Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-KSB

x **ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Fiscal Year Ended December 31, 2007

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission File Number 000-51843

ALARION FINANCIAL SERVICES, INC.

(Exact name of registrant as specified in its charter)

Florida **(State or other jurisdiction of incorporation or organization)**	**20-3851373** **(I.R.S. Employer Identification No.)**
One Northeast First Avenue, Ocala, Florida **(Address of principal executive offices)**	**34470** **(Zip Code)**

Registrant's telephone number, including area code: (352) 547-1200

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

Securities registered pursuant to Section 12(g) of the Exchange Act: Common Stock, Par Value $0.01

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the issuer was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES x NO ¨

Check if disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of issuer's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act). (Check one):

Large accelerated filer ¨	Accelerated ¨
Non-accelerated ¨ (Do not check if a smaller reporting company)	Smaller Reporting company x

The issuer's revenues for its most recent fiscal year were $ 13,152,000.

Indicate by check mark whether the issuer is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes ¨ No x

The aggregate market value of the Common Stock of the issuer held by non-affiliates of the issuer (1,855,791 shares) on December 31, 2007, was approximately $18,557,910. As of such date, no organized trading market existed for the Common Stock of the issuer. The aggregate market value was computed by reference the sale price of the Common Stock of the issuer at its last sales price of $10.00 per share. For the purposes of this response, directors, officers and holders of 15.01% or more of the issuer's Common Stock are considered the affiliates of the issuer at that date.

As of January 31, 2008, there were issued and outstanding 2,238,610 shares of the issuer's Common Stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Shareholders to be filed with the Securities and Exchange Commission pursuant to Regulation 14A are incorporated into Part III, Items 9 through 12 and 14 of this Annual Report on Form 10-KSB.

Table of Contents

TABLE OF CONTENTS

PART I

Item 1. Description of Business

Forward-Looking Statements

Some of the statements in this Form 10-KSB discuss future expectations. There may also be statements regarding projections of results of operations or financial condition or state other "forward-looking" information. Those statements are subject to known and unknown risks, uncertainties and other factors that could cause the actual results to differ materially from those contemplated by the statements. We based the forward-looking information on various factors and numerous assumptions, which may or may not turn out to be correct.

Important factors that may cause actual results to differ from those contemplated by forward-looking statements include, for example:

The success or failure of our efforts to implement our business strategy;

The effect of changing economic conditions, both nationally and in our local community;

Changes in government regulations, tax and interest rates applicable to our business and similar matters;

Our ability to attract and retain quality employees; and

Other risks which may be described in our future filings with the SEC.

We do not promise to update forward-looking information to reflect actual results or changes in assumptions or other factors that could affect those statements other than material changes to such information.

General

Alarion Financial Services, Inc. ("AFSI") was incorporated under the laws of the State of Florida on August 16, 2005, for the purpose of becoming a bank holding company by acquiring Alarion Bank ("Bank") (AFSI and the Bank are collectively referred to herein as the "Company"). The Bank is a full-service Florida state chartered commercial bank, providing a wide range of business and consumer financial services in our target marketplace, which is comprised primarily of Marion and Alachua Counties in Florida. The Bank was formed by a group of business leaders, who believed that there was a significant demand for a locally-owned community bank.

Under Federal Reserve Board regulations, AFSI is expected to be a source of financial strength to the Bank. Banking regulations require that the Bank maintain a minimum ratio of capital to assets. In the event that the Bank's growth is such that this minimum ratio is not maintained, AFSI may borrow funds, subject to the capital adequacy guidelines of the Federal Reserve, and contribute them to the capital of the Bank and otherwise raise capital in a manner which is unavailable to the Bank under existing banking regulations.

The Bank commenced business operations on February 28, 2005 in Ocala, Florida. The Bank opened a temporary Gainesville, Florida branch on March 2, 2005, and moved the branch to the permanent facility on September 1, 2005. The Bank opened a second branch in Gainesville on 34 th Street on March 28, 2006. A branch in Alachua, Florida was opened on December 20, 2006 and a second Ocala office opened on June 7, 2007.

The Bank's deposits are insured by the Federal Deposit Insurance Corporation up to applicable limits. The operations of the Bank are subject to the supervision and regulation of the Federal Deposit Insurance Corporation (FDIC) and the Florida Office of Financial Regulation ("Florida Office").

The Bank provides a range of consumer and commercial banking services to individuals, businesses and industries. The basic services offered by the Bank include: demand interest-bearing and non-interest-bearing accounts, money market deposit accounts, NOW accounts, time deposits, credit cards, direct deposits, notary services, money orders, night depository, travelers' checks, cashier's checks, savings bonds, bank drafts, automated teller services, and drive-in tellers. In addition, the Bank makes secured and unsecured commercial, consumer, and real estate loans and issues stand-by letters of credit. The Bank provides automated teller machine (ATM) cards and is a member of the Star ATM network, thereby permitting customers to utilize the convenience of larger ATM networks. In addition to the foregoing services, the offices of the Bank provide customers with extended banking hours. The Bank does not have trust powers and, accordingly, no trust services are provided.

The revenues of the Bank are primarily derived from interest on, and fees received in connection with, real estate and other loans, and from interest and dividends from investment and mortgage-backed securities, and short-term investments. The principal sources of funds for the Bank's lending activities are its deposits, repayment of loans, and the sale and maturity of investment securities. The principal expenses of the Bank are the interest paid on deposits, and operating and general administrative expenses.

As is the case with banking institutions generally, the Bank's operations are materially and significantly influenced by general economic conditions and by related monetary and fiscal policies of financial institution regulatory agencies, including the Board of Governors of the Federal Reserve System (the "Federal Reserve") and the FDIC. Deposit flows and costs of funds are influenced by interest rates on competing investments and general market rates of interest. Lending activities are affected by the demand for financing of real estate and other types of loans, which in turn is affected by the interest rates at which such financing may be offered and other factors affecting local demand and availability of funds. The Bank faces strong competition in the attraction of deposits (its primary source of lendable funds) and in the origination of loans. *See* "Competition."

The Company's fiscal year ends December 31. This Form 10-KSB is also being used as the Bank's Annual Disclosure Statement under Federal Deposit Insurance Corporation ("FDIC") Regulations. This Form 10-KSB has not been reviewed or confirmed for accuracy or relevance by the FDIC.

Critical Accounting Policies

The Company's financial condition and results of operations are sensitive to accounting measurements and estimates of matters that are inherently uncertain. When applying accounting policies in areas that are subjective in nature, the Company must use its best judgment to arrive at the carrying value of certain assets. The most critical accounting policy applied is related to the valuation of the loan portfolio.

A variety of estimates impact carrying value of the loan portfolio including the calculation of the allowance for loan losses, valuation of underlying collateral, the timing of loan charge-offs and the amount and amortization of loan fees and deferred origination costs.

The allowance for loan losses is the most difficult and subjective judgment. The allowance is established and maintained at a level that the Company believes is adequate to cover losses resulting from the inability of borrowers to make required payments on loans. Estimates for loan losses are arrived at by analyzing risks associated with specific loans and the loan portfolio, current trends in delinquencies and charge-offs, the views of regulators, changes in the size and composition of the loan portfolio and peer comparisons. The analysis also requires consideration of the economic climate and direction, change in the interest rate environment, which may impact a borrower's ability to pay, legislation impacting the banking industry and economic conditions specific to its service area. Because the calculation of the allowance for loan losses relies on estimates and judgments relating to inherently uncertain events, results may differ from the Company's estimates.

The allowance for loan losses is also discussed as part of "Management's Discussion and Analysis—Financial Condition" and in Note 3 to the consolidated financial statements. The significant accounting policies are discussed in Note 1 to the consolidated financial statements.

Lending Activities

The Bank offers a range of lending services, including real estate, consumer and commercial loans, to individuals and small businesses and other organizations that are located in or conduct a substantial portion of their business in the Bank's market area. The Bank's net loans at December 31, 2007 were $164 million, or 81% of total assets. The interest rates charged on loans vary with the degree of risk, maturity, and amount of the loan, and are further subject to competitive pressures, money market rates, availability of funds, and government regulations. The Bank has no foreign loans or loans for highly leveraged transactions.

The Bank's loans are concentrated in five major areas: commercial real estate loans, residential real estate loans, construction, commercial loans (for equipment purchases, working capital and various other business purposes) and consumer loans. A majority of the Bank's loans are made on a secured basis. As of December 31, 2007, approximately 90% of the Bank's loan portfolio consisted of loans secured by real estate, of which approximately 49% of the total loan portfolio is secured by commercial properties. Our emphasis is on loans secured by commercial real estate, rather than riskier receivables or business inventory loans. Risks of these types of loans include the general business conditions of the local economy and borrowers' ability to conduct their businesses to generate sufficient profits to repay their loans under the agreed upon terms and conditions. Personal guarantees may be obtained from the principals of business borrowers and third parties to support the borrowers' ability to service the debt and reduce the risk of non-payment. Commercial loans may be made at variable or fixed rates of interest.

Commercial lines of credit are typically granted on a one-year basis, with loan covenants and monetary thresholds. Other commercial loans with terms or amortization schedules of longer than one year may carry interest rates which vary with the prime lending rate and will become payable in full and are generally refinanced in three to five years. Commercial loans not secured by real estate amounted to approximately 8% of the Bank's total loan portfolio as of December 31, 2007.

The Bank's real estate loans are secured by mortgages and consist primarily of loans to individuals and businesses for the purchase, improvement of or investment in real estate and for the construction of single-family residential units or the development of single-family residential building lots. These real estate loans may be made at fixed or variable interest rates. The Bank generally does not make fixed-rate commercial real estate loans for terms exceeding five years. Loans in excess of five years are generally adjustable.

The Bank originates residential real estate loans on one to four family homes to be sold in the secondary market. These loans are to qualified buyers with commitments to purchase from correspondent banks prior to closing. These loans generally are repayable in monthly installments based on up to a 30-year amortization schedule with both fixed and variable interest rates. These loans are typically purchased within thirty days of closing, though the bank does portfolio certain adjustable rate loans generally underwritten to secondary market guidelines.

The Bank's consumer loan portfolio consists primarily of loans to individuals for various consumer purposes, but includes some business purpose loans which are payable on an installment basis. Consumer loans generally involve more risk than mortgage loans because the collateral for a defaulted loan may not provide an adequate source of repayment of the principal. This risk is due to the potential for damage to the collateral or other loss of value, and the fact that any remaining deficiency often does not warrant further collection efforts. The majority of these loans are for terms of less than five years and are secured by liens on various personal assets of the borrowers, but consumer loans may also be made on an unsecured basis. Consumer loans are made at fixed and variable interest rates, and are often based on up to a five-year amortization schedule.

Loan originations are derived from a number of sources. Loan originations can be attributed to direct solicitation by the Bank's loan officers, existing customers and borrowers, advertising, walk-in customers and, in some instances, referrals from brokers.

Certain credit risks are inherent in making loans. These include prepayment risks, risks resulting from uncertainties in the future value of collateral, risks resulting from changes in economic and industry conditions, and risks inherent in dealing with individual borrowers. In particular, longer maturities increase the risk that economic conditions will change and adversely affect collectibility. The Bank attempts to minimize credit losses through various means. In particular, on larger credits, the Bank generally relies on the cash flow of a debtor as the source of repayment and secondarily on the value of the underlying collateral. In addition, the Bank attempts to utilize shorter loan terms in order to reduce the risk of a decline in the value of such collateral.

We attempt to mitigate these risks through our underwriting process and the requirement that loans be secured by collateral. With regard to commercial loans, we require that borrowers provide current financial information. Such documentation should include a complete itemized balance sheet with supporting schedules for listed asset values, fiscal year-end operating statements and income tax returns. Businesses are also typically required to provide us with copies of annual reports if prepared by outside accounting firms. Loan and renewals to businesses are not considered until the required financial documents are compiled and thoroughly reviewed by our lending staff.

Loans to commercial establishments are typically secured by inventory, equipment, supplies, accounts receivable and any other asset of value that relates to the business' operations. Lines of credit and loans secured by accounts receivable and/or inventory are monitored periodically by our staff. Loans secured by "all business assets," or a "blanket lien" are typically made only by high quality borrowers, due to the non-specific nature of the collateral. Valuation of business collateral must be supported by a valuation, purchase order, or third party physical inspection. Should we not be able to obtain any of these items, the loan is then considered unsecured. Personal guarantees of the principals of business borrowers are required in instances where we deem it necessary or appropriate depending on the business' assets or other financial indicators.

All loans to businesses must have a clearly stated and reasonable payment plan that allows for timely retirement of debt. Revolving lines of credit are occasionally granted to credit worthy businesses for the purpose of carrying current assets, such as inventory or accounts receivable, and are structured to coincide with the seasonal or natural business cycle of the borrower. We do not provide such lines to be used as a substitute for permanent equity capital of a borrower. All lines are reviewed not less than annually and must be paid in full and out of use at least annually for a period determined at the time of approval or renewal.

Loans secured by real estate primarily fall into three categories: (i) commercial, (ii) construction and (iii) residential. These real estate loans are secured by liens on commercial or residential real property or made for the purpose of financing the construction of a building or other improvements to real estate, regardless of whether any lien position has been perfected on the property. All real estate financing products are provided on a non-discriminatory basis throughout our lending area.

Our underwriting takes into consideration the amount financed, term, amortization and pricing, as well as all relevant borrower credit factors. Basic credit factors include the borrower's overall creditworthiness, debt service capacity and secondary sources of repayment. Underwriting standards relevant to real estate financing also address market valuation of the mortgaged property, the level of the borrower's equity or proposed ownership capital investment, projected income producing property revenue and overall property marketability. In almost all instances, we require a first or second lien on the real estate which secures the loan. In cases where we have accepted a second, or more junior lien, we require an estoppel letter from the senior lien holders. We also typically require a title insurance policy insuring our interest in the real estate collateral. We require independent appraisals on all assets valued at over $250,000.

We typically make consumer loans to purchase automobiles, boats, recreational equipment and mobile homes. Prior to making such loans, we require the borrower to complete an application and we confirm the information contained therein prior to committing funds. We grant or deny consumer loan requests based on the customer's ability to meet scheduled payments and the quality of offered collateral. We value collateral based on standard guidelines (i.e. National Automobile Dealer Association listings for used cars). All consumer loans must have a clearly stated and reasonable payment plan that allows for timely repayment of debt.

On occasion, we also make unsecured loans. We underwrite each unsecured loan based on the borrower's and any guarantor's cash flow and past credit history. In addition, we limit the terms of such unsecured extension of credit to one year for commercial loans and three years for consumer loans. With respect to sources of repayment, we require identification of primary and secondary sources to help ensure retirement of debts on schedule. Furthermore, we obtain borrower's financial data and income tax returns to document favorable net-worth-to-debt ratios and sufficient liquidity to repay the debts in a timely fashion.

Loan Loss Allowance

In considering the adequacy of our allowance for loan losses, the Bank has considered that as of December 31, 2007, approximately 49% of outstanding loans are in the commercial real estate loan category. At December 31, 2007, commercial loans including commercial real estate represented 57% of our loan portfolio. Commercial loans are generally considered by management as having greater risk than other categories of loans in our loan portfolio. We believe that the real estate collateral securing our commercial real estate loans reduces the risk of loss inherently present in commercial loans.

