwill was \$15,004,524 at December 31, 2012 and 2011. Included in goodwill at December 31, 2012 and 2011 was \$691,131 generated from the Company's acquisition of Salt Lick Deposit Bank.

Impairment exists when a reporting unit's carrying value of goodwill exceeds its fair value. At December 31, 2012, the Company's reporting unit had positive equity and the Company performed a qualitative assessment to determine if it was more likely than not that the fair value of the reporting unit exceeded its carrying value, including goodwill. The qualitative assessment indicated that it was more likely than not that the fair value of the reporting unit exceeded its carrying value, resulting in no impairment. Management also quantitatively determined the fair value of the reporting unit and compared it to its carrying amount. The result of this assessment supported the qualitative analysis.

Acquired intangible assets were as follows as of December 31:

	2012		2011	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Customer relationship intangibles	\$ 4,923,564	\$ 3,900,592	\$ 4,923,564	\$ 3,406,004

Aggregate amortization expense was \$494,588 for 2012 and 2011.

Estimated amortization expense for each of the next five years is as follows:

2013	\$ 413,968
2014	263,348
2015	263,348
2016	82,308
2017	-

NOTE 8. DEPOSITS

Time deposits of \$100,000 or more were \$399,518,990 and \$450,807,744 at December 31, 2012 and 2011, including \$20,262,861 and \$19,681,279 at December 31, 2012 and 2011 representing time deposits included in the Salt Lick Deposit Bank transaction.

Scheduled maturities of time deposits for the next five years are as follows:

	<u>Company</u>	<u>Held for Sale</u>	<u>Total</u>
2013	\$ 449,660,871	\$ 20,575,439	\$ 470,236,310
2014	66,526,499	6,086,016	72,612,515
2015	65,008,033	5,333,458	70,341,491
2016	43,131,698	1,939,250	45,070,948
2017	22,646,330	2,354,197	25,000,527
Thereafter	50,765	-	50,765
	<u>\$ 647,024,196</u>	<u>\$ 36,288,360</u>	<u>\$ 683,312,556</u>

Deposits of directors and executive officers of the Banks and companies in which they have beneficial ownership were approximately \$24,266,000 and \$18,929,000 at December 31, 2012 and 2011. These amounts include approximately \$540,000 and \$430,000 in deposits at Salt Lick Deposit Bank.

NOTE 9. FEDERAL HOME LOAN BANK ADVANCES AND OTHER BORROWINGS

At December 31, advances from the Federal Home Loan Bank are as follows:

	<u>2012</u>	<u>2011</u>
Maturities March 2013 through December 2027, fixed rates ranging from 1.88% to 8.05%, averaging 4.04% in 2012 and 2.69% in 2011	\$ 5,703,898	\$ 16,696,491
Less: held for sale in Salt Lick Deposit Bank transaction	(2,481,555)	(2,936,815)
Total	<u>\$ 3,222,343</u>	<u>\$ 13,759,676</u>

Each advance is payable at its maturity date, with a prepayment penalty for fixed rate advances that are paid off earlier than maturity. The advances are borrowed under a blanket lien agreement. The advances are collateralized by Federal Home Loan Bank stock and first mortgage loans with an aggregate unpaid principal balance of approximately \$262,583,000 and \$247,630,000 at December 31, 2012 and 2011. Based on this collateral and the holding of Federal Home Loan Bank stock, the Banks are eligible to borrow up to a total of \$87,919,529 at year end 2012.

Payment Information: Scheduled principal repayments associated with the advances over the next five years are as follows:

	<u>Company</u>	<u>Held for Sale</u>	<u>Total</u>
2013	\$ 118,427	\$ 489,103	\$ 607,530
2014	39,228	382,054	421,282
2015	1,930,194	362,574	2,292,768
2016	41,185	334,196	375,381
2017	42,199	349,627	391,826
Thereafter	1,051,110	564,001	1,615,111
	<u>\$ 3,222,343</u>	<u>\$ 2,481,555</u>	<u>\$ 5,703,898</u>

Subordinated Debentures: In March 2009, Central Bancshares KY Statutory Trust III, a trust formed by the Company, closed a private placement offering of 22,600 trust preferred securities with a liquidation amount of \$1,000 per security. The Company issued \$23,278,000 of subordinated debentures to the trust in exchange for ownership of all of the common security of the trust and the proceeds of the preferred securities sold by the trust. The Company may redeem the subordinated debentures, in whole or in part, in a principal amount, with integral multiples of \$1,000, on or after March 31, 2014 at 100% of the principal amount, plus accrued and unpaid interest. The subordinated debentures mature on March 31, 2039. The subordinated debentures are also redeemable, in whole or in part from time to time, upon the occurrence of specific events defined within the trust indenture. The Company has the option to defer interest payments on the subordinated debentures from time to time for a period not to exceed five consecutive years.

The \$22,600,000 in trust preferred securities may be included in Tier I capital (with certain limitations applicable) under current regulatory guidelines and interpretations. The trust preferred securities and subordinated debentures have a fixed rate of interest of 10.00%. The Company's investment in the common stock of the trust was \$678,000 and is included in other assets.