At December 31, 2007, our consumer loan portfolio consisted primarily of lines of credit and installment loans secured by automobiles and other consumer goods. We believe that the risk associated with these types of loans has been adequately provided for in the loan loss allowance.

The Bank's Board of Directors monitors the loan portfolio monthly in order to evaluate the adequacy of the allowance for loan losses. In addition to reviews by regulatory agencies, the Bank engages the services of outside consultants to assist in the evaluation of credit quality and loan administration. These professionals complement our internal system, which identifies potential problem credits as early as possible, categorizes the credits as to risk and includes a reporting process to monitor the progress of the credits.

The allowance for loan losses is established through a provision for loan losses charged to expenses. Loans are to be charged off against the allowance when management believes the collectibility of principal is unlikely. In addition, loss experience will be monitored in establishing the provision. During the year ended December 31, 2007, no loans were charged off against the allowance for loan losses.

Deposit Activities

Deposits are the major source of the Bank's funds for lending and other investment activities. The Bank considers the majority of its regular savings, demand, NOW and money market deposit accounts to be core deposits. These accounts comprised approximately 29% of the Bank's total deposits at December 31, 2007. Approximately 71% of the Bank's deposits at December 31, 2007 were time deposits. Generally, the Bank attempts to maintain the rates paid on its deposits at a competitive level. Time deposits of $100,000 and over made up approximately 30% of the Bank's total deposits at December 31, 2007. The majority of the deposits of the Bank are generated from Alachua and Marion County.

Investments

The Bank invests a portion of its assets in U.S. Government agency obligations, mortgage-backed securities, and federal funds sold. The Bank's investments are managed in relation to loan demand and deposit growth, and are generally used to provide for the investment of excess funds at minimal risks while providing liquidity to fund increases in loan demand or to offset fluctuations in deposits.

With respect to the Bank's investment portfolio, the Bank's total portfolio may be invested in U.S. Treasury and general obligations of its agencies and bank-qualified municipal securities because such securities generally represent a minimal investment risk. Occasionally, the Bank may purchase certificates of deposit of national and state banks. Mortgage-backed securities generally have a shorter life than the stated maturity. Federal funds sold is the excess cash the Bank has available over and above daily cash needs. This money is invested on an overnight basis with approved correspondent banks.

The Bank monitors changes in financial markets. In addition to investments for its portfolio, the Bank monitors its daily cash position to ensure that all available funds earn interest at the earliest possible date. A portion of the investment account is designated as secondary reserves and invested in liquid securities that can be readily converted to cash with minimum risk of market loss. These investments usually consist of U.S. Treasury obligations, U.S. government agencies and federal funds. The remainder of the investment account may be placed in investment securities of different type and longer maturity. Daily surplus funds are sold in the federal funds market for one business day. The Bank attempts to stagger the maturities of its securities so as to produce a steady cash-flow in the event the Bank needs cash, or economic conditions change to a more favorable rate environment.

Correspondent Banking

Correspondent banking involves one bank providing services to another bank which cannot provide that service for itself from an economic or practical standpoint. The Bank is required to purchase correspondent services offered by larger banks, including check collections, purchase of federal funds, security safekeeping, investment services, coin and currency supplies, overline and liquidity loan participations and sales of loans to or participation with correspondent banks.

The Bank sells loan participations to correspondent banks with respect to loans which exceed the Bank's lending limit.

Effect of Governmental Policies

The earnings and business of the Bank are and will be affected by the policies of various regulatory authorities of the United States, especially the Federal Reserve. The Federal Reserve, among other things, regulates the supply of credit and deals with general economic conditions within the United States. The instruments of monetary policy employed by the Federal Reserve for these purposes influence in various ways the overall level of investments, loans, other extensions of credit and deposits, and the interest rates paid on liabilities and received on assets.

Interest and Usury

The Bank is subject to numerous state and federal statutes that affect the interest rates that may be charged on loans. These laws do not, under present market conditions, deter the Bank from continuing the process of originating loans.

Supervision and Regulation

Banks and their holding companies, and many of their affiliates, are extensively regulated under both federal and state law. The following is a brief summary of certain statutes, rules, and regulations affecting the Company and the Bank. This summary is qualified in its entirety by reference to the particular statutory and regulatory provisions referred to below and is not intended to be an exhaustive description of the statutes or regulations applicable to the business of the Company and the Bank. Supervision, regulation, and examination of banks by regulatory agencies are intended primarily for the protection of depositors, rather than shareholders.

Bank Holding Company Regulation. The Holding Company is a bank holding company, registered with the Federal Reserve under the BHC Act. As such, the Company is subject to the supervision, examination and reporting requirements of the BHC Act and the regulations of the Federal Reserve. The BHC Act requires that a bank holding company obtain the prior approval of the Federal Reserve before (i) acquiring direct or indirect ownership or control of more than 5% of the voting shares of any bank, (ii) taking any action that causes a bank to become a subsidiary of the bank holding company, or (iii) merging or consolidating with any other bank holding company.

The BHC Act further provides that the Federal Reserve may not approve any transaction that would result in a monopoly or would be in furtherance of any combination or conspiracy to monopolize or attempt to monopolize the business of banking in any section of the United States, or the effect of which may be substantially to lessen competition or to tend to create a monopoly in any section of the country, or that in any other manner would be in restraint of trade, unless the anticompetitive effects of the proposed transaction are clearly outweighed by the public interest in meeting the convenience and needs of the community to be served. The Federal Reserve is also required to consider the financial and managerial resources and future prospects of the bank holding companies and banks concerned and the convenience, and needs of the community to be served. Consideration of financial resources generally focuses on capital adequacy and consideration of convenience and needs issues includes the parties' performance under the Community Reinvestment Act of 1977 (the "CRA"), both of which are discussed below.

Banks are subject to the provisions of the CRA. Under the terms of the CRA, the appropriate federal bank regulatory agency is required, in connection with its examination of a bank, to assess such bank's record in meeting the credit needs of the community served by that bank, including low- and moderate-income neighborhoods. The regulatory agency's assessment of the bank's record is made available to the public. Further, such assessment is required of any bank which has applied to:

- charter a bank,

- obtain deposit insurance coverage for a newly chartered institution,
- establish a new branch office that will accept deposits,
- relocate an office, or
- merge or consolidate with, or acquire the assets or assume the liabilities of, a federally regulated financial institution

In the case of a bank holding company applying for approval to acquire a bank or other bank holding company, the Federal Reserve will assess the record of each subsidiary bank of the applicant bank holding company, and such records may be the basis for denying the application.

The BHC Act generally prohibits a bank holding company from engaging in activities other than banking, or managing or controlling banks or other permissible subsidiaries, and from acquiring or retaining direct or indirect control of any company engaged in any activities other than those activities determined by the Federal Reserve to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. In determining whether a particular activity is permissible, the Federal Reserve must consider whether the performance of such an activity can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest, or unsound banking practices. For example, factoring accounts receivable, acquiring or servicing loans, leasing personal property, conducting securities brokerage activities, performing certain data processing services, acting as agent or broker in selling credit life insurance and certain other types of insurance in connection with credit transactions, and certain insurance underwriting activities have all been determined by regulations of the Federal Reserve to be permissible activities of bank holding companies. Despite prior approval, the Federal Reserve has the power to order a holding company or its subsidiaries to terminate any activity or terminate its ownership or control of any subsidiary, when it has reasonable cause to believe that continuation of such activity or such ownership or control constitutes a serious risk to the financial safety, soundness, or stability of any bank subsidiary of that bank holding company.

Gramm-Leach-Bliley Act. In 1999, the Gramm-Leach-Bliley Act was enacted which reforms and modernizes certain areas of financial services regulation. The law permits the creation of new financial services holding companies that can offer a full range of financial products under a regulatory structure based on the principle of functional regulation. The legislation eliminates the legal barriers to affiliations among banks and securities firms, insurance companies, and other financial services companies. The law also provides financial organizations with the opportunity to structure these new financial affiliations through a holding company structure or a financial subsidiary. The new law reserves the role of the Federal Reserve Board as the supervisor for bank holding companies. At the same time, the law also provides a system of functional regulation which is designed to utilize the various existing federal and state regulatory bodies. The law also sets up a process for coordination between the Federal Reserve Board and the Secretary of the Treasury regarding the approval of new financial activities for both bank holding companies and national bank financial subsidiaries.

The law also includes a minimum federal standard of financial privacy. Financial institutions are required to have written privacy policies that must be disclosed to customers. The disclosure of a financial institution's privacy policy must take place at the time a customer relationship is established and not less than annually during the continuation of the relationship. The act also provides for the functional regulation of bank securities activities. The law repeals the exemption that banks were afforded from the definition of "broker," and replaces it with a set of limited exemptions that allow the continuation of some historical activities performed by banks. In addition, the act amends the securities laws to include banks within the general definition of dealer. Regarding new bank products, the law provides a procedure for handling products sold by banks that have securities elements. In the area of the Community Reinvestment Act activities, the law generally requires that financial institutions address the credit needs of low-to-moderate income individuals and neighborhoods in the communities in which they operate. Bank regulators are required to take the Community Reinvestment Act ratings of a bank or of the bank subsidiaries of a holding company into account when acting upon certain branch and bank merger and acquisition applications filed by the institution. Under the law, financial holding companies and banks that desire to engage in new financial activities are required to have satisfactory or better Community Reinvestment Act ratings when they commence the new activity.

Bank Regulation. The Bank is chartered under the laws of Florida and their deposits are insured by the FDIC to the extent provided by law. The Bank is subject to comprehensive regulation, examination and supervision by the FDIC and the Florida Office and to other laws and regulations applicable to banks. Such regulations include limitations on loans to a single borrower and to its directors, officers and employees; restrictions on the opening and closing of branch offices; the maintenance of required capital ratios; the granting of credit under equal and fair conditions; and the disclosure of the costs and terms of such credit. The Bank is examined periodically by the FDIC and the Florida Office, to whom it submits periodic reports regarding its financial condition and other matters. The FDIC and the Florida Office have a broad range of powers to enforce regulations under their jurisdiction, and to take discretionary actions determined to be for the protection and safety and soundness of banks, including the institution of cease and desist orders and the removal of directors and officers. The FDIC and the Florida Office also have the authority to approve or disapprove mergers, consolidations, and similar corporate actions.

There are various statutory limitations on the ability of the Bank to pay dividends. The FDIC also has the general authority to limit the dividend payment by banks if such payment may be deemed to constitute an unsafe and unsound practice.

Under federal law, federally insured banks are subject, with certain exceptions, to certain restrictions on any extension of credit to their parent holding companies or other affiliates, on investment in the stock or other securities of affiliates, and on the taking of such stock or securities as collateral from any borrower. In addition, banks are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit or the providing of any property or service.

The Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA") imposed major regulatory reforms, stronger capital standards for savings and loan associations and stronger civil and criminal enforcement provisions. FIRREA also provides that a depository institution insured by the FDIC can be held liable for any loss incurred by, or reasonably expected to be incurred by, the FDIC in connection with:

- the default of a commonly controlled FDIC insured depository institution; or
- any assistance provided by the FDIC to a commonly controlled FDIC insured institution in danger of default

The FDIC Improvement Act of 1991 ("FDICIA") made a number of reforms addressing the safety and soundness of deposit insurance funds, supervision, accounting, and prompt regulatory action, and also implemented other regulatory improvements. Annual full-scope, on-site examinations are required of all insured depository institutions. The cost for conducting an examination of an institution may be assessed to that institution, with special consideration given to affiliates and any penalties imposed for failure to provide information requested. Insured state banks also are precluded from engaging as principal in any type of activity that is impermissible for a national bank, including activities relating to insurance and equity investments. The Act also recodified current law restricting extensions of credit to insiders under the Federal Reserve Act.

Also important in terms of its effect on banks has been the deregulation of interest rates paid by banks on deposits and the types of deposit accounts that may be offered by banks. Most regulatory limits on permissible deposit interest rates and minimum deposit amounts expired several years ago. The effect of the deregulation of deposit interest rates generally has been to increase the costs of funds to banks and to make their costs of funds more sensitive to fluctuations in money market rates. A result of the pressure on banks interest margins due to deregulation has been a trend toward expansion of services offered by banks and an increase in the emphasis placed on fee or noninterest income.

Capital Requirements. Bank regulatory agencies require financial institutions to maintain capital at adequate levels based on a percentage of assets and off balance sheet exposures, adjusted for risk weights ranging from 0% to 100%. Under the risk-based standard, capital is classified into two tiers. Tier 1 capital consists of common shareholders' equity, excluding the unrealized gain (loss) on available-for-sale securities, minus certain intangible assets. Tier 2 capital consists of the general allowance for credit losses except for certain limitations. An institution's qualifying capital base for purposes of its risk-based capital ratio consists of the sum of its Tier 1 and Tier 2 capital. The regulatory minimum requirements are 4% for Tier 1 and 8% for total risk-based capital. Bank holding companies and banks are also required to maintain capital at a minimum level based on total assets, which is known as the leverage ratio. The minimum requirement for the leverage ratio is 3%, but all but the highest rated institutions are required to maintain ratios 100 to 200 basis points above the minimum. At December 31, 2007 the Bank met all capital requirements to which they were subject.

For additional information regarding the Company's capital ratios and requirements, see "Management's Discussion and Analysis - Capital Resources, Commitments and Capital Requirements" and notes to the consolidated financial statements.

FDICIA contains "prompt corrective action" provisions pursuant to which banks are to be classified into one of five categories based upon capital adequacy, ranging from "well capitalized" to "critically undercapitalized" and which require (subject to certain exceptions) the appropriate federal banking agency to take prompt corrective action with respect to an institution which becomes "significantly undercapitalized" or "critically undercapitalized."

The FDIC has issued regulations to implement the "prompt corrective action" provisions of FDICIA. In general, the regulations define the five capital categories as follows:

- an institution is "well capitalized" if it has a total risk-based capital ratio of 10% or greater, has a Tier 1 risk-based capital ratio of 6% or greater, has a leverage ratio of 5% or greater and is not subject to any written capital order or directive to meet and maintain a specific capital level for any capital measures;

- an institution is “adequately capitalized” if it has a total risk-based capital ratio of 8% or greater, has a Tier 1 risk-based capital ratio of 4% or greater, and has a leverage ratio of 4% or greater;
- an institution is “undercapitalized” if it has a total risk-based capital ratio of less than 8%, has a Tier 1 risk-based capital ratio that is less than 4% or has a leverage ratio that is less than 4%;
- an institution is “significantly undercapitalized” if it has a total risk-based capital ratio that is less than 6%, a Tier 1 risk-based capital ratio that is less than 3% or a leverage ratio that is less than 3%; and
- an institution is “critically undercapitalized” if its “tangible equity” is equal to or less than 2% of its total assets.

The FDIC also, after an opportunity for a hearing, has authority to downgrade an institution from “well capitalized” to “adequately capitalized” or to subject an “adequately capitalized” or “undercapitalized” institution to the supervisory actions applicable to the next lower category, for supervisory concerns.

Generally, FDICIA requires that an “undercapitalized” institution must submit an acceptable capital restoration plan to the appropriate federal banking agency within 45 days after the institution becomes “undercapitalized” and the agency must take action on the plan within 60 days. The appropriate federal banking agency may not accept a capital restoration plan unless, among other requirements, each company having control of the institution has guaranteed that the institution will comply with the plan until the institution has been adequately capitalized on average during each of the three consecutive calendar quarters and has provided adequate assurances of performance. The aggregate liability under this provision of all companies having control of an institution is limited to the lesser of:

- 5% of the institution’s total assets at the time the institution becomes “undercapitalized” or
- the amount which is necessary, or would have been necessary, to bring the institution into compliance with all capital standards applicable to the institution as of the time the institution fails to comply with the plan filed pursuant to FDICIA.

An “undercapitalized” institution may not acquire an interest in any company or any other insured depository institution, establish or acquire additional branch offices or engage in any new business unless the appropriate federal banking agency has accepted its capital restoration plan, the institution is implementing the plan, and the agency determines that the proposed action is consistent with and will further the achievement of the plan, or the appropriate Federal banking agency determines the proposed action will further the purpose of the “prompt corrective action” sections of FDICIA.

If an institution is “critically undercapitalized,” it must comply with the restrictions described above. In addition, the appropriate Federal banking agency is authorized to restrict the activities of any “critically undercapitalized” institution and to prohibit such an institution, without the appropriate Federal banking agency’s prior written approval, from:

- entering into any material transaction other than in the usual course of business;

- engaging in any covered transaction with affiliates (as defined in Section 23A(b) of the Federal Reserve Act);
- paying excessive compensation or bonuses; and
- paying interest on new or renewed liabilities at a rate that would increase the institution's weighted average costs of funds to a level significantly exceeding the prevailing rates of interest on insured deposits in the institution's normal market areas.

The "prompt corrective action" provisions of FDICIA also provide that in general no institution may make a capital distribution if it would cause the institution to become "undercapitalized." Capital distributions include cash (but not stock) dividends, stock purchases, redemptions, and other distributions of capital to the owners of an institution.

Additionally, FDICIA requires, among other things, that:

- only a "well capitalized" depository institution may accept brokered deposits without prior regulatory approval and
- the appropriate federal banking agency annually examine all insured depository institutions, with some exceptions for small, "well capitalized" institutions and state-chartered institutions examined by state regulators. FDICIA also contains a number of consumer banking provisions, including disclosure requirements and substantive contractual limitations with respect to deposit accounts.

As of December 31, 2007, the Bank met the capital requirements of a "well capitalized" institution. Bank holding companies are not subject to "prompt corrective action" of FDICIA.

The FDIC has proposed revising its risk-based capital requirements to ensure that such requirements provide for explicit consideration by commercial banks of interest rate risk. Under the proposed rule, a bank's interest rate risk exposure would be quantified using either the measurement system set forth in the proposal or the bank's internal model for measuring such exposure, if such model is determined to be adequate by the bank's examiner. If the dollar amount of a bank's interest rate risk exposure, as measured by either measurement system, exceeds 1% of the bank's total assets, the bank would be required under the proposed rule to hold additional capital equal to the dollar amount of the excess. It is anticipated that the regulatory agencies will issue a revised proposed rule for further public comment. Pending issuance of such revised proposal, the Bank's management cannot determine what effect, if any, an interest rate risk component would have on the capital of the Bank.

<u>Enforcement Powers</u>. Congress has provided the federal bank regulatory agencies with an array of powers to enforce laws, rules, regulations and orders. Among other things, the agencies may require that institutions cease and desist from certain activities, may preclude persons from participating in the affairs of insured depository institutions, may suspend or remove deposit insurance, and may impose civil money penalties against institution-affiliated parties for certain violations.

<u>Maximum Legal Interest Rates</u>. Like the laws of many states, Florida law contains provisions on interest rates that may be charged by banks and other lenders on certain types of loans. Numerous exceptions exist to the general interest limitations imposed by Florida law. The

relative importance of these interest limitation laws to the financial operations of the Bank will vary from time to time, depending on a number of factors, including conditions in the money markets, the costs and availability of funds, and prevailing interest rates.

Bank Branching. Banks in Florida are permitted to branch state wide. Such branch banking, however, is subject to prior approval by the FDIC and the Florida Office. Any such approval would take into consideration several factors, including the bank's level of capital, the prospects and economics of the proposed branch office, and other conditions deemed relevant by the FDIC and the Florida Office for purposes of determining whether approval should be granted to open a branch office.

Change of Control. Federal law restricts the amount of voting stock of a bank holding company and a bank that a person may acquire without the prior approval of banking regulators. The overall effect of such laws is to make it more difficult to acquire a bank holding company and a bank by tender offer or similar means than it might be to acquire control of another type of corporation. Consequently, shareholders of the Bank may be less likely to benefit from the rapid increases in stock prices that may result from tender offers or similar efforts to acquire control of other companies. Federal law also imposes restrictions on acquisitions of stock in a bank holding company and a state bank. Under the federal Change in Bank Control Act and the regulations thereunder, a person or group must give advance notice to the Federal Reserve before acquiring control of any bank holding company (such as the Company). Upon receipt of such notice, the Federal Reserve may approve or disapprove the acquisition. The Change in Bank Control Act creates a rebuttable presumption of control if a member or group acquires a certain percentage or more of a bank holding company's or state bank's voting stock, or if one or more other control factors set forth in the Act are present.

Interstate Banking. The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1996, provides for nationwide interstate banking and branching. Under the law, interstate acquisitions of banks or bank holding companies in any state by bank holding companies in any other state will be permissible one year after enactment. Interstate branching and consolidation of existing bank subsidiaries in different states is permissible. Florida has a law that allows out-of-state bank holding companies (located in states that allow Florida bank holding companies to acquire banks and bank holding companies in that state) to acquire Florida banks and Florida bank holding companies. The law essentially provides for out-of-state entry by acquisition only (and not by interstate branching) and requires the acquired Florida bank to have been in existence for at least two years.

Sarbanes-Oxley Act of 2002. In 2002, the Sarbanes-Oxley Act of 2002 was enacted. The Securities and Exchange Commission (the "SEC") has promulgated certain regulations pursuant to the Act that will continue to impose additional implementing or clarifying regulations as necessary in furtherance of the Act. The passage of the Act and the regulations implemented by the SEC subject publicly-traded companies to additional and more extensive reporting regulations and disclosure. Compliance with the Act and corresponding regulations will increase the Company's expenses.

Effect of Governmental Policies. The earnings and businesses of the Bank are affected by the policies of various regulatory authorities of the United States, especially the Federal Reserve. The Federal Reserve, among other things, regulates the supply of credit and deals with general economic conditions within the United States. The instruments of monetary policy employed by the Federal Reserve for those purposes influence in various ways the overall level of investments, loans, other extensions of credit, and deposits, and the interest rates paid on liabilities and received on assets.

USA Patriot Act

The terrorist attacks in September 2001, have led to the adoption of the *Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001*, commonly known as the *USA Patriot Act*. Part of the *USA Patriot Act* is the *International Money Laundering Abatement and financial Anti-Terrorism Act of 2001*. This act requires the Secretary of the Treasury, in consultation with the heads of other government agencies, to adopt special measures applicable to financial institutions. These measures include enhanced recordkeeping and reporting requirements for certain financial transactions that are of primary money laundering concern, due diligence requirements concerning the beneficial ownership of certain types of accounts, and restrictions or prohibitions on certain types of accounts with foreign financial institutions. Among its other provision, this law requires each financial institution to: (i) establish an anti-laundering program; (ii) establish due diligence policies, procedures and controls with respect to private banking accounts and correspondent banking accounts involving foreign individuals and certain foreign banks; and (iii) avoid establishing, maintaining, administering, or managing correspondent accounts in the United States for, or on behalf of, a foreign bank that does not have a physical presence in this country. In addition, the law contains a provision encouraging cooperation among financial institutions, regulatory authorities and law enforcement authorities with respect to individuals, entities and organizations engaged in, or reasonably suspected of engaging in, terrorist acts or money laundering activities. The law expands the circumstances under which funds in a bank account may be forfeited and requires covered financial institutions to respond under certain circumstances to requests for information from federal banking agencies within 120 hours.

Other Laws

The Bank's loans will also be subject to federal laws applicable to credit transactions, such as the following (including the rules and regulations of various federal agencies charged with the responsibility of implementing such federal laws):

- *Federal Truth-in-Lending Act* – governs disclosures of credit terms to consumer borrowers;
- *Home Mortgage Disclosure Act* – requires financial institutions to provide information to enable public officials to determine whether a financial institution is fulfilling its obligations to meet the housing needs of the community it serves;
- *Equal Credit Opportunity Act* – prohibits discrimination on the basis of race, creed or other prohibitive factors in extending credit;
- *Real Estate Settlement Procedures Act* – requires lenders to disclose certain information regarding the nature and cost of real estate settlements, and prohibits certain lending practices, as well as limits escrow account amounts in real estate transactions; and
- *Fair Credit Reporting Act* – governs the manner in which consumer debts may be collected by collection agencies.

The Company and the Bank's operations are also subject to the:

- *Right to Financial Privacy Act* – imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial record; and

- *Electronic Funds Transfer Act and Regulation E* – governs automatic deposits to, and withdrawals from, deposit accounts and customer's rights and liabilities arising from the use of debit cards, automated teller machines and other electronic banking services.

Liquidity

A Florida-chartered commercial bank is expected to maintain an adequate liquidity reserve. The liquidity reserve may consist of cash on hand, cash on demand deposit with correspondent banks and other investments and short-term marketable securities, such as federal funds sold and United States securities or securities guaranteed by the United States.

Competition

The Company encounters strong competition both in making loans and in attracting deposits. The deregulation of the banking industry and the widespread enactment of state laws which permit multi-bank holding companies as well as an increasing level of interstate banking have created a highly competitive environment for commercial banking. In one or more aspects of its business, the Company competes with other commercial banks, savings and loan associations, credit unions, finance companies, mutual funds, insurance companies, brokerage and investment banking companies, and other financial intermediaries. Most of these competitors, some of which are affiliated with bank holding companies, have substantially greater resources and lending limits, and may offer certain services that the Company does not currently provide. In addition, many of the Company's non-bank competitors are not subject to the same extensive federal regulations that govern bank holding companies and federally insured banks. Recent federal and state legislation has heightened the competitive environment in which financial institutions must conduct their business, and the potential for competition among financial institutions of all types has increased significantly.

To compete, the Company relies upon specialized services, responsive handling of customer needs, and personal contacts by its officers, directors, and staff. Large multi-branch banking competitors tend to compete primarily by rate and the number and location of branches while smaller, independent financial institutions tend to compete primarily by rate and personal service.

Employees

As of December 31, 2007, the Company and the Bank collectively had 54 full-time employees (including executive officers) and 4 part-time employees. The employees are not represented by a collective bargaining unit. The Company considers relations with employees to be good.

Item 2. Description of Properties

The following table sets forth information on the Bank's offices as of December 31, 2007.

Table of Contents

Location	Facility Status
Headquarters & Main Office One Northeast First Avenue Ocala, Florida	Leased by Bank
Gainesville Branch Office 4373 Newberry Road Gainesville, Florida	Owned by Bank
34th Street Branch Office 4200 SW 34th Street Gainesville, Florida	Owned by Bank
Alachua Branch 16404 NW 174th Drive Alachua, Florida	Owned by Bank
17th Street Branch Office 2510 SE Maricamp Road Ocala, Florida	Owned by Bank

None of these properties are encumbered by any liens or mortgages. Other than in the ordinary course of the Bank's lending and investment business, the Company does not invest in real estate or real estate mortgages. Such activities are described in "Description of Business" and "Management's Discussion and Analysis."

Item 3. Legal Proceedings

As of December 31, 2007, neither the Company nor the Bank was a party to any legal proceedings.

Item 4. Submission of Matters to a Vote of Security Holders

None

PART II

Item 5. Market for the Registrant's Common Equity and Related Stockholder Matters

There is no public market for the Common Stock and only isolated, privately negotiated sales of Common Stock have occurred since the Bank opened for business in February 2005, and AFSI became a bank holding company by acquiring the Bank on November 16, 2005. There is no established public trading market for the Common Stock and, historically, the shares of Common Stock have been inactively traded. Management of the Company is aware of certain transactions in its Common Stock, although the trading prices and number of shares transferred in all transactions are not known. The last known trade occurred at $10.00 per share. On December 31, 2007, AFSI had approximately 681 shareholders of record.

Neither the Bank nor AFSI has paid any cash dividends on shares of their Common Stock. AFSI does not intend to pay dividends for the foreseeable future. If at any time the Board of Directors of AFSI determines to pay dividends, such payment will depend upon several factors including AFSI’s earnings, financial condition and capital needs, the impact of legislation and regulations as then in effect or as may be proposed, economic conditions, and such other factors as the Board may deem relevant. Further, dividend payments by AFSI are restricted by statute. AFSI’s ability to make dividend payments also is subject to AFSI and the Bank meeting on a continuing basis all of their capital requirements and achieving and continuing profitable operations. There can be no assurance that future capital or earnings of the Bank will support dividend payments. No assurance can be given that dividends will be paid or, if paid, what the amount of dividends will be or whether such dividends, once paid, will continue.

The primary source of funds for payment of dividends by AFSI will be dividends received from the Bank. Payments by the Bank to AFSI are limited by law and regulations of the bank regulatory authorities. There are various statutory and contractual limitations on the ability of the Bank to pay dividends to AFSI. The FDIC and the Florida Office also have the general authority to limit the dividends paid by banks if such payment may be deemed to constitute an unsafe and unsound practice. Under Florida law applicable to banks and subject to certain limitations, after charging off bad debts, depreciation and other worthless assets, if any, the board of directors of a bank may declare a dividend of up to the bank’s aggregate net income for the current year combined with any retained earnings for the preceding two years as the board shall deem to be appropriate and, with the approval of the Florida Office, may declare a dividend from retained earnings for prior years. No dividends may be paid at a time when a bank’s net earnings from the preceding two years is a loss, or which would cause the capital accounts of the bank to fall below the minimum amount required by law, regulation, order, or any written agreement with the Florida Office or a federal regulatory agency.

Florida law applicable to companies (including the Company) provides that dividends may be declared and paid only if, after giving it effect, (i) the company is able to pay its debts as they become due in the usual course of business, and (ii) the company’s total assets would be greater than the sum of its total liabilities plus the amount that would be needed if the company were to be dissolved at the time of the dividend to satisfy the preferential rights upon dissolution of shareholders whose preferential rights are superior to those receiving the dividend.

AFSI did not repurchase any of its shares in 2007.

The following table sets forth information about the number of shares reserved for issuance under the 2005 Stock Plan as of December 31, 2007.