In March 2005, Central Bancshares KY Statutory Trust I, a trust formed by the Company, closed a pooled private offering of 15,000 trust preferred securities with a liquidation amount of \$1,000 per security. The Company issued \$15,464,000 of subordinated debentures to the trust in exchange for ownership of all of the common security of the trust and the proceeds of the preferred securities sold by the trust. The Company may redeem the subordinated debentures, in whole or in part, in a principal amount with integral multiples of \$1,000, on or after June 15, 2010 at 100% of the principal amount, plus accrued and unpaid interest. The subordinated debentures mature on June 15, 2035. The subordinated debentures are also redeemable, in whole or in part from time to time, upon the occurrence of specific events defined within the trust indenture. The Company has the option to defer interest payments on the subordinated debentures from time to time for a period not to exceed five consecutive years.

The \$15,000,000 in trust preferred securities may be included in Tier I capital (with certain limitations applicable) under current regulatory guidelines and interpretations. The trust preferred securities and subordinated debentures have a variable rate of interest equal to the sum of the three month London Interbank Offered Rate ("LIBOR") and 1.75%, which was 2.06% at year end 2012. The Company's investment in the common stock of the trust was \$464,000 and is included in other assets.

The Company has an outstanding line of credit for \$10,000,000 from a commercial bank for the purpose of securing additional funds for capital infusion to its Subsidiaries or for debt service needs. As of December 31, 2012, the Company had not drawn upon this line. Terms of the line of credit include a variable interest rate equal to the sum of prime as published in *The Wall Street Journal* and 0.50% (3.75% as of December 31, 2012) with a floor of 4.75%, and monthly payments of interest only with the balance due at maturity on September 30, 2013. The line of credit is secured by 100% of the stock of Central Bank & Trust Co.

NOTE 10. FAIR VALUE

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (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. There are three levels of inputs that may be used to measure fair values:

Level 1: Quoted prices (unadjusted) for 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; or other inputs that are observable or can be corroborated by observable market data.

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

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

Investment Securities: The fair values of securities available for sale are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs).

Impaired Loans: At the time a loan is considered impaired, it is valued at the lower of cost or fair value. Impaired loans carried at fair value generally receive specific allocations of the allowance for loan losses. For collateral dependent loans, fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

Other Real Estate Owned: Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

Appraisals for both collateral-dependent impaired loans and other real estate owned are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Company. Once received, a member of the Loan Review Department reviews the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison with independent data sources such as recent market data or industry-wide statistics. On an annual basis, the Company compares the actual selling price of collateral that has been sold to the most recent appraised value to determine what additional adjustment should be made to the appraisal value to arrive at fair value. The most recent analysis performed indicated that a discount of 10% should be applied to all appraisal values. The Company has all collateral-dependent impaired loans and other real estate owned appraised annually.

Loans Held For Sale in the Secondary Market: Loans held for sale in the secondary market are carried at the lower of cost or fair value, which is evaluated on a pool-level basis. The fair value of loans held for sale is determined using quoted prices for similar assets, adjusted for specific attributes of that loan or other observable market data, such as outstanding commitments from third party investors (Level 2).

Assets Measured on a Recurring Basis

Assets measured at fair value on a recurring basis are summarized below and include assets owned by Salt Lick Deposit Bank:

	Fair Value Measurements at December 31, Using		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets (2012):			
Available for sale securities:			
U.S. government agency securities	\$ -	\$ 82,525,288	\$ -
Obligations of states and political subdivisions	-	1,257,047	-
Agency mortgage-backed securities: Residential	-	80,579,913	-
Corporate bond	-	4,888,500	-
Assets (2011):			
Available for sale securities:			
U.S. government agency securities	\$ -	\$ 79,633,743	\$ -
Obligations of states and political subdivisions	-	1,332,503	-
Agency mortgage-backed securities: Residential	-	69,552,676	-
Corporate bond	-	4,137,500	-

There were no transfers between Level 1 and Level 2 during 2012 or 2011.

Assets Measured on a Non-Recurring Basis

Assets measured at fair value on a non-recurring basis are summarized below and include assets owned by Salt Lick Deposit Bank:

	Fair Value Measurements at December 31, Using		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets (2012):			
Impaired loans:			
Commercial	\$ -	\$ -	\$ 2,419,438
Commercial real estate	-	-	12,387,833
Residential real estate	-	-	6,333,609
Installment	-	-	7,944
Other real estate owned:			
Commercial	-	-	3,808,940
Commercial real estate	-	-	15,438,470
Residential real estate	-	-	1,710,231
Loans held for sale in the secondary market	-	12,342,000	-
Assets (2011):			
Impaired loans:			
Commercial	\$ -	\$ -	\$ 5,629,823
Commercial real estate	-	-	12,372,664
Residential real estate	-	-	3,830,685
Installment	-	-	43,824
Other real estate owned:			
Commercial	-	-	983,878
Commercial real estate	-	-	15,070,511
Residential real estate	-	-	9,569,857
Loans held for sale in the secondary market	-	13,701,000	-

The following represents impairment charges recognized during the period:

Impaired loans that are measured for impairment using the fair value of the collateral for collateral dependent loans, had a principal balance of \$109,501,451 at December 31, 2012. Those collateral dependent loans with a valuation allowance of \$11,449,690 at December 31, 2012, resulting in \$1,879,473 of additional provision for loan losses for the year ended December 31, 2012. Impaired loans that are measured for impairment using the fair value of the collateral for collateral dependent loans, had a principal balance of \$102,398,183 at December 31, 2011. Those collateral dependent loans with a valuation allowance of \$13,883,742 at December 31, 2011, resulting in \$9,306,762 of additional provision for loan losses for the year ended December 31, 2011.