	Number of securities to be issued upon exercise of outstanding options	Weighted average exercise price of outstanding options	Number of securities remaining available for future issuance
Plans approved by security holders	253,808	$ 10.13	57,685
Equity compensation plans not approved by security holders (1)	0	$ 0	0
Total	253,808	$ 10.13	57,685

Item 6. Management's Discussion and Analysis

SELECTED FINANCIAL DATA

The following table presents selected financial data for the Company. The data for the fiscal year 2005 is derived from audited financial statements of the Company (Bank prior to reorganization). The selected financial data should be read in conjunction with, and are qualified in their entirety by, the financial statements and the notes thereto and the other information included elsewhere herein. Selected financial data for the organizational phase in 2004 prior to the Bank opening is immaterial and therefore not presented.

SELECTED CONSOLIDATED FINANCIAL DATA AT DECEMBER 31, OR FOR THE YEAR THEN ENDED

($ in thousands, except per share amounts)

	2007	2006	2005
Total assets	$203,404	139,444	72,227
Loans, net	164,051	106,289	44,529
Cash and cash equivalents	3,638	6,734	10,900
Securities held to maturity	—	—	10,308
Securities-Available for Sale	20,537	13,837	—
Deposits	164,243	109,072	57,086
Borrowed funds	17,807	15,339	703
Stockholders' equity	20,251	14,337	13,791
Interest income	$ 12,063	6,934	1,781
Interest expense	6,819	3,703	725
Net interest income	5,244	3,231	1,056
Provision for loan losses	701	781	564
Net interest income after provision for loan losses	4,543	2,450	492
Noninterest income	1,089	933	185
Noninterest expense	5,580	3,945	2,464
Earnings (loss) before income tax benefit	52	(562)	(1,787)
Income tax expense (benefit)	49	(199)	(778)
Net earnings (loss)	3	(363)	(1,009)
Basic and diluted loss per share	—	(.23)	(.67)

SELECTED CONSOLIDATED FINANCIAL RATIOS AND OTHER DATA:

	2007	2006	2005
Return on average assets	0.00%	(0.33)%	(2.17)%
Return on average equity	0.02%	(2.63)%	(7.30)%
Dividend payout ratio	N/A	N/A	N/A
Average equity to average assets	10.54%	12.61%	29.66%
Total equity to total assets	9.96%	10.28%	19.09%

Yield on average earning assets (1)	7.12%	6.99%	5.05%
Net interest margin	3.10%	3.26%	2.89%
Nonperforming assets to total assets (2)	N/A	N/A	N/A
Nonperforming loans to total loans (2)	N/A	N/A	N/A
Allowance for loan losses to gross loans	1.23%	1.25%	1.26%
Noninterest expenses to average assets	3.08%	3.60%	5.29%
Operating efficiency ratio (3)	88.11%	94.74%	198.55%
Net interest income to noninterest expenses	93.98%	81.90%	42.86%
Total shares outstanding	2,183,485	1,607,140	1,514,200
Book value per common share outstanding	$ 9.27	$ 8.92	$ 9.11
Number of banking offices (all full-service)	5	4	2

(1) Reflects interest income as a percent of average interest earning assets.
(2) Non-performing loans consist of nonaccrual loans and accruing loans contractually past due ninety days or more.
(3) Noninterest expense divided by the sum of net interest income plus noninterest income.

General

AFSI was incorporated on August 16, 2005 for the purpose of operating as a one-bank holding company. AFSI currently owns 100% of the outstanding shares of the Bank (collectively, the “Company”). AFSI’s only business is the ownership and operation of the Bank. The Bank is a Florida-chartered commercial bank which opened for business on February 28, 2005. The Bank’s deposits are insured by the Federal Deposit Insurance Corporation. The Bank provides community banking services to business and individuals from its banking offices located in Ocala, Gainesville and Alachua, Florida.

The Bank’s deposits are insured by the Federal Deposit Insurance Corporation up to applicable limits. The operations of the Bank are subject to the supervision and regulation of the FDIC and the Florida Office of Financial Regulation.

Historically, the Bank’s market area has been served both by large banks headquartered out of state as well as a number of community banks offering a higher level of personal attention, recognition and service. The large banks have generally applied a transactional business approach, based upon volume considerations, to the market while community banks have traditionally offered a more service relationship approach. Recent mergers and acquisitions have created an opportunity for the Bank. The Bank’s strategic focus is to exploit this opportunity by catering to the “displaced bank customer” in this marketplace.

The Bank provides a range of consumer and commercial banking services to individuals, businesses and industries. The basic services offered by the Bank include: demand interest bearing and noninterest bearing accounts, money market deposit accounts, NOW accounts, time deposits, safe deposit services, credit cards, debit cards, direct deposits, notary services, money orders, night depository, travelers’ checks, cashier’s checks, domestic collections, savings bonds, bank drafts, automated teller services, drive-in tellers, banking by mail and the full range of consumer loans, both collateralized and uncollateralized. In addition, the Bank makes secured and unsecured commercial and real estate loans and issues stand-by letters of credit. The Bank provides automated teller machine (ATM) cards and is a member of the Star ATM network thereby permitting customers to utilize the convenience of the Bank’s ATM network and Star member machines both nationwide and internationally. The Bank does not have trust powers and, accordingly, no trust services are provided.

The Bank's target market is owner occupied and non owner occupied commercial real estate, small businesses, developers, consumers and professionals. The small business customer (typically a commercial entity with sales of $10 million or less) has the opportunity to generate significant revenue for banks yet is generally underserved by large bank competitors. These customers generally can afford profitability opportunities more than the average retail customer.

The Bank has actively pursued its targeted market for deposits, particularly the small businesses and professionals. In today's environment, the product of every system itself becomes a sales tool. Recognizing that fact, the Bank endeavors to offer current technology to the marketplace. Such technology includes debit cards, internet banking and voice response account information systems. The goal is to provide a "high tech - high touch" experience.

The Bank has capitalized upon its market strategy to grow rapidly. As of December 31, 2007, the Bank had grown to approximately $203 million in total assets, $164 million in deposits, and $164 million in net loans. The Bank attributes its successful growth to its location in a dynamic growth area and its focus on its targeted market.

The revenues of the Bank are primarily derived from interest on, and fees received in connection with, real estate and other loans, from interest and dividends from investment securities, service charge income generated from demand accounts and ATM fees, and other services. The principal sources of funds for the Bank's lending activities are its deposits, loan repayments, and proceeds from investment securities. The principal expenses of the Bank are the interest paid on deposits, and operating and general administrative expenses.

Lending Activities

The Bank's loans are concentrated in commercial and real estate loans. A majority of the Bank's loans are made on a secured basis, and, as of December 31, 2007, approximately 90% of the loan portfolio consisted of loans secured by first or second mortgages on residential or commercial real estate.

The Bank's real estate loans are secured by mortgages and consist primarily of loans to individuals and businesses for the purchase, construction of, improvement of or investment in real estate, or for various other consumer and business purposes (whether or not related to the real estate securing them). The Bank also engages in lending to individuals and builders for the construction of single-family residences. These real estate loans may be made at fixed or variable interest rates. The Bank generally makes commercial real estate loans repayable in monthly installments based on up to a 20-year amortization schedule which become payable in full for terms generally five years or less. The Bank's residential real estate loans generally are repayable in monthly installments based on up to a 30-year amortization schedule with variable interest rates. Fixed rate residential loans are available and are subsequently sold on the secondary market.

The Bank also makes non-real estate commercial loans which include loans to individuals and small-to-medium sized businesses and professionals located primarily in Marion and Alachua Counties for working capital, equipment purchases, and various other business purposes. A majority of these commercial loans are secured by inventory, equipment or similar assets, but these loans may also be made on an unsecured basis. Commercial loans may be made at variable or fixed rates of interest; typically, those loans which will have terms or amortization schedules of longer than one year will carry interest rates which vary with the prime lending rate and are generally refinanced or become payable in full in three to five years.

The Bank's installment loan portfolio consists primarily of loans to individuals for various consumer purposes, but includes some business purpose loans which are payable on an installment basis. The majority of these loans are for terms of less than five years and are secured by liens on various personal assets of the borrowers, but installment loans also may be made on an unsecured basis. Installment loans are made at fixed and variable interest rates, and may be made based on up to a ten-year amortization schedule.

For additional information regarding the Bank's loan portfolio, *see* "Page 25 Loan Portfolio" and "Page 3 Lending Activities" and footnote 3 to the consolidated financial statements.

Liquidity

Liquidity management involves the ability to meet the cash flow requirements of customers who may be either depositors wanting to withdraw their funds or borrowers needing assurance that sufficient funds will be available to meet their credit needs. In the ordinary course of business, the Bank's cash flows are generated from deposits, interest and fee income, as well as from loan repayments and the sale, repayments or maturity of securities available-for-sale. In addition to cash and due from banks, the Bank considers all securities available-for-sale and federal funds sold as primary sources of asset liquidity. Many factors affect the ability to accomplish these liquidity objectives successfully, including the economic environment, the asset/liability mix within the balance sheet, as well as the Bank's reputation in the community. The Bank's principal sources of funds are net increases in deposits, principal and interest payments on loans and proceeds from sales, calls and maturities of securities. The Bank used its capital resources primarily to fund existing and continuing loan commitments and to purchase securities. At December 31, 2007, the Bank had commitments to originate loans totaling $9 million, and had issued standby letters of credit of $906,000. At December 31, 2007, the Bank also had commitments to extend credit under the undisbursed portion of outstanding lines of credit of $35 million. Scheduled maturities of certificates of deposit during the twelve months following December 31, 2007 totaled $91 million. Management believes that the Bank has adequate resources to fund all its commitments, that substantially all of its existing commitments will be funded in the subsequent twelve months and, if so desired, that it can adjust the rates on certificates of deposit and other deposit accounts to retain deposits in a changing interest rate environment.

Capital Resources, Commitments and Capital Requirements

The Company's principal sources of funds are those generated by the Bank, including net increases in deposits and other borrowings, principal and interest payments on loans, and proceeds from maturities of investment securities.

The Company uses its capital resources principally to fund existing and continuing loan commitments and to purchase investment securities. Off-balance sheet commitments to extend credit, which amounted to $9 million at December 31, 2007, represent legally binding agreements to lend to customers with fixed expiration dates or other termination clauses. Since many commitments are expected to expire without being funded, committed amounts do not necessarily represent future cash requirements.

The following table summarizes the Company's contractual obligations, including certain on-balance sheet and off-balance sheet obligations, at December 31, 2007 (in thousands):

	Payments Due by Period				
Contractual Obligations	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
Time deposit maturities	$116,152	90,865	16,346	8,941	—
FHLB advances	13,000	—	—	—	13,000
Other borrowings	4,807	4,807	—	—	—
Loan commitments	9,111	9,111	—	—	—
Standby letters of credit	906	906	—	—	—
Undisbursed line of credit loans	35,199	6,314	4,083	6,223	18,579
Total	$179,175	112,003	20,429	15,164	31,579

Management believes that the Company has adequate resources to fund all its commitments and that the Company can adjust the rates and terms on time deposits and other deposit accounts to retain or obtain new deposits in a changing interest rate environment.

The Company's stockholders' equity was $20 million at December 31, 2007, 9.9% of total assets.

The federal banking regulatory authorities have adopted certain "prompt corrective action" rules with respect to depository institutions. The rules establish five capital tiers: "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized," and "critically undercapitalized." The various federal banking regulatory agencies have adopted regulations to implement the capital rules by, among other things, defining the relevant capital measures for the five capital categories. An institution is deemed to be "well capitalized" if it has a total risk-based capital ratio of 10% or greater, a Tier 1 risk-based capital ratio of 6% or greater, and a Tier 1 leverage ratio of 5% or greater and is not subject to a regulatory order, agreement, or directive to meet and maintain a specific capital level. At December 31, 2007, the Bank met the capital ratios of a "well capitalized" financial institution with a total risk-based capital ratio of 11.52% Tier 1 risk-based capital ratio of 10.39%, and a Tier 1 leverage ratio of 9.20%. Depository institutions which fall below the "adequately capitalized" category generally are prohibited from making any capital distribution, are subject to growth limitations, and are required to submit a capital restoration plan. There are a number of requirements and restrictions that may be imposed on institutions treated as "significantly undercapitalized" and, if the institution is "critically undercapitalized," the banking regulatory agencies have the right to appoint a receiver or conservator.

The following table summarizes the regulatory capital levels and ratios for the Bank:

At December 31, 2007:	Actual Bank Ratios	Regulatory Requirement For Well Capitalized Bank
Total capital to risk-weighted assets	11.52%	10.0%
Tier I capital to risk-weighted assets	10.39%	6.0%
Tier I capital to average assets - leverage ratio	9.20%	5.0%

Loan Portfolio

A significant source of the Bank's income is the interest earned on its loan portfolio. At December 31, 2007, the Bank's total assets were $203 million and its net loans receivable were $164 million or 81% of total assets.

The Bank's primary market area consists of the Central Florida region (consisting primarily of Marion and Alachua Counties and surrounding areas). The Bank's market area's economic base is diversified. Significant industries include agribusiness and manufacturing, service enterprises, technology and information concerns. Adverse conditions in any one or more of the industries operating in such markets or a slow-down in general economic conditions could have an adverse effect on the Bank.

Lending activities are conducted pursuant to a written policy which has been adopted by the Bank. Each loan officer has defined lending authority beyond which loans, depending upon their type and size, must be reviewed and approved by a loan committee comprised of certain officers and directors of the Bank.

Table of Contents

The composition of the Bank's loan portfolio was as follows ($ in thousands):

	December 31, 2007 Amount	2007 % of Total	2006 Amount	2006 % of Total	2005 Amount	2005 % of Total
Commercial real estate	$ 80,652	48.6%	$ 58,146	54.2%	$26,626	59.3%
Residential real estate and home equity	28,784	17.4%	16,527	15.4%	5,784	12.8%
Construction	39,722	24.0%	18,611	17.3%	7,079	15.8%
Commercial loans	13,889	8.4%	12,751	11.9%	4,979	11.1%
Consumer	2,699	1.6%	1,308	1.2%	456	1.0%
Total loans	165,746	100.0%	107,343	100.0%	44,924	100.0%
Less: Allowance for loan losses	(2,046)		(1,345)		(564)	
Deferred loan costs, net	351		291		169	
Loans receivable, net	$164,051		$106,289		$44,529	

Maturities of Loans. The following table shows the contractual maturities of the Bank's loan portfolio at December 31, 2007. Loans with scheduled maturities (based on only contract term) are reported in the maturity category in which the payment is due. Demand loans with no stated maturity and overdrafts, if any, are reported in the "due one year or less" category. Loans that have adjustable rates are shown as amortizing to final maturity rather than when the interest rates are next subject to change. The table does not include prepayment or scheduled principal repayments (in thousands):

Type of Loan	Due in 1 Year or Less	Due After 1 to 5 Years	Due After 5 Years	Total
Commercial Real Estate	$31,461	26,587	22,604	80,652
Residential Real Estate and Home Equity	1,873	6,101	20,810	28,784
Construction	12,704	10,998	16,020	39,722
Commercial	6,175	3,273	4,441	13,889
Consumer	1,415	1,177	107	2,699
Total	$53,628	48,136	63,982	165,746

For the above loans due after one year or more, the following is a presentation of an analysis of sensitivities to changes in interest rates at December 31, 2007 (in thousands):

Type of Loan	Fixed Interest Rate	Floating Interest Rate	Total
Commercial Real Estate	$17,232	31,959	49,191
Residential Real Estate and Home Equity	6,365	20,546	26,911
Construction	15,459	11,559	27,018
Commercial	2,735	4,979	7,714
Consumer	1,203	81	1,284
Total	$42,994	69,124	112,118

Loan Quality

Management seeks to maintain a high quality of loans through sound underwriting and lending practices. As of December 31, 2007, approximately 90% of the total loan portfolio was collateralized by commercial and residential real estate mortgages. The level of non-performing loans and real estate owned also is relevant to the credit quality of a loan portfolio. As of December 31, 2007, there were no non-performing loans (those 90 days or more past due).

The commercial real estate mortgage loans in the Bank's portfolio consist of fixed and adjustable-interest rate loans which were originated at prevailing market interest rates. The Bank's policy has been to originate commercial real estate mortgage loans predominantly in its primary market area. Commercial real estate mortgage loans are generally made in amounts up to 80% of the appraised value of the property securing the loan and entail significant additional risks compared to residential mortgage loans. In making commercial real estate loans, the Bank primarily considers the net operating income generated by the real estate to support the debt service, the financial resources and income level and managerial expertise of the borrower, the marketability of the collateral and the Bank's lending experience with the borrower.

Unlike residential mortgage loans, which generally are made on the basis of the borrower's ability to make repayment from his employment and other income and which are collateralized by real property whose value tends to be more readily ascertainable, commercial loans typically are underwritten on the basis of the borrower's ability to make repayment from the cash flow of their business and generally are collateralized by business assets, such as accounts receivable, equipment and inventory. As a result, the availability of funds for the repayment of commercial loans may be substantially dependent on the success of the business itself, which is subject to adverse conditions in the economy. Further, the collateral underlying the loans may depreciate over time, cannot be appraised with as much precision as real estate, and may fluctuate in value based on the success of the business.

Construction loans are made to businesses and individuals to acquire land and construct improvements. These improvements can be both structural like homes and commercial buildings, or could be roads for such things as residential subdivisions. Repayment generally comes from the sale of the property, or occasionally, from permanent financing. The bank underwrites these loans carefully, reviewing such areas as the selling market, contracts on the property, surrounding development trends, overall market trends and most importantly, the ability of the borrower to service the debt for an extended time if necessary. These loans are secured with mortgages on the real estate and enhanced with other loan terms.

The Bank makes consumer and personal loans on a collateralized and noncollateralized basis. These loans are often collateralized by automobiles, recreational vehicles and mobile homes. Consumer and personal loans also are generated by the Bank. Such loans generally have a term of 60 months or less.

Loan concentrations are defined as amounts loaned to a number of borrowers engaged in similar activities which would cause them to be similarly impacted by economic or other conditions. The Bank, on a routine basis, monitors these concentrations in order to consider adjustments in its lending practices to reflect economic conditions, loan to deposit ratios, and industry trends. As of December 31, 2007, loans collateralized with mortgages on real estate represented 90% of the loan portfolio and were to borrowers in varying activities and businesses.

The Loan Committee of the Board of Directors of the Bank concentrates its efforts and resources, and that of its senior management and lending officers, on loan review and underwriting procedures. Internal controls include ongoing reviews of loans made to monitor documentation and the existence and valuations of collateral. In addition, management of the Bank has established a review process with the objective of identifying, evaluating, and initiating necessary corrective action for marginal loans. The goal of the loan review process is to address classified and non-performing loans as early as possible.

Classification of Assets and Potential Problem Loans

Generally, interest on loans accrues and is credited to income based upon the principal balance outstanding. It is management's policy to discontinue the accrual of interest income and classify a loan as non-accrual when principal or interest is past due 90 days or more unless, in the determination of management, the principal and interest on the loan are well collateralized and in the process of collection, or when in the opinion of management, principal or interest is not likely to be paid in accordance with the terms of the obligation. Consumer installment loans are generally charged-off after 90 days of delinquency unless adequately collateralized and in the process of collection. Loans are not returned to accrual status until principal and interest payments are brought current and future payments appear reasonably certain. Interest accrued and unpaid at the time a loan is placed on nonaccrual status is charged against interest income.

Real estate acquired by the Bank as a result of foreclosure or by deed in lieu of foreclosure is classified as other real estate owned ("OREO"). OREO properties are recorded at the lower of cost or fair value less estimated selling costs, and the estimated loss, if any, is charged to the allowance for credit losses at the time it is transferred to OREO. Further write-downs in OREO are recorded at the time management believes additional deterioration in value has occurred and are charged to noninterest expense. As of December 31, 2007, the Company had no OREO.

The Bank has adopted Statements of Financial Accounting Standards No. 114 and 118. These Statements address the accounting by creditors for impairment of certain loans and generally require the Bank to identify loans, for which the Bank probably will not receive full repayment of principal and interest, as impaired loans. The Statements require that impaired loans be valued at the present value of expected future cash flows, discounted at the loan's effective interest rate, or at the observable market price of the loan, or the fair value of the underlying collateral if the loan is collateral dependent. The Bank has implemented the Statements by including in its quarterly review of the adequacy of the allowance for credit losses, to also identify and value impaired loans in accordance with guidance in the Statements. No loans were deemed to be impaired under the Bank's policy at December 31, 2007.

At December 31, 2007, the Bank had no accruing loans which were contractually past due 90 days or more as to principal and interest and no troubled debt restructurings as defined by Statement of Financial Accounting Standards No. 15.

Classified Assets. Federal regulations and the Bank's policy require the classification of loans and other assets, such as debt and equity securities, considered to be of lesser quality as "substandard", "doubtful" or "loss" assets. An asset would be considered "substandard" if it is inadequately protected by the current net worth and paying capacity of the obligator or of the collateral pledged, if any. "Substandard" assets include those characterized by the "distinct possibility" that the institution will sustain "some loss" if the deficiencies are not corrected. Assets that would be classified as "doubtful" have all of the weaknesses inherent in those classified "substandard," with the added characteristic that the weaknesses present make "collection or liquidation in full", on the basis of currently existing facts, conditions, and values, "highly questionable and improbable." Assets that would be classified as "loss", are those considered "uncollectible" and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted. In addition, the Bank's policies require that assets which do not currently expose the insured institution to sufficient risk to warrant classification as substandard but possess other weaknesses are designated "special mention" by management.

At December 31, 2007, loan balances totaling $4,125,691 were classified as Special Mention. There were no concentrations of loans exceeding 10% of total loans which has not been disclosed as a category of loans.

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

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

If an asset is impaired, the estimated fair value of the asset would be determined and if that value is loss than the then carrying value of the asset, the difference would be established as a specific reserve. If an asset is classified as loss, the amount of the asset classified as loss would be reserved. General reserves or general valuation allowances represent loss allowances which have been established to recognize the inherent risk associated with lending activities but, unlike specific reserves, are not allocated to particular assets.

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

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer and residential real estate and home equity loans for impairment disclosures.

The allowance for loan losses totaled approximately $2,046,000 at December 31, 2007, and there were no loans charged-off since the Bank began operations. Considering the nature of the Bank's loan portfolio, management believes that the allowance for loan losses at December 31, 2007, was adequate.

The Bank's general allowance for possible loan losses was allocated using peer group averages and actual loss experiences of peers, as follows (in thousands):

	At December 31,					
	2007		2006		2005	
	Amount	% of Loans to Total Loans	Amount	% of Loans to Total Loans	Amount	% of Loans to Total Loans
At the end of year allocated to:						
Commercial	$ 208	8.4%	$ 183	11.9%	$ 75	11.0%
Commercial real estate	1,060	48.6%	809	54.2%	352	59.3%
Residential real estate and home equity	139	17.4%	79	15.4%	23	12.9%
Construction	593	24.0%	252	17.3%	106	15.8%
Consumer	46	1.6%	22	1.2%	8	1.0%
Total	$2,046	100.0%	$1,345	100.0%	$ 564	100.0%

Investment Securities

At December 31, 2007 the Bank's investment portfolio has been classified as Available-for-Sale with no securities classified as Held-to-Maturity. The portfolio was previously classified as Held-for-Maturity until reclassified on December 29, 2006. The following table sets forth the carrying amount of the Bank's investment portfolio ($ in thousands):

	At December 31, 2007	2006	2005
Available-for-Sale:			
Mortgage-backed securities	$ 5,496	$ 1,856	—
U.S. Government agency securities	15,041	11,981	—
Total securities available for sale	$20,537	$13,837	—
Held to maturity:			
Mortgage-backed securities	—	—	$ 2,319
U.S. Government agency securities	—	—	7,989
Total securities held to maturity	—	—	$10,308
Federal Home Loan Bank stock	$ 836	$ 595	$ 35
Federal funds sold	$ 1,730	$ 3,848	$ 8,371
Interest-earning deposits	$ 103	$ 105	$ 121
Interest-bearing time deposits in Banks	$ 2,046	$ 1,000	$ —

The carrying amount and weighted average yields for investments at December 31, 2007 are shown below ($ in thousands):

Maturing In	Mortgage Backed	U.S. Government Agency Securities	Total	Weighted Average Yields (1)
Due in Less than 1 year	$ —	5,008	5,008	4.84%
After 1 through 5 years	—	10,033	10,033	5.15%
After 5 through 10 years	—	—	—	—
Mortgage backed securities	5,496	—	5,496	5.09%
Total	$ 5,496	15,041	20,537	5.04%

(1) All securities are listed at actual yield and not on a tax equivalent basis. No securities are tax exempt.

The Bank has adopted Statement of Financial Accounting Standards No. 115 (“FAS 115”), which requires companies to classify investments securities, including mortgage-backed securities as either held-to-maturity or available-for-sale. Securities classified as held-to-maturity are carried at amortized cost. Securities classified as available-for-sale are reported at fair value, with unrealized gains and losses, net of tax effect, reported as a separate component of stockholders’ equity. As of December 31, 2007, none of the Bank’s securities were classified as Held-to-Maturity.

Deposit Activities

Deposits are the major source of the Bank’s funds for lending and other investment purposes. Deposits are attracted principally from within the Bank’s primary market area through the offering of a broad variety of deposit instruments including checking accounts, money market accounts, regular savings accounts, term certificate accounts (including “jumbo” certificates in denominations of $100,000 or more) and retirement savings plans. The distribution by type of the Bank’s deposit accounts, was as follows ($ in thousands):

	December 31,					
	2007		2006		2005	
	Amount	% of Deposits	Amount	% of Deposits	Amount	% of Deposits
Noninterest-bearing deposits	$ 13,159	8.0	$ 9,615	8.8	$ 9,335	16.4
Money-market accounts	28,433	17.3	24,687	22.6	16,010	28.1
NOW	5,630	3.5	4,581	4.2	3,369	5.8
Savings	869	.5	659	0.6	1,048	1.8
Subtotal	$ 48,091	29.3	39,542	36.2	29,762	52.1
Time deposits:						
1.00-1.99%	—	—	—	—	349	.6
2.00-2.99%	21	—	104	.1	171	.3
3.00-3.99%	542	.3	487	.4	5,581	9.8
4.00-4.99%	24,977	15.2	25,501	23.4	18,701	32.8
5.00-5.99%	90,211	54.9	43,028	39.5	2,522	4.4
6.00-6.99%	401	.3	410	.4	—	—
Total time deposits	$116,152	70.7	$ 69,530	63.8	27,324	47.9
Total deposits	$164,243	100.0	$109,072	100.0	$57,086	100.0

Maturity terms, service fees and withdrawal penalties are established by the Bank on a periodic basis. The determination of rates and terms is predicated on funds acquisition and liquidity requirements, rates paid by competitors, growth goals and federal regulations.

FDIC regulations limit the ability of certain insured depository institutions to accept, renew, or rollover deposits by offering rates of interest which are significantly higher than the prevailing rates of interest on deposits offered by other insured depository institutions having the same type of charter in such depository institutions' normal market area. Under these regulations, "well capitalized" depository institutions may accept, renew, or roll over deposits at such rates without restriction, "adequately capitalized" depository institutions may accept, renew or roll over deposits at such rates with a waiver from the FDIC (subject to certain restrictions on payments of rates), and "undercapitalized" depository institutions may not accept, renew or roll over deposits at such rates. The regulations contemplate that the definitions of "well capitalized," "adequately capitalized" and "undercapitalized" will be the same as the definitions adopted by the agencies to implement the prompt corrective action provisions of applicable law. *See* "Supervision, Regulation and Governmental Policy – Capital Requirements." As of December 31, 2007, the Bank met the definition of a "well capitalized" depository institution.

The Bank does not have a concentration of deposits from any one source, the loss of which would have a material adverse effect on the Bank. Management believes that substantially all of the Bank's depositors are residents in its primary market area.

The Company also utilizes customer funds in the CDARS program, which allows customers to obtain full FDIC insurance and has the Bank offer offsetting certificates of deposit in participating banks. These deposits from other banks count as brokered deposits and totaled $9.9 million as of December 31, 2007.

Time deposits of $100,000 and over, public fund deposits and other large deposit accounts tend to be short-term in nature and more sensitive to changes in interest rates than other types of deposits and, therefore, may be a less stable source of funds. In the event that existing short-term deposits are not renewed, the resulting loss of the deposited funds could adversely affect the Bank's liquidity. In a rising interest rate market, such short-term deposits may prove to be a costly source of funds because their short-term nature facilitates renewal at increasingly higher interest rates, which may adversely affect the Bank's earnings. However, the converse is true in a falling interest-rate market where such short-term deposits are more favorable to the Bank.

As of December 31, 2007, time deposits of $100,000 and over mature as follows (in thousands):

Due in three months or less	$14,917
Due from three months to six months	10,738
Due from six months to one year	12,562
Due over one year	10,068
Total	$48,285

Borrowings

During 2007, the Company entered into short-term borrowing arrangements with customers consisting of securities sold under repurchase agreements. The agreements are on a demand basis and call for the payment of interest based on the federal funds rate.

The following summarizes these borrowings as of December 31, 2007 ($ in thousands):

Balance outstanding at year-end	$4,807
Average balance outstanding during the year	$5,445
Average interest rate paid	4.53%
Maximum amount outstanding at any month-end during year	$7,001

The Bank has available short term fed funds lines to meet short term liquidity needs. A line of $4,000,000 is available with the Independent Bankers Bank of Florida and $4,500,000 is available with Silverton Bank. There were no borrowings under these lines in 2007.

The Bank also has an agreement with the Federal Home Loan Bank of Atlanta to borrow and has drawn funds of $5,000,000 during 2007. An advance outstanding at December 31, 2007 in the amount of $2,000,000 with an original maturity of December 22, 2007 was paid off in early 2007. The Bank pledges its loan portfolio as collateral. There were three advances in 2007. The maturity and interest rate of the Federal Home Loan Bank ("FHLB") advances are as follows at December 31, 2007 ($ in thousands):

Advance	Maturity	Interest Rate	Amount
5/23/06	2016	4.47%	$5,000
8/30/06	2016	4.71%	3,000
5/18/07	2017	4.22%	5,000

The two advances with 2016 maturity dates have call features benefiting the issuer with call dates of May 23, 2008 and August 29, 2008, respectively. The advance with a 2017 maturity has a call date of May 19, 2008.