Other real estate owned measured at fair value less costs to sell, had a net carrying amount of \$20,957,641, which is made up of the outstanding balance of \$29,598,476, net of a valuation allowance of \$8,640,835 at December 31, 2012, resulting in an additional provision of \$2,224,208 for the year ended December 31, 2012. Other real estate owned measured at fair value less costs to sell, had a net carrying amount of \$25,624,246, which is made up of the outstanding balance of \$33,170,168, net of a valuation allowance of \$7,545,922 at December 31, 2011, resulting in an additional provision of \$2,126,738 for the year ended December 31, 2011.

The following table presents qualitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at December 31, 2012:

Valuation Techniques	Fair Value	Asset Category	Unobservable Input(s)	Range (Weighted Average)
Sales approach commercial	\$ 16,648,244	Other real estate owned, all classes of impaired loans	Adjustment for differences between the comparable sales, selling costs, aging, and specific borrower information	5%–29% (21%)
Income approach	\$ 25,458,221	Other real estate owned, all classes of impaired loans	Adjustments for aging, selling costs, and specific borrower information	10%–23% (19%)

The carrying amount and estimated fair value of the Company's financial instruments at December 31, including Salt Lick Deposit Bank's financial instruments, are as follows:

	2012		2011	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets				
Cash and cash equivalents	\$ 221,725,820	\$ 221,725,820	\$ 192,419,679	\$ 192,419,679
Securities available for sale	169,250,748	169,250,748	154,656,422	154,656,422
Securities held to maturity	3,308,699	3,442,000	7,111,167	7,296,000
Loans, net	1,632,770,427	1,639,354,000	1,630,757,863	1,644,057,000
Loans held for sale	12,292,863	12,342,000	13,592,523	13,701,000
Federal Home Loan Bank stock	7,959,300	not applicable	7,959,300	not applicable
Interest receivable	5,773,081	5,773,081	6,118,451	6,118,451
Financial liabilities				
Deposits	\$ 1,876,715,151	\$ 1,879,986,000	\$ 1,858,076,694	\$ 1,862,551,000
Federal funds purchased and repurchase agreements	60,302,320	60,302,320	52,494,526	52,494,526
Federal Home Loan Bank advances	5,703,898	6,274,000	16,696,491	17,448,000
Subordinated debentures	38,742,000	32,148,000	38,742,000	34,109,000
Interest payable	605,084	605,084	757,173	757,173

The following is a summary of the fair value estimation methodologies, not previously presented, used by the Company for the financial instruments above:

Cash and cash equivalents and interest receivable and payable are presented at their carrying value, which is a reasonable estimate of their fair value. The fair value of loans is estimated by discounting the future cash flows using market rates currently offered for loans of similar remaining maturities. It is not practicable to determine the fair value of Federal Home Loan Bank stock due to restrictions placed on its transferability.

The fair value of non-interest bearing deposits is the amount payable on demand. The fair value of interest bearing deposits is estimated using market rates currently offered for deposits of similar remaining maturities. The carrying amount is the estimated fair value for federal funds purchased and repurchase agreements that reprice frequently and fully. The fair value of Federal Home Loan Bank advances and the subordinated debentures is estimated based on rates currently available to the Company for borrowings with similar terms and remaining maturities.

The estimated fair value of commitments to extend credit and standby letters of credit is estimated using fees currently charged for similar arrangements and is not material in relation to the consolidated financial statements.

The fair value estimates presented herein are based on pertinent information available to management as of December 31, 2012 and 2011. 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 consolidated financial statements since that date and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

NOTE 11. INCOME TAXES

The provision for income taxes consists of the following:

	<u>2012</u>	<u>2011</u>
Current	\$ 636,761	\$ 2,069,049
Deferred	<u>(691,788)</u>	<u>(2,877,787)</u>
	\$ (55,027)	\$ (808,738)

The tax provision is less than that obtained by using the statutory federal income tax rates due to tax credits generated by Central Bank & Trust Co.'s limited partnership interest in 16 low-income housing projects, two historic renovation projects, two New Market Tax Credit projects, ownership of Qualified Zone Academy Bonds, and tax exempt interest income totaling approximately \$5,009,000 and \$5,923,000 for 2012 and 2011.