Results of Operations

Net interest income, which constitutes the principal source of income for the Bank, represents the excess of interest income on interest-earning assets over interest expense on interest-bearing liabilities. The principal interest-earning assets are federal funds sold, investment securities and loans receivable. Interest-bearing liabilities primarily consist of time deposits, interest-bearing checking accounts ("NOW accounts"), savings deposits and money-market accounts. Funds attracted by these interest-bearing liabilities are invested in interest-earning assets. Accordingly, net interest income depends upon the volume of average interest-earning assets and average interest-bearing liabilities and the interest rates earned or paid on them.

The following table sets forth, information regarding (i) the total dollar amount of interest and dividend income of the Company from interest-earning assets and the resultant average yields; (ii) the total dollar amount of interest expense on interest-bearing liabilities and the resultant average costs; (iii) net interest income; (iv) interest-rate spread; and (v) net interest margin; and (vi) weighted average yields and rates. Yields and costs were derived by dividing annualized income or expense by the average balance of assets or liabilities. There were no non-accrual loans or tax exempt income for the period indicated. The yields and costs include the amortization of fees which are considered to constitute adjustments to yields ($ in thousands).

	December 31,								
	2007			2006			2005		
	Average Balance	Interest and Dividends	Average Yield/ Rate	Average Balance	Interest and Dividends	Average Yield/ Rate	Average Balance	Interest and Dividends	Average Yield/ Rate
Interest-earning assets:									
Loans	$138,018	$10,453	7.57%	$ 72,206	$ 5,652	7.83%	$19,916	1,104	6.59%
Securities	16,477	968	5.87%	14,802	737	4.98%	3,773	122	3.84%
Other(1)	14,876	642	4.32%	12,194	545	4.47%	16,128	555	3.44%
Total interest-earning assets	169,371	12,063	7.12%	99,202	6,934	6.99%	39,817	1,781	5.05%
Noninterest-earning assets	11,685			10,400			6,769		
Total Assets	$181,056			$109,602			$46,586		
Interest-bearing liabilities:									
Savings, NOW and MMKT	$ 33,223	$ 1,148	3.45%	26,242	937	3.57%	12,993	289	2.64%
Time Deposits <$100,000	48,897	2,645	5.41%	26,239	1,213	4.62%	5,627	191	4.04%
Time Deposits >=$100,000	47,351	2,386	5.04%	23,202	1,190	5.13%	7,236	240	3.94%
Deposits	129,471	6,179	4.77%	75,683	3,340	4.41%	25,856	720	2.78%
Other borrowings	$ 17,318	789	4.56%	7,753	363	4.68%	153	5	3.27%
Total interest-bearing liabilities	146,789	6,968	4.75%	83,436	3,703	4.44%	26,009	725	2.79%
Capitalized interest		(149)			—			—	
Net interest expense		6,819			3,703			725	
Noninterest-bearing deposits	13,975			11,550			5,995		
Noninterest bearing liabilities	1,215			792			765		
Stockholder's equity	19,077			13,824			13,817		
Total liabilities and stockholder's equity	$181,056			$109,602			$46,586		
Net earning assets	$ 22,582			$ 15,766			$13,808		
Net Interest income		$ 5,244							
Interest-rate spread			2.37%		$ 3,231	2.55%		$ 1,056	2.26%
Net interest margin(2)			3.10%			3.26%			2.89%
Ratio of average interest-earning assets to average interest- bearing liabilities	1.15			1.19			1.53		

(1) Other interest-earning assets included Federal funds sold and Federal Home Loan Bank stock.

(2) Net interest margin is net interest income annualized in 2005 divided by total interest-earning stock.

Table of Contents

Rate/Volume Analysis

The following table sets forth certain information regarding changes in interest income and interest expense for the periods indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to: (1) changes in rate (change in rate multiplied by prior volume); (2) changes in volume (changes in volume multiplied by prior rate); and (3) changes in rate-volume (change in rate multiplied by change in volume).

	Rate	Volume	Rate/Volume	Total
		(In thousands)		
Year Ended December 31, 2007 vs. 2006:				
Interest-earning assets:				
Loans	$(184)	$5,152	$ (167)	$4,801
Securities	133	83	15	231
Other Interest Earning Assets	(19)	120	(4)	97
Total	(70)	5,355	(156)	5,129
Interest-bearing liabilities:				
Deposits				
Savings, demand, money-market and NOW deposits	(30)	248	(8)	210
Time deposits	182	2,292	175	2,649
Other borrowings	(13)	433	(14)	406
Total	139	2,973	153	3,265
Net change in net interest income	$(209)	$2,382	$ (309)	$1,864

	Rate	Volume	Rate/Volume	Total
		(In thousands)		
Year Ended December 31, 2006 vs. 2005:				
Interest-earning assets:				
Loans	$455	$2,899	$ 1,194	$4,548
Securities	66	356	193	615
Other Interest Earning Assets	165	(135)	(40)	(10)
Total	686	3,120	1,347	5,153
Interest-bearing liabilities:				
Deposits				
Savings, demand, money-market and NOW deposits	175	295	178	648
Time deposits	194	1,213	545	1,952
Other borrowings	2	261	115	378
Total	371	1,769	838	2,978
Net change in net interest income	$315	$1,351	$ 509	$2,175

Comparison of the years ended December 31, 2007 and 2006

General Operating Results. Net earnings for the twelve month period ended December 31, 2007 was $3,000 or $0.00 per basic and diluted share, compared to a net loss of $363,000, or $0.23 per basic and diluted share for the comparable period in 2006. The $366,000 increase in net earnings resulted primarily from an increase net interest income of $2.0 million and an increase in non-interest income of $156,000 and a $80,000 decrease in provision for loan losses, partially offset by a $1.6 million increase in non-interest expense and an increase in income tax expense of $248,000.

Interest Income. Interest income increased $5.1 million to $12.1 million for the twelve month period ended December 31, 2007, compared to $6.9 million in interest income for the twelve month period ended December 31, 2006. The increase was due to an increase in the average yield earned on interest earning assets from 6.99% for the twelve months ended December 31, 2006 to 7.12% for the twelve months ended December 31, 2007 and a $70.2 million increase in average interest earning assets outstanding at December 31, 2007 compared to December 31, 2006.

Interest Expense. Interest expense increased $3.1 million from $3.7 million for the twelve month period ended December 31, 2006 to $6.8 million for the twelve month period ended December 31, 2007. The increase was primarily due to an increase of $63.4 million in average interest bearing liabilities outstanding and an increase in the average cost of interest bearing liabilities from 4.44% for the twelve months ended December 31, 2006 to 4.75% for the comparable 2007 period.

Provision for Loan Losses. The provision for loan losses is charged to operations to increase the total loan loss allowance to a level deemed appropriate by management. The provision is based upon the volume and type of lending conducted by the Company, industry standards, general economic conditions, particularly as they relate to the Company's market area, and other factors related to the collectibility of the Company's loan portfolio. The Company recorded provisions for loan losses for the twelve month periods ended December 31, 2007 and 2006 of $701,000 and $781,000, respectively. Management believes that the allowance for loan losses, which was $2.0 million or 1.23% of gross loans at December 31, 2007, is adequate.

Non-Interest Income. Non-interest income increased $156,000 during 2007 to $1.1 million, compared to $933,000 in 2006. The increase was primarily due to an increase of $321,000 in loan brokerage fees, and an increase of $121,000 in deposit account fees, partially offset by a decrease of $302,000 on net gain of loans held for sale.

Non-Interest Expense. Non-interest expenses increased by $1.6 million from $3.9 million for the twelve month period ended December 31, 2006 to $5.6 million for the twelve month period ended December 31, 2007. The increase was primarily due to increases of $1.0 million in salaries and employee benefits, $217,000 in occupancy and equipment expense, $41,000 increase in advertising and promotion, $140,000 in data processing expense, and $200,000 in other non-interest expense, all related to the overall growth of the Company.

Income Taxes. The income tax benefit was $199,000 for the twelve month period ended December 31, 2006 and the income tax expense was $3,000 for the corresponding period in 2007.

Comparison of the years ended December 31, 2006 and 2005

General Operating Results. Net loss for the twelve month period ended December 31, 2006 was $363,000, or $0.23 per basic and diluted share, compared to $1,009,000, or $0.67 per basic and diluted share, for the comparable period in 2005. The $646,000 decrease in net loss resulted primarily from an increase in net interest income of $2.2 million and an increase in non-interest income of $748,000, partially offset by a $217,000 increase in provision for loan losses, a $1.5 million increase in non-interest expense and a decrease in income tax benefit of $579,000. For the 2005 period, the Bank had only been in operation for ten months.

Interest Income. Interest income increased $5.2 million to $6.9 million for the twelve month period ended December 31, 2006, when compared to the twelve month period ended December 31, 2005. The increase was due to an increase in the average yield earned on interest earning assets from 5.05% for the twelve months ended December 31, 2005 to 6.99% for the twelve months ended December 31, 2006 and a $59.4 million increase in average interest earning assets outstanding at December 31, 2006 compared to December 31, 2005.

Interest Expense. Interest expense increased $3.0 million from $725,000 for the twelve month period ended December 31, 2005 to $3.7 million for the twelve month period ended December 31, 2006. The increase was primarily due to an increase of $57.4 million in average interest bearing liabilities outstanding and an increase in the average cost of interest bearing liabilities from 2.79% for the twelve months ended December 31, 2005 to 4.44% for the comparable 2006 period.

Provision for Loan Losses. The provision for loan losses is charged to operations to increase the total loan loss allowance to a level deemed appropriate by management. The provision is based upon the volume and type of lending conducted by the Company, industry standards, general economic conditions, particularly as they relate to the Company's market area, and other factors related to the collectibility of the Company's loan portfolio. The Company recorded provisions for loan losses for the twelve month periods ended December 31, 2006 and 2005 of $781,000 and $564,000, respectively. The increase in the provision was primarily due to the overall growth of the loan portfolio. Management believes that the allowance for loan losses, which was $1.3 million or 1.25% of gross loans at December 31, 2006, is adequate.

Non-Interest Income. Non-interest income increased $748,000 during the 2006 period. The increase was primarily due to an increase of $593,000 in net gain on sale of loans held for sale, and an increase of $114,000 in deposit account fees.

Non-Interest Expense. Non-interest expenses increased by $1.5 million from $2.5 million for the twelve month period ended December 31, 2005 to $3.9 million for the twelve month period ended December 31, 2006. The increase was primarily due to increases of $930,000 in salaries and employee benefits, $177,000 in occupancy and equipment expense, $77,000 increase in advertising and promotion, $98,000 in data processing expense, and $161,000 in other non-interest expense, all related to the overall growth of the Company.

Income Taxes. The income tax benefit was $778,000, an effective rate of 43.5%, for the twelve month period ended December 31, 2005 and $199,000, an effective rate of 35.4% for the corresponding period in 2006. In 2006, the effective rate was higher due to the reversal of a valuation allowance.

Based on the Company's current earnings forecast and/or budget, the losses that generated the deferred tax asset are only temporary and taxable income is projected in the near future which would utilize and support the reversal of the valuation allowance initially established. Based on this positive evidence it is more likely than not that the deferred tax asset will be utilized.

The Company's future performance will depend on a number of factors outside of our control. Some of our borrowers may not repay loans that we make to them. If a significant number of loans are not repaid, it will have an adverse effect on our earnings and overall financial condition. The determination of an appropriate level of loan loss allowance is an inherently difficult process and is based on numerous assumptions. As a result, our allowance for loan losses may not be adequate to cover actual losses, and future provision for loan losses may adversely affect our earnings. Furthermore, a prolonged economic downturn or recession in our target markets would result in operating losses, impaired liquidity and the erosion of capital. A variety of factors could cause such an economic dislocation or recession, including adverse developments in the industries in these areas. Also, a significant portion of our loan portfolio is secured by real estate located in our market areas. If real estate prices decline in our markets, the value of the real estate collateral securing our loans could be reduced. Such a reduction in the value of our collateral could increase the number of non-performing loans and adversely affect our financial performance.

To support our effort to reach profitability, we are attempting to make loans and obtain low cost funding sources, to increase our earning asset base and net interest income. We will need to reach a significant level of net interest income in order to offset the non-interest expenses we incur for such things as salaries, occupancy, data processing, professional services and advertising. We will spend the same amount on many of these items, regardless of the amount of net-interest income we receive. Therefore, it is important for us to reach a certain asset size in order to reach profitability.

In addition to pursuing loan and deposit growth, we are also utilizing an expanding branch network. We currently operate four offices, with two more to open later this year. These facilities are expected to enable us to serve and acquire more loan and deposit customers. The opening of these offices and their continued operation required, and will continue to require, us to spend more money on salaries, rent and advertising. Until the new branches can produce enough net interest income to offset their incremental contribution to our non-interest expenses, they could have the effect of decreasing our net earnings.

Asset/Liability Management

A principal objective of the Company's asset/liability management strategy is to minimize its exposure to changes in interest rates by matching the maturity and repricing horizons of interest-earning assets and interest-bearing liabilities. This strategy is overseen in part through the direction of the Bank's Asset and Liability Committee ("ALCO") which establishes policies and monitors results to control interest rate sensitivity.

Management evaluates interest rate risk and then formulates guidelines regarding asset generation and repricing, funding sources and pricing, and off-balance sheet commitments in order to maintain interest rate risk within target levels for the appropriate level of risk which are determined by the ALCO. The ALCO uses internally generated reports to measure the Bank's interest rate sensitivity. From these reports, the ALCO can estimate the net earnings effect of various interest rate scenarios.

As a part of the Company's interest rate risk management policy, the ALCO examines the extent to which its assets and liabilities are "interest rate sensitive" and monitors the Bank's interest rate sensitivity "gap." An asset or liability is considered to be interest rate sensitive if it will reprice or mature within the time period analyzed, usually one year or less. The interest rate sensitivity gap is the difference between interest-earning assets and interest-bearing liabilities scheduled to mature or reprice within such time period. A gap is considered positive when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities. A gap is considered negative when the amount of interest rate sensitive liabilities exceeds interest rate sensitive assets. During a period of rising interest rates, a negative gap would tend to adversely affect net interest income, while a positive gap would tend to result in an increase in net interest income. During a period of falling interest rates, a negative gap would tend to result in an increase in net interest income, while a positive gap would tend to adversely affect net interest income. If the repricing of each bank's assets and liabilities were equally flexible and moved concurrently, the impact of any increase or decrease in interest rates on net interest income would be minimal.

A simple interest rate "gap" analysis by itself may not be an accurate indicator of how net interest income will be affected by changes in interest rates. Accordingly, the ALCO also evaluates how the repayment of particular assets and liabilities is impacted by changes in interest rates. Income associated with interest-earning assets and costs associated with interest-bearing liabilities may not be affected uniformly by changes in interest rates. In addition, the magnitude and duration of changes in interest rates may have a significant impact on net interest income. For example, although certain assets and liabilities may have similar maturities or period of repricing, they may react in different degrees to changes in market interest rates. Interest rates on certain types of assets and liabilities fluctuate in advance of changes in general market interest rates, while interest rates on other types may lag behind changes in general market rates. In addition, certain assets, such as adjustable rate mortgage loans, have features (generally referred to as "interest rate caps") which limit changes in interest rates on a short-term basis and over the life of the asset. In the event of a change in interest rates, prepayment (on loans) and early withdrawal (of deposit accounts) levels also could deviate significantly from those assumed in calculating the interest rate gap. The ability of many borrowers to service their debts also may decrease in the event of an interest rate increase.