Deferred tax assets and liabilities relate principally to unrealized losses on securities available for sale, adjustment for pension obligations, premises and equipment, mortgage servicing rights, the allowance for credit losses, Federal Home Loan Bank stock dividends, fair value adjustments, prepaid pension benefits and net operating loss carryforwards generated by Central Bank of Jefferson County prior to the Company's acquisition. At December 31, 2012, the Company had net operating loss carryforwards of \$3,094,000 which expire in 2025. Deferred tax assets are recognized for net operating losses because the benefit is more likely than not to be realized. The utilization of the net operating loss carryforwards is limited annually under Internal Revenue Code Section 382. The Company's deferred tax assets and deferred tax liabilities at December 31 are as follows:

	<u>2012</u>	<u>2011</u>
Deferred tax assets	\$ 23,400,263	\$ 23,032,145
Deferred tax liabilities	<u>(7,325,082)</u>	<u>(7,368,310)</u>
	\$ 16,075,181	\$ 15,663,835

Included in these deferred tax items are a liability in the amount of \$15,249 as of December 31, 2012 and an asset in the amount of \$77,463 as of December 31, 2011 for the Salt Lick Deposit Bank assets and liabilities held for sale. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. No valuation allowance for the realization of deferred tax assets is considered necessary.

The Company has no unrecognized tax benefits as of December 31, 2012 and 2011. The Company does not expect the total amount of unrecognized tax benefits to significantly increase or decrease in the next 12 months. Should the accrual of any interest or penalties relative to unrecognized tax benefits be necessary, it is the Company's policy to record such accruals in its income tax expense accounts; no such accruals existed as of December 31, 2012 and 2011. The Company and its Subsidiaries file a consolidated U.S. Corporation federal income tax return and the Company and its non-bank Subsidiaries file Kentucky Corporation income tax returns. The federal return is subject to examination by taxing authorities for all years after 2008 and the Kentucky returns are subject to examination by taxing authorities for all years after 2007.

NOTE 12. RETIREMENT PLANS

The Company has a funded noncontributory defined benefit pension plan covering substantially all employees. The plan generally provides pension benefits that are based on compensation levels and years of service. Annual contribution to the plan is made according to established laws and regulations. Plan assets are primarily invested in equity securities, fixed income securities and cash equivalents. The plan provides defined benefits based on years of service and final average salary. The Company uses December 31 as the measurement date for its pension plans. Employees of Salt Lick Deposit Bank who were participants in the funded noncontributory defined benefit pension plan as of December 31, 2012 will continue to participate in the plan after the sale of the bank.

The Company also maintains a non-qualified supplemental pension plan covering certain key executives, which provides for benefit payments that exceed the limit for deductibility imposed by income tax regulations. The benefit obligation related to this unfunded plan was \$2,462,418 and \$2,345,098 at December 31, 2012 and 2011.

During 2009, the Company curtailed these defined benefit plans, fully vesting and freezing benefits for all employees. The Company expects to make no contributions to the plans in 2013.

Information about plan assets, obligations, contributions, and benefits paid follows:

	December 31	
	2012	2011
Benefit obligation	\$ (26,857,751)	\$ (26,605,747)
Fair value of plan assets	<u>27,731,460</u>	<u>27,815,416</u>
Funded status	\$ 873,709	\$ 1,209,669
	2012	2011
Employer contributions	\$ -	\$ -
Benefits paid	2,335,070	137,262

The following benefit payments are expected:

2013	\$ 762,000
2014	300,000
2015	440,000
2016	657,000
2017	887,000
2018–2022	6,331,000

Amounts recognized in accumulated other comprehensive income at December 31 consist of:

	2012	2011
Net actuarial loss	\$ <u>5,917,143</u>	\$ 5,825,051
	\$ 5,917,143	\$ 5,825,051

The accumulated benefit obligation was \$26,857,751 and \$26,605,747 at year end 2012 and 2011.

Components of net periodic pension cost and other amounts recognized in other comprehensive income for 2012 and 2011 for the Company's defined benefit pension plans included the following:

	2012	2011
Service cost – benefits earned during the period	\$ -	\$ -
Interest cost on projected benefit obligation	1,296,843	1,268,585
Expected return on plan assets	(1,357,326)	(1,303,573)
Net amortization of net gain (loss)	304,351	409,955
Net periodic pension cost	<u>243,868</u>	<u>374,967</u>
Net loss (gain)	(678,726)	209,575
Net amortization of net gain (loss)	770,818	(409,955)
Total recognized in other comprehensive income (loss)	<u>92,092</u>	<u>(200,380)</u>
Total recognized in net periodic pension cost and other comprehensive income	\$ 335,960	\$ 174,587

The estimated net gain (loss) for the defined benefit pension plans that will be amortized from accumulated other comprehensive income into net periodic pension cost over the next fiscal year was \$314,400 and \$304,351 as of December 31, 2012 and 2011.

The weighted average assumptions used to determine net periodic pension cost were a discount rate of 4.75% and 5% for 2012 and 2011 and an expected return on plan assets of 4.75% and 5% for 2012 and 2011.

Plan Assets: The Company's overall investment strategy is to achieve a mix of long-term growth and fixed income investments. The target allocations for plan assets are shown in the table below. Equity securities primarily include investments in mutual funds and blue chip stocks. Debt securities include agency securities and municipal securities.

The weighted-average expected long-term rate of return is estimated based on current trends in the plan assets as well as projected future rates of return on those assets. The long-term rate of return considers historical returns.