Currently the Company has not entered into any interest rate swaps or similar hedging instruments in connection with its asset/liability management and the Company does not expect to use interest rate swaps in its operations. Further discussion on off-balance-sheet arrangements can be found in Note 9 of the Notes to Consolidated Financial Statements. The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit, unused lines of credit and standby letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments as it does for on-balance sheet instruments. The Company also did not have any significant interest rate lock commitments at December 31, 2007.

Management's strategy is to maintain a balanced interest rate risk position to protect its net interest margin from market fluctuations.

Principal among the Company's asset/liability management strategies has been the emphasis on managing its interest rate sensitive liabilities in a manner designed to attempt to reduce the Company's exposure during periods of fluctuating interest rates. Management believes that the type and amount of the Company's interest rate sensitive liabilities may reduce the potential impact that a rise in interest rates might have on the Company's net interest income. The Company seeks to maintain a core deposit base by providing quality services to its customers without significantly increasing its cost of funds or operating expenses. Management anticipates that these accounts will continue to comprise a significant portion of the Company's total deposit base. The Company also maintains a portfolio of liquid assets in order to reduce its overall exposure to changes in market interest rates. The Company also maintains a "floor," or minimum rate, on certain of its floating or prime based loans. These floors allow the Company to continue to earn a higher rate when the floating rate falls below the established floor rate. All interest rate caps and floors are clearly and closely related to the loan agreement and therefore not bifurcated and valued separately.

The following table sets forth certain information relating to the Company's interest-earning assets and interest-bearing liabilities at December 31, 2007 that are estimated to mature or are scheduled to reprice within the period shown ($ in thousands):

	Under 3 Months	3 to 12 Months	1-5 Years	Over Five Years	Total
Interest-earning deposits	$ 103	—	—	—	103
Federal funds sold	1,730	—	—	—	1,730
Interest bearing time deposits in Banks	—	2,046	—	—	2,046
Loans (1)	73,642	12,470	70,913	9,072	166,097
Securities (2)	7,206	8,601	4,730	836	21,373
Total rate-sensitive assets (earning assets)	$82,681	23,117	75,643	9,908	191,349
Money market (3)	14,217	7,108	7,108	—	28,433
Savings and NOW deposits (3)	3,250	3,249	—	—	6,499
Time deposits (3)	32,581	58,283	25,288	—	116,152
Other borrowings (4)	4,807	—	13,000	—	17,807
Total rate-sensitive liabilities	$54,855	68,640	45,396	—	168,891
Gap (repricing differences)	$27,827	(45,523)	30,247	9,908	22,458
Cumulative Gap	$27,827	(17,697)	12,550	22,458	
Cumulative Gap/total assets	13.7%	(8.7)%	6.2%	11.0%	
Cumulative Gap/total earning assets	14.5%	(9.2)%	6.6%	11.7%	
Total assets					$203,404
Total earning assets					$191,349

(1) In preparing the table above, adjustable-rate loans were included in the period in which the interest rates are next scheduled to adjust rather than in the period in which the loans mature. Fixed-rate loans were scheduled according to their contractual maturities.

(2) Securities were scheduled based on their remaining maturity or repricing frequency. Fixed-rate mortgage-backed securities are scheduled ratably over nine years. Includes FHLB stock grouped in over five years.

(3) Excludes noninterest-bearing deposit accounts. Money-market, NOW, and savings deposits are scheduled based on FDICIA studies on nonmaturity deposits. All other time deposits were scheduled through the maturity dates.

(4) Federal Home Loan Bank advances with call features are scheduled based on call dates.

Table of Contents

Selected Quarterly Results

	2007			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$2,472	$2,877	$3,296	$3,418
Interest expense	1,401	1,556	1,899	1,963
Net interest income	1,071	1,321	1,397	1,455
Provision for loan losses	143	198	135	225
Noninterest income	272	304	289	224
Noninterest expense	1,298	1,338	1,494	1,450
Earnings before income taxes	(98)	89	57	4
Net earnings	(60)	58	25	(20)
Earnings (loss) per share – basic	(0.03)	0.03	0.01	(0.01)
Earnings (loss) per share – diluted	(0.03)	0.03	0.01	(0.01)

	2006				2005			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$1,169	1,549	1,944	2,272	116	233	570	862
Interest expense	578	811	1,049	1,265	8	92	238	387
Net interest income	591	738	895	1,007	108	141	332	475
Provision for loan losses	126	232	205	218	15	118	259	172
Noninterest income	117	276	291	249	0	35	83	67
Noninterest expense	763	929	1,022	1,231	486	509	705	764
Earnings before income taxes	(181)	(147)	(41)	(193)	(393)	(451)	(549)	(394)
Net earnings	(114)	(97)	(29)	(123)	(143)	(326)	(325)	(215)
Basic earnings per common and diluted share	(.08)	(.06)	(.02)	(.07)	(.10)	(.22)	(.22)	(.13)

Impact of Inflation and Changing Prices

The financial statements and related financial data concerning the Company presented in this 10-KSB have been prepared in accordance with accounting principles generally accepted in the United States of America, which require the measurement of financial position and operating results in terms of historical dollars without considering changes in the relative purchasing power of money over time due to inflation. The primary impact of inflation on the operations of the Company is reflected in increased operating costs. Unlike most industrial companies, virtually all of the assets and liabilities of a financial institution are monetary in nature. As a result, changes in interest rates have a more significant impact on the performance of a financial institution than do the effects of changes in the general rate of inflation and changes in prices. Interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services.

Item 7. Financial Statements

The financial statements of the Company at December 31, 2007 and 2006 and for the years then ended are set forth in this Form 10-KSB as Exhibit 13.1.

Item 8. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None

Item 8A(T). Controls and Procedures

Evaluation of Disclosure Controls and Procedures. We have carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Securities Exchange Act of 1934 Rule 13a-14. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective in timely alerting them to material information relating to the Company required to be included in our periodic Securities and Exchange Commission filings. No significant changes were made in our internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation.

Management's Report on Internal Control Over Financial Reporting. Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) and 15d-15(f) promulgated under the Securities Exchange Act of 1934 as a process designated by, or under the supervision of, our Principal Executive and Principal Financial Officers and effected by our Board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and disposition of our assets;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and
- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2007. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control – Integrated Framework.

Based on our assessment, management believes that, as of December 31, 2007, our internal control over financial reporting is effective based on those criteria.

This annual report does not include an attestation report of our registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit us to provide only management's report in this annual report.

Changes in Internal Control Over Financial Reporting. There was no change in our internal control over financial reporting that occurred during the period covered by this Report that has materially affected, or is reasonably likely to materially affect, our internal control over-financial reporting.

Item 8B. Other Information

Not applicable.

PART III

Item 9. Directors, Executive Officers, Promoters and Control Persons; Compliance with Section 16(a) of the Exchange Act

The information contained under the sections captioned "Directors" and "Executive Officers" under "Election of Directors" and "Section 16(a) Reporting Requirements" in the Proxy Statement, is incorporated herein by reference.

Item 10. Executive Compensation

The Company has a Code of Ethics that applies to its principal executive officer and principal financial officer (who is also its principal accounting officer), a copy of which is incorporated by reference into this Form 10-KSB as Exhibit 14.1. The information contained in the section captioned "Information About the Board of Directors and Its Committees," and "Executive Compensation and Benefits" under "Election of Directors" in the Proxy Statement, is incorporated herein by reference.

Item 11. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Information contained in the section captioned "Directors" and under "Election of Directors," in the Proxy Statement, is incorporated herein by reference.

Item 12. Certain Relationships and Related Transactions

AFSI does not make loans to our directors, officers or employees. The Bank, however, does promote lending relationships with our directors, officers and employees. Loans made to directors, executive officers and principal shareholders, defined as individuals owning 10% or more of AFSI's common stock (collectively "Affiliates") are governed under provisions of Section 22(h) of the Federal Reserve Act, which requires that any loans made to Affiliates, or to any related interest of an Affiliate, must (i) be on substantially the same terms, including interest rates and collateral as those prevailing at the time for comparable transactions with non-affiliated parties; and (ii) not involved more that the normal risk of repayment or present other unfavorable features. There is, however, an exception for loans made to employees who are Affiliates that are made pursuant to a benefit or compensation package that is widely available to all Bank employees and does not give a preference to Affiliates. There is also an aggregate limit of $25,000, or 5% of the amount of the Bank's unimpaired capital and unimpaired surplus on all loans to an individual Affiliate, unless the amount has been approved by the Board of Directors and the Affiliate has abstained from participating in the voting.

There is a further exception regarding loans to executive officers of the Bank. Executive officers are those people who participate, or who have authority to participate, in major policy making functions of the Bank, regardless of their title. The Bank may lend any otherwise permissible sum of money to an executive officer for (i) financing the education of the officer's children; (ii) a Board of Director's approved first mortgage on the officer's residence; or (iii) a loan secured by certain low-risk collateral. The Bank may also lend up to the higher of $25,000 or 2.5% of the Bank's unimpaired capital and unimpaired surplus (but never more than $100,000) to an executive officer for any other purpose.

As of December 31, 2007, the Bank had an aggregate total of $6,885,165 outstanding in loans and other extensions of credit to Affiliates. At December 31, 2007, the Bank had unsecured loans outstanding with aggregate outstanding balances of $3,179,937 of which $701,070 were to insiders. All such loans (both those to insiders and those to unaffiliated borrowers) were underwritten to the same policy standards and are due on demand. No insider received any preferential treatment with regard to interest rates, maturity, payment schedule or other features of the loans. All of the outstanding loans to directors and executive officers are performing pursuant to their terms. As of December 31, 2007 the Bank had the following outstanding loans to AFSI's and the Bank's directors and executive officers:

Name	Maturity Date of Loan	Largest Amount Outstanding in 2007	Amount Outstanding At December 31, 2007	Loan Type	Interest Rate
Barrett, Spencer Director	Demand	$78,729.17	$78,729.17	Unsecured LOC	6.000%
Bosshardt, Carol Director	Demand	$782,104.17	$301,500.00	Unsecured LOC	7.250%
Bosshardt, Carol Director	Demand	$250,000.00	$147,000.00	Unsecured LOC	7.250%
Bosshardt, Carol Director	4/27/2016	$421,797.03	$414,890.57	Commercial – SFR	7.460%
Bosshardt, Carol Director	10/23/2008	$140,000.00	$139,125.97	Unsecured LOC	6.750%
Bosshardt, Carol Director	4/28/2016	$162,500.00	$156,542.3	Commercial R/E	7.750%
Bosshardt, Carol Director	12/6/2017	$115,000.00	$115,000.00	Single Family Condo	7.000%
Bosshardt, Carol Director	6/8/2008	$60,000.00	$35,000.00	Unsecured	6.750%
Bosshardt, Carol Director	12/19/2017	$273,922.00	$273,922.00	Commercial R/E	7.000%
Czuryla, Walter Bank EVP	Demand	$3,524.94	—	Unsecured ODP	7.250%
Fletcher, Gloria Director	7/13/2015	$1,813,470.69	$1,790,376.42	Commercial R/E	6.710%
Fletcher, Gloria Director	6/26/2007	$188,456.58	$186,178.32	Single Family Condo	6.631%
Hill, Michael Director	Demand	$4,157.73	$153.54	Unsecured ODP	7.250%
Hill, Michael Director	9/29/2007	$147,052.66	$146,148.68	Residential Lot	7.500%
Hill, Michael Director	Demand	$36.03	—	Unsecured LOC	7.250%
Hill, Michael Director	12/29/2021	$100,000.00	$93,891.36	HELOC	6.250%
Kurtz, Jon President and CEO	Demand	$242.00	—	Unsecured ODP	7.250%
Leon, Ignacio Director	11/16/2022	—	—	HELOC	6.250%
Page, Robert Bank EVP	Demand	$3,000.00	—	Unsecured ODP	7.250%
White, Job E. Director	Demand	$782,104.17	$301,500.00	Unsecured LOC	7.250%
White, Job E. Director	10/24/2012	$350,000.00	$348,500.00	Commercial – SFR	6.855%
White, Job E. Director	10/21/2020	$399,545.71	—	HELOC	6.250%
Williams, Tommy Director	Demand	$782,104.17	$301,500.00	Unsecured LOC	7.250%
Williams, Tommy Director	Demand	$2,500,000.00	$1,122,194.29	S/F Residences	6.750%
Williams, Tommy Director	11/1/2011	$1,500,000.00	$933,452.00	S/F Residences	6.750%

The Company entered into a lease with Halachua Properties, LLC, which is owned by certain directors, during 2006 to rent office space for a branch in Alachua, Florida. This lease was for one year with a one year renewal option for $34,000 annually. The Company purchased the property in October 2007.

Item 13. Exhibits

Exhibits marked with an (a) were filed with the Form 10-KSB filed with the Securities and Exchange Commission on March 15, 2006.

(a)	3.1	Articles of Incorporation
(a)	3.2	Bylaws
(a)	4.1	Specimen Common Stock Certificate
(a)	4.2	Warrant Plan and Specimen Warrant Plan
(a)	10.1	Employment Agreement with Jon M. Kurtz
(a)	10.2	Lease for Main Office
	13.1	Financial Statements
(a)	14.1	Code of Ethics
(a)	21.1	Schedule of Subsidiaries
	31.1	Certification of Chief Executive Officer required by Rule 13a-14(a)/15d-14(a) under the Exchange Act
	31.2	Certification of Chief Financial Officer required by Rule 13a-14(a)/15d-14(a) under the Exchange Act
	32.1	Certification of Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
	32.2	Certification of Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Item 14. Principal Accountant Fees and Services

The information contained in the section captioned “Ratification of the Appointment of the Independent Auditor for the Fiscal Year Ending December 31, 2008” in the Proxy Statement is incorporated herein by reference.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has caused this report to be duly signed on its behalf by the undersigned, thereunto duly authorized, in the City of Ocala, State of Florida, on the 27th day of March, 2008.

ALARION FINANCIAL SERVICES, INC.

/s/ Jon M. Kurtz

Jon M. Kurtz
Principal Executive Officer

/s/ Matthew Ivers

Matthew Ivers
Chief Financial Officer

Table of Contents

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the 27th day of March, 2008:

/s/ Loralee W. Miller Loralee W. Miller	Chairperson of the Board
/s/ Michael P. Hill Michael P. Hill	Director and Vice Chairman of the Board
/s/ Spencer Barrett Spencer Barrett	Director
/s/ Carol R. Bosshardt Carol R. Bosshardt	Director
/s/ Gloria W. Fletcher Gloria W. Fletcher	Director
/s/ Jon M. Kurtz Jon M. Kurtz	Chief Executive Officer, President and Director
/s/ Ignacio L. Leon Ignacio L. Leon	Director
/s/ Job E. White Job E. White	Director
/s/ Tommy W. Williams, Jr. Tommy W. Williams, Jr.	Director

Alarion Financial Services, Inc.
Form 10-KSB
For Fiscal Year Ending December 31, 2007

EXHIBIT INDEX

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Exhibit 13.1

ALARION FINANCIAL SERVICES, INC.