The Company's pension plan asset allocation at year end 2012 and 2011, target allocation for 2013, and expected long-term rate of return by asset category are as follows:

Asset Category	Target Allocation 2013	Percentage of Plan Assets at Year End		Weighted-Average Expected Long-Term Rate of Return
		2012	2011	
Equity securities	20-25%	26.45%	25.16%	6.00% - 8.00%
Investment funds:				
Mutual funds	10-15%	13.03	20.49	6.00% - 8.00%
Real estate	0-3%	2.06	2.12	6.00% - 8.00%
Debt securities:				
U.S. government agency securities	0-3%	0.01	3.64	4.00%
Obligations of states and political subdivisions	50-55%	58.45	39.94	4.00%
Corporate bonds	0-2%	-	8.65	-
Total		100.00%	100.00%	

Fair Value of Plan Assets: Fair value is the exchange price that would be received for an asset in the principal or most advantageous market for the asset in an orderly transaction between market participants on the measurement date.

The Company used the following methods and significant assumptions to estimate the fair value of each type of financial instrument:

Equity and Debt Securities: The fair values for investment securities are determined by quoted market prices, if available (Level 1). For securities where quoted prices are not available, fair values are calculated based on market prices of similar securities (Level 2). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3). Discounted cash flows are calculated using spread to swap and LIBOR curves that are updated to incorporate loss severities, volatility, credit spread and optionality. During times when trading is more liquid, broker quotes are used (if available) to validate the model. Rating agency and industry research reports as well as defaults and deferrals on individual securities are reviewed and incorporated into the calculations.

The fair value of the plan assets at December 31, 2012 and 2011, by asset category, is as follows:

	Fair Value Measurements at December 31, Using			
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
2012				
Plan assets				
Cash and cash equivalents	\$ 235,000	\$ 235,000	\$ -	\$ -
Equity securities	7,273,000	7,273,000	-	-
Investment funds:				
Mutual funds	3,582,000	3,582,000	-	-
Real estate	567,000	567,000	-	-
Debt securities:				
U.S. government agency securities	1,000	-	1,000	-
Obligations of states and political subdivisions	16,073,000	-	16,073,000	-
Total plan assets	\$27,731,000	\$ 11,657,000	\$ 16,074,000	\$ -
2011				
Plan assets				
Cash and cash equivalents	\$ 210,000	\$ 210,000	\$ -	\$ -
Equity securities	6,945,000	6,945,000	-	-
Investment funds:				
Mutual funds	5,656,000	5,656,000	-	-
Real estate	584,000	584,000	-	-
Debt securities:				
U.S. government agency securities	1,005,000	-	1,005,000	-
Obligations of states and political subdivisions	11,026,000	-	11,026,000	-
Corporate bonds	2,389,000	2,389,000	-	-
Total plan assets	\$ 27,815,000	\$ 15,784,000	\$ 12,031,000	\$ -

There were no transfers between Level 1 and Level 2 during 2012 or 2011.

Deferred Compensation Plans: The Company maintains deferred compensation plans covering selected directors and key employees. Net deferred compensation expense was \$36,970 and \$101,070 in 2012 and 2011. The accrued liability associated with these plans of \$609,629 and \$573,159 at December 31, 2012 and 2011 is included in other liabilities.

Employee Stock Ownership Plan: The Company maintains an employee stock ownership plan (the "ESOP"). Contributions are determined annually by the Board of Directors in amounts not to exceed 15 percent of the total compensation of all participants. ESOP expense was \$609,150 and \$935,028 in 2012 and 2011. As of December 31, 2012 and 2011, a total of 34,579 and 35,139 shares with a fair value of approximately \$13,313,000 and \$14,091,000 were allocated to active participants as well as \$6,400 and \$0 in cash. There were no unallocated shares. Any participant who receives a distribution of Company stock under the ESOP has the option to require the Company to repurchase the shares at fair value during a defined period within each of the succeeding two years. The total "put" obligation at December 31, 2012 is the fair value of all ESOP shares distributed in 2012 and shares to be distributed in 2013 to participants who had terminated as of year-end 2012. The Company has a right of first refusal with respect to distributed ESOP shares, which requires former participants to offer to sell their shares to the Company before selling them to another purchaser.

401(k) Retirement Plan: The Company has a 401(k) retirement plan. The Company determines annually the rate at which employee contributions will be matched and the maximum amount of employee contributions which will be matched. The Company made matching contributions totaling \$1,364,716 and \$1,341,380 in 2012 and 2011.

NOTE 13. REGULATORY MATTERS

The Company is a bank holding company and is subject to regulation by the Federal Reserve. Central Bank & Trust Co., Salt Lick Deposit Bank, and Central Bank of Jefferson County, Inc. operate under state bank charters and are subject to regulation by the Kentucky Department of Financial Institutions and the Federal Deposit Insurance Corporation.

The Company and the Banks are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Banks must meet specific capital guidelines that involve quantitative measures of the Company's and the Banks' assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Company's and the Banks' capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. As of December 31, 2012, Central Bank of Jefferson County, Inc. is required under a regulatory agreement to maintain a Tier I capital to average assets ratio of 8.00 percent. The Bank was in compliance as of that date.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as are asset growth and expansion, and capital restoration plans are required.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Banks to maintain minimum amounts and ratios (set forth in the following table) of Total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital to average assets (as defined). Management believes, as of December 31, 2012 and 2011, that the Company and the Banks meet all capital adequacy requirements to which they are subject. Notification from the Federal Deposit Insurance Corporation as of December 31, 2012 and 2011, categorized the Banks as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the institutions' category.

Actual and required capital amounts and ratios are presented below:

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2012:						
Total Capital (to Risk-Weighted Assets):						
Consolidated	\$218,002,426	12.4%	\$140,183,018	8.0%	N/A	N/A
Central Bank & Trust Co.	188,162,980	12.1	124,630,612	8.0	\$155,788,265	10.0%
Central Bank of Jefferson County, Inc.	17,675,825	11.8	12,021,378	8.0	15,026,722	10.0
Salt Lick Deposit Bank	7,901,009	15.5	4,075,627	8.0	5,094,534	10.0
Tier I Capital (to Risk-Weighted Assets):						
Consolidated	\$196,029,984	11.2%	\$70,091,509	4.0%	N/A	N/A
Central Bank & Trust Co.	168,623,948	10.8	62,315,306	4.0	\$93,472,959	6.0%
Central Bank of Jefferson County, Inc.	15,795,230	10.5	6,010,689	4.0	9,016,033	6.0
Salt Lick Deposit Bank	7,264,151	14.3	2,037,814	4.0	3,056,721	6.0
Tier I Capital (to Average Assets):						
Consolidated	\$196,029,984	9.3%	\$84,721,959	4.0%	N/A	N/A
Central Bank & Trust Co.	168,623,948	8.9	75,894,020	4.0	\$94,867,525	5.0%
* Central Bank of Jefferson County, Inc.	15,795,230	8.7	7,232,695	4.0	9,040,868	5.0
Salt Lick Deposit Bank	7,264,151	10.0	2,895,957	4.0	3,619,946	5.0
December 31, 2011:						
Total Capital (to Risk-Weighted Assets):						
Consolidated	\$206,432,550	11.8%	\$139,464,865	8.0%	N/A	N/A
Central Bank & Trust Co.	177,973,281	11.6	122,988,107	8.0	\$153,735,134	10.0%
Central Bank of Jefferson County, Inc.	17,154,992	11.1	12,315,933	8.0	15,394,917	10.0
Salt Lick Deposit Bank	8,101,892	15.1	4,284,467	8.0	5,355,584	10.0
Tier I Capital (to Risk-Weighted Assets):						
Consolidated	\$184,554,850	10.6%	\$69,732,433	4.0%	N/A	N/A
Central Bank & Trust Co.	158,672,308	10.3	61,494,054	4.0	\$92,241,080	6.0%
Central Bank of Jefferson County, Inc.	15,256,633	9.9	6,157,967	4.0	9,236,950	6.0
Salt Lick Deposit Bank	7,430,127	13.9	2,142,234	4.0	3,213,350	6.0
Tier I Capital (to Average Assets):						
Consolidated	\$184,554,850	8.8%	\$84,402,558	4.0%	N/A	N/A
Central Bank & Trust Co.	158,672,308	8.5	74,837,491	4.0	\$93,546,863	5.0%
* Central Bank of Jefferson County, Inc.	15,256,633	8.8	6,907,190	4.0	8,633,988	5.0
Salt Lick Deposit Bank	7,430,127	9.8	3,027,638	4.0	3,784,548	5.0

*At December 31, 2012 and 2011, Central Bank of Jefferson County, Inc. is required to maintain a Tier I capital to average assets ratio of 8.0%.

As state-chartered banks, Central Bank & Trust Co., Salt Lick Deposit Bank, and Central Bank of Jefferson County, Inc. are subject to the dividend restrictions set forth by Kentucky Revised Statutes. Under such restrictions, state-chartered banks may not pay dividends in excess of year-to-date net income combined with the preceding two years' undistributed net income or loss unless approval from the Kentucky Commissioner of Banking is obtained. Central Bank of Jefferson County, Inc. is restricted from declaring dividends without permission of the regulatory authorities.

Under the most restrictive dividend limitations described, the Central Bank & Trust Co. could pay dividends in 2013 of approximately \$19,035,000 plus any 2013 earnings retained through the date of the dividend declaration.

NOTE 14. FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK

The Banks are parties to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of their customers. The financial instruments are commitments to extend credit, unused lines of credit and standby letters of credit. Such financial instruments are recorded in the consolidated financial statements when they become payable. The Banks use the same credit policies in making conditional obligations as they do for on-balance-sheet instruments.

At December 31, 2012 and 2011, the Banks, including Salt Lick Deposit Bank, had the following financial instruments:

	2012	2011
Standby letters of credit	\$ 33,395,000	\$ 25,094,000
Commitments to extend credit	\$ 127,572,000	\$ 158,417,000
Unused lines of credit	\$ 254,090,000	\$ 229,453,000

Standby letters of credit represent conditional commitments issued by the Banks 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 the credit risk involved in extending loans to customers. The Banks hold certificates of deposit and real estate as collateral supporting those commitments for which collateral is deemed necessary.

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.

Commitments are generally made for periods of 45 days or less. The Banks evaluate each customer's creditworthiness on a case-by-case basis. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Collateral held varies but may include accounts receivable, marketable securities, inventory, property and equipment, and income-producing properties.

NOTE 15 – BUSINESS COMBINATIONS

Salt Lick Deposit Bank Transaction

On October 29, 2012, the Company agreed to sell Salt Lick Deposit Bank ("SLDB") to a non-related third-party financial institution. SLDB's assets and liabilities are presented as assets and liabilities held for sale on the consolidated balance sheets. The sale was consummated on January 1, 2013. The sale price of \$8,630,000 was paid in cash and resulted in a gain, net of tax, of \$196,119.

Management evaluated the assets and liabilities held for sale for impairment as of December 31, 2012. As the transaction resulted in a net gain, management determined there was no impairment and, accordingly, the assets and liabilities held for sale were carried at their historical cost, net of any previously established valuation allowance.

Following are components of SLDB's assets and liabilities as of December 31:

	2012	2011
Cash and cash equivalents	\$ 727,858	\$ 1,068,536
Available for sale securities	2,722,993	2,587,999
Held to maturity securities	487,754	710,028
Loans held for sale in the secondary market	386,656	70,850
Loans	52,238,090	54,734,775
Allowance for credit losses	(640,139)	(857,124)
Premises and equipment, net	2,839,661	2,981,044
Other real estate owned	845,972	846,560
Federal Home Loan Bank stock, at cost	908,400	908,400
Goodwill	691,131	691,131
Other assets	526,380	661,806
Total assets held for sale	\$ 61,734,756	\$ 64,404,005
Deposits	\$ 61,731,020	\$ 60,497,419
Federal Home Loan Bank advances	2,481,555	2,936,815
Other liabilities	109,035	241,839
Total liabilities held for sale	\$ 64,321,610	\$ 63,676,073

SLDB also held \$10,542,985 and \$7,393,235 in intercompany federal funds sold as of December 31, 2012 and 2011. These amounts were eliminated during consolidation.

SLDB's condensed income statements for the years ended December 31, 2012 and 2011 follow:

	<u>2012</u>	<u>2011</u>
Interest and dividend income	\$ 3,092,727	\$ 3,478,400
Interest expense	<u>770,767</u>	<u>1,062,442</u>
Net interest income	<u>2,321,960</u>	<u>2,415,958</u>
Provision for credit losses	<u>101,313</u>	381,000
Noninterest income	<u>716,315</u>	704,837
Noninterest expense	<u>1,981,196</u>	1,932,279
Provision for income taxes	<u>286,742</u>	<u>243,956</u>
Net income	<u>\$ 669,024</u>	<u>\$ 563,560</u>

Central Bank, FSB Transaction

On January 18, 2011, the operations of Central Bank, FSB ("FSB") were merged into Central Bank & Trust Co. ("CB&T"). This transaction was a business combination under common control as both CB&T and FSB are Subsidiaries of the Company. Assets and liabilities were recorded at their carrying amounts in the financial statements. The business combination resulted in gross assets of \$192 million, gross liabilities of \$174 million, and \$18 million in total capital transferred to CB&T's financial statements. The combination did not have an impact on the consolidated balance sheets, or the consolidated statements of income, changes in shareholders' equity and cash flows as of and for the year ended December 31, 2011.

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Mary Littrell
Vice President

Wealth Management

Bill Kaiser
Vice President

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Central Bank & Trust Co.

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(502) 570-2265
100 W. Main Street

SAT 410 Connector Road

LEXINGTON

MAIN OFFICE
(859) 253-6222
300 W. Vine Street
(ATM available in lobby
and drive-thru)

SAT ANDOVER

(859) 253-6127
3101 Maple Leaf Drive

EASTLAND

(859) 253-6063
649 E. New Circle Road

NICHOLASVILLE ROAD

(859) 253-6073
100 E. Reynolds Road

SAT NORTH PARK

(859) 253-6104
515 New Circle Road, NW

SAT PALOMAR CENTRE

(859) 253-6177
3700 Palomar Centre Drive

SAT RICHMOND ROAD

(859) 253-6083
2233 Richmond Road

SIR BARTON, HAMBURG

(859) 253-8760
2443 Sir Barton Way
Suite 175

SAT SOUTHLAND

(859) 253-6053
256 Southland Drive

SAT TATES CREEK CENTRE

(859) 253-6387
4090 Tates Creek Centre Drive

TATES CREEK ROAD

(859) 253-6113
3270 Tates Creek Road

VERSAILLES ROAD

(859) 253-6093
2347 Versailles Road

MADISON COUNTY

SAT BERA

(859) 986-0357
101 Brenwood Street

SAT RICHMOND

(859) 625-6500
350 W. Main Street

SAT NICHOLASVILLE

(859) 885-2282
301 N. Main Street
1471 Keene Road

NORTHERN KENTUCKY

SAT CRESTVIEW HILLS

(859) 905-5580
2850 Turkeyfoot Road

FLORENCE

(859) 647-0222
7310 Turfway Road
Suite 110

SAT FT. MITCHELL

(859) 905-5590
2075 Dixie Highway

WINCHESTER

(859) 744-3972
43 N. Maple Street

SAT 1110 Pioneer Drive

Central Bank of Jefferson County

LOUISVILLE

Hurstbourne Place
(502) 499-5600
9300 Shelbyville Road
Suite 100

SAT TAYLORSVILLE ROAD

(502) 493-2366
4630 Taylorsville Road

WATERFRONT PLAZA

(502) 456-3838
321 W. Main Street

Free-Standing ATM Locations

CENTRAL BAPTIST HOSPITAL
1740 S. Limestone, Lexington

FAYETTE DISTRICT COURT*
150 N. Limestone Street, Lexington

SAINT JOSEPH HOSPITAL
One Saint Joseph Drive, Lexington

WATTERSON TOWER
1930 Bishop Lane, Louisville

RJ CORMAN
AMBULATORY CENTER*
1250 Keene Road, Nicholasville

UK COMMONWEALTH STADIUM*

UK HOSPITAL*
Pavilion A
1000 S. Limestone, Lexington

* Cash machine only

Banking Center Hours for Central Bank & Trust Co.

Lobbies are open Monday through Thursday from 9:00 a.m. to 4:00 p.m. and Friday from 9:00 a.m. to 6:00 p.m.

Our drive-thrus are open 8:00 a.m. to 6:00 p.m.
Monday through Friday.

SAT Saturday hours 9:00 a.m. to 1:00 p.m., as indicated.

Hours may vary by location. Please call for details or
visit centralbank.com for hours and locations.

Whom to Call for More Information

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For account information
or for problem resolution,
call (859) 253-6359
or (800) 637-6884.

MasterCard®/Visa®

For MasterCard®/Visa® account
inquiries or to report
a lost or stolen MasterCard®
or Visa®, call (859) 253-6359.

The Central Card

To report a lost or stolen
card, call (859) 253-6359.

ATM Card

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Central Insurance Services

(859) 253-6283

Central Investment Center

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(859) 253-6246

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(859) 253-6302

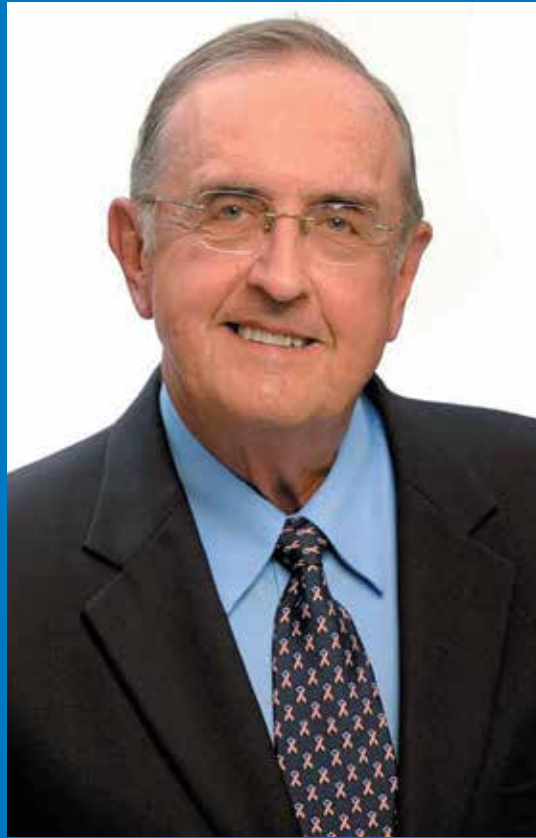
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(859) 253-6001

Web Site

centralbank.com

Note: Products may vary by
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IN MEMORIAM Richard W. Furst

Director, Central Bank & Trust Co. & Central Bancshares, Inc.

We lost a trusted friend and advisor with the death of our associate Dr. Richard W. Furst on May 19, 2012. He was a valued friend who will be dearly missed and whose contributions to the Bank, its Board of Directors, the University of Kentucky, central Kentucky and the entire Commonwealth will be forever remembered and treasured. Since joining our Board, he provided sound advice and expert guidance on a wide variety of business and banking subjects. We will miss his tireless dedication to excellence, his unbending loyalty and his broad vision that served as a beacon of inspiration to all who knew him. He was truly a friend and comrade to all.

Dr. Furst was a member of the Board of Central Bank & Trust Co. and Central Bancshares, Inc., having served since 2003. He was former Dean of the Gatton College of Business and Economics at the University of Kentucky and had been associated with the College of Business at the University of South Carolina and with the University of Missouri-St. Louis. His community service included the boards of Community Ventures, Inc.; Economic Development Planning Commission, Commonwealth of Kentucky; Commerce Lexington; Host Communications; UK Business Partnership Foundation; Office Suites Plus; Foam Design, Inc.; Seed Restaurant Group, Inc.; Armada Funds; and Parkstone Funds.

Dr. Furst was a graduate of Alfred University and held a Doctorate in Business Administration and a Masters in Business Administration from Washington University.

Our deepest sympathy has been extended to his family, including his wife, Janis Hatton Furst, his two children, Pamela Shunk and Stacie Holloway, one sister, Norma Gibson and six grandchildren: Stephen, Meaghan and Katherine Shunk, Ellie Furst and Andrew and Emily Holloway.



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