Holding Company for

Audited Consolidated Financial Statements

At December 31, 2007 and 2006 and For the Years Then Ended

(Together with Report of Independent Registered Public Accounting Firm)

Report of Independent Registered Public Accounting Firm

Alarion Financial Services, Inc.
Ocala, Florida:

We have audited the accompanying consolidated balance sheets of Alarion Financial Services, Inc. and Subsidiary (the "Company") as of December 31, 2007 and 2006, and the related consolidated statements of operations, stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company at December 31, 2007 and 2006, and the results of its operations and its cash flows for years then ended, in conformity with U.S. generally accepted accounting principles.

HACKER, JOHNSON & SMITH PA
Tampa, Florida
March 24, 2008

ALARION FINANCIAL SERVICES, INC. AND SUBSIDIARY

Consolidated Balance Sheets
($ in thousands, except per share amounts)

	At December 31, 2007	2006
Assets		
Cash and due from banks	$ 1,805	2,781
Interest-earning deposits and federal funds sold	1,833	3,953
Cash and cash equivalents	3,638	6,734
Interest bearing time deposits in banks	2,046	1,000
Securities available for sale	20,537	13,837
Loans, net of allowance for loan losses of $2,046 and $1,345	164,051	106,289
Loans held for sale	—	2,436
Accrued interest receivable	931	648
Premises and equipment, net	9,603	6,724
Federal Home Loan Bank stock, at cost	836	595
Deferred income taxes	909	990
Other assets	853	191
Total assets	$203,404	139,444
Liabilities and Stockholders' Equity		
Liabilities:		
Noninterest-bearing demand deposits	13,159	9,615
NOW, money-market and savings deposits	34,932	29,927
Time deposits < $100,000	67,867	36,572
Time deposits > = $100,000	48,285	32,958
Total deposits	164,243	109,072
Federal Home Loan Bank advances	13,000	10,000
Other borrowings	4,807	5,339
Accrued interest payable	799	400
Accrued expenses and other liabilities	304	296
Total liabilities	183,153	125,107
Commitments (Notes 4, 9 and 17)		
Stockholders' equity:		
Preferred stock, $.01 par value; 1,000,000 shares authorized, none issued or outstanding	—	—
Common stock, $.01 par value; 4,000,000 shares authorized, 2,183,485 and 1,607,140 shares issued and outstanding in 2007 and 2006	22	16
Additional paid-in capital	21,856	16,002
Accumulated deficit	(1,657)	(1,660)
Accumulated other comprehensive income (loss)	30	(21)
Total stockholders' equity	20,251	14,337
Total liabilities and stockholders' equity	$203,404	139,444

See Accompanying Notes to Consolidated Financial Statements.

ALARION FINANCIAL SERVICES, INC. AND SUBSIDIARY

Consolidated Statements of Operations
(In thousands, except per share amounts)

	Year Ended December 31, 2007	2006
Interest income:		
Loans	$ 10,453	5,652
Securities	968	737
Other	642	545
Total interest income	12,063	6,934
Interest expense:		
Deposits	6,179	3,340
Borrowings	640	363
Total interest expense	6,819	3,703
Net interest income	5,244	3,231
Provision for loan losses	701	781
Net interest income after provision for loan losses	4,543	2,450
Noninterest income:		
Deposit account fees	253	132
Net gain on sales of loans held for sale	197	499
Loan brokerage fees	570	249
Other	69	53
Total noninterest income	1,089	933
Noninterest expenses:		
Salaries and employee benefits	3,216	2,205
Occupancy and equipment	734	517
Data processing	371	231
Professional services	179	161
Advertising and promotion	194	153
Office supplies and printing	143	135
Other	743	543
Total noninterest expenses	5,580	3,945
Earnings (loss) before income tax expense (benefit)	52	(562)
Income tax expense (benefit)	49	(199)
Net earnings (loss)	$ 3	(363)
Earnings (loss) per share – basic	$ —	(.23)
Earnings (loss) per share – diluted	$ —	(.23)
Weighted-average number of common shares outstanding, basic	2,124,883	1,544,912
Weighted-average number of common shares outstanding, diluted	2,141,885	1,544,912
Dividends per share	$ —	—

See Accompanying Notes to Consolidated Financial Statements.

ALARION FINANCIAL SERVICES, INC. AND SUBSIDIARY

Consolidated Statements of Stockholders' Equity

Years Ended December 31, 2007 and 2006
($ in thousands)

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Accumulated Deficit	Accumulated Compre-hensive Income (Loss)	Total Stockholders' Equity
Balance at December 31, 2005	1,514,200	$ 15	15,073	(1,297)	—	13,791
Comprehensive loss						
Net loss	—	—	—	(363)	—	(363)
Net unrealized loss on securities available for sale, net of tax benefit of $13	—	—	—	—	(21)	(21)
Comprehensive loss						(384)
Common stock options exercised	5,000	—	50	—	—	50
Common stock warrants exercised	87,940	1	879	—	—	880
Balance at December 31, 2006	1,607,140	16	16,002	(1,660)	(21)	14,337
Comprehensive income						
Net earnings	—	—	—	3	—	3
Net change in unrealized loss on securities available for sale, net of taxes of $32	—	—	—	—	51	51
Comprehensive income						54
Share-based compensation	—	—	96	—	—	96
Common stock options exercised	1,030	—	10	—	—	10
Common stock warrants exercised	575,315	6	5,748	—	—	5,754
Balance at December 31, 2007	2,183,485	$ 22	21,856	(1,657)	30	20,251

See Accompanying Notes to Consolidated Financial Statements.

ALARION FINANCIAL SERVICES, INC. AND SUBSIDIARY

Consolidated Statements of Cash Flows
(In thousands)

	Year Ended December 31, 2007	2006
Cash flows from operating activities:		
Net earnings (loss)	$ 3	(363)
Adjustments to reconcile net earnings (loss) to net cash provided by (used in) operating activities:		
Provision for loan losses	701	781
Share-based compensation	96	—
Depreciation and amortization	353	260
Deferred income tax expense (benefit)	49	(199)
Net amortization on premiums and discounts on securities	—	(42)
Net amortization of deferred loan fees and costs	164	82
Net gain on sales of loans held for sale	(197)	(499)
Loans originated for sale	(5,424)	(50,213)
Proceeds from sales of loans held for sale	8,057	48,597
Net increase in accrued interest payable	399	251
Net increase in accrued interest receivable	(283)	(440)
Net (increase) decrease in other assets	(662)	34
Net increase (decrease) in accrued expenses and other liabilities	8	(202)
Net cash provided by (used in) operating activities	3,264	(1,953)
Cash flows from investing activities:		
Proceeds from principal repayments and maturities on securities held to maturity	—	7,447
Proceeds from principal repayments and maturities on securities available for sale	17,377	—
Purchase of securities held to maturity	—	(10,968)
Purchase of securities available for sale	(23,994)	—
Purchase of time deposits	(1,046)	(1,000)
Loan disbursements, net of repayments	(58,627)	(62,623)
Purchase of premises and equipment	(3,232)	(2,061)
Purchase of Federal Home Loan Bank stock	(241)	(560)
Net cash used in investing activities	(69,763)	(69,765)
Cash flows from financing activities:		
Net increase in deposits	56,601	50,556
Net (decrease) increase in other borrowings	(1,962)	6,066
Net increase in advances from Federal Home Loan Bank	3,000	10,000
Proceeds from common stock options and warrants exercised	5,764	930
Net cash provided by financing activities	63,403	67,552
Net decrease in cash and cash equivalents	(3,096)	(4,166)
Cash and cash equivalents at beginning of year	6,734	10,900
Cash and cash equivalents at end of year	$ 3,638	6,734

(continued)

ALARION FINANCIAL SERVICES, INC. AND SUBSIDIARY

Consolidated Statements of Cash Flows, Continued
(In thousands)

	Year Ended December 31, 2007	2006
Supplemental disclosure of cash flow information:		
Cash paid during the year for- Interest, net of capitalized interest of $149 in 2007	$ 6,569	3,452
Income taxes	$ —	—
Noncash transactions:		
Accumulated other comprehensive income (loss), net change in unrealized loss on securities available for sale, net of taxes	$ 51	(21)
Transfer of securities held to maturity to available for sale	$ —	13,837

See Accompanying Notes to Consolidated Financial Statements.

(1) Summary of Significant Accounting Policies

Organization. Alarion Financial Services, Inc. (the “Holding Company”) owns 100% of the outstanding common stock of Alarion Bank (the “Bank”). The Holding Company’s primary activity is the operation of the Bank. The Bank is a state (Florida)-chartered commercial bank. The Bank commenced operations on February 28, 2005. The Bank offers a variety of banking and financial services to individual and corporate customers through its five banking offices located in Ocala, Gainesville and Alachua, Florida. The deposit accounts of the Bank are insured up to the applicable limits by the Federal Deposit Insurance Corporation.

Basis of Presentation. The accompanying consolidated financial statements include the accounts of the Holding Company and the Bank (collectively, the “Company”). All significant intercompany accounts and transactions have been eliminated in consolidation. The accounting and reporting practices of the Company conform to accounting principles generally accepted in the United States of America and to general practices within the banking industry. The following summarizes the more significant of these polices and practices.

Use of Estimates. In preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation of deferred tax assets.

Cash and Cash Equivalents. For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash and balances due from banks, interest-earning deposits and federal funds sold, all of which mature within ninety days.

At December 31, 2007 and 2006, the Bank was not required by law or regulation to maintain cash reserves with the Federal Reserve Bank, in accounts with other banks or in the vault.

(continued)

(1) Summary of Significant Accounting Policies, Continued

Securities. Securities may be classified as either trading, held to maturity or available for sale. Securities that are held principally for resale in the near term are considered trading securities and recorded at fair value with changes in fair value recorded in operations. Debt securities that the Company has the positive intent and ability to hold to maturity are classified as "held to maturity" and are reported at amortized cost. Available-for-sale securities consist of securities not classified as trading securities nor as held-to-maturity securities. Unrealized holding gains and losses, net of tax, on available-for-sale securities are excluded from operations and reported in accumulated other comprehensive income (loss). Gains and losses on the sale of available-for-sale securities are recorded on the trade date and are determined using the specific-identification method. Purchase premiums and discounts are recognized in interest-income using the interest method over the terms of the securities. In December 2006, the Company reclassified all securities held to maturity to securities available for sale (see note 2).

Loans. Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding principal adjusted for any charge-offs, the allowance for loan losses, and any deferred fees or costs.

Loan origination fees are capitalized and certain direct origination costs are deferred. Both are recognized as an adjustment of the yield of the related loan.

The accrual of interest on loans is discontinued at the time the loan is ninety days delinquent unless the loan is well collateralized and in process of collection. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual or charged-off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

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

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

(continued)

(1) Summary of Significant Accounting Policies, Continued

Allowance for Loan Losses, Continued. The allowance consists of specific and general components. The specific component relates to loans that are considered impaired. For such loans, an allowance is established when the discounted cash flows or the collateral value of the impaired loan is lower than the carrying value of that loan. The general component covers all other loans and is based on historical peer group loss experience adjusted for qualitative factors, such as economic conditions and other trends or uncertainties that could affect management's estimate of probable losses.

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

Large groups of smaller-balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual residential real estate, home equity or consumer loans for impairment disclosures.

Loans Held for Sale. Loans held for sale are carried at the lower of cost or estimated fair value in the aggregate. Net unrealized losses are recognized through a valuation allowance by charges to operations. At December 31, 2006, the estimated fair value exceeded book value for all loans held to sale. There were no loans held for sale at December 31, 2007.

Loan origination fees are deferred and direct loan origination costs are capitalized until the related loan is sold, at which time the net fees are included in the net gain on sale of loans held for sale in the consolidated statements of operations.

Premises and Equipment. Land is stated at cost. Other premises, equipment and leasehold improvements are stated at cost less accumulated depreciation and amortization. Interest costs are capitalized in connection with construction of new banking offices. Depreciation and amortization expense are computed using the straight-line method over the shorter of the estimated useful life of each type of asset or related lease term which includes certain renewal options.

(continued)

(1) Summary of Significant Accounting Policies, Continued

Comprehensive Income (Loss). Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net earnings (loss). Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the consolidated balance sheet, such items, along with net earnings (loss), are components of comprehensive income (loss).

Transfer of Financial Assets. Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Income Taxes. Deferred income tax assets and liabilities are recorded to reflect the tax consequences on future years of temporary differences between revenues and expenses reported for financial statement and those reported for income tax purposes. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled. Valuation allowances are provided against assets which are not likely to be realized.

The Holding Company and the Bank file consolidated income tax returns. Income taxes are allocated between the Holding Company and the Bank as though separate income tax returns were filed.

Stock Compensation Plan. Effective January 1, 2006, the Company adopted the fair value recognition provisions of FASB Statement No. 123(R), *Share-Based Payment* ("SFAS 123(R)"), using the modified-prospective-transition method. Under that transition method, compensation cost recognized includes: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value calculated in accordance with the original provisions of SFAS 123, *Accounting for Stock-Based Compensation* (as amended by SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*) (collectively SFAS 123) and (b) compensation cost for all share-based payments granted subsequent to December 31, 2005, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123(R). Prior to December 31, 2005, the Company was not considered a public company as defined in SFAS 123 and used the minimum value method to determine stock based compensation. Therefore, the stock options granted in 2005 that vested in 2007 and 2006 were not required to be expensed by the Company upon implementation of SFAS 123(R).

(continued)

(1) Summary of Significant Accounting Policies, Continued

Earnings (Loss) Per Share. Earnings (loss) per share ("EPS") of common stock has been computed on the basis of the weighted-average number of shares of common stock outstanding. Outstanding stock options and warrants were not considered dilutive securities for 2006 due to the net loss incurred by the Company. Outstanding stock options and warrants are considered dilutive securities for the fiscal year 2007 for the purposes of calculating diluted EPS, which is computed using the treasury stock method. The following table represents the calculations of the weighted-average number of shares for diluted EPS.

	Weighted-Average Shares
Year Ended December 31, 2007:	
For basic EPS	2,124,883
Effect of dilutive securities-incremental shares from assumed conversion of options and warrants	17,002
For diluted EPS	2,141,885

For the year ended December 31, 2007, the following options were excluded from the calculation of diluted earnings per share due to the exercise price exceeding the average market price for the period:

Number of Outstanding Options	Exercise Price	Expiration Date
67,850	$ 10.50	2017

Off-Balance-Sheet Instruments. In the ordinary course of business the Company has entered into off-balance-sheet financial instruments consisting of 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 are funded.

(continued)

(1) Summary of Significant Accounting Policies, Continued

Fair Values of Financial Instruments. The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument or may not necessarily represent the underlying fair value of the Company. The following methods and assumptions were used by the Company in estimating fair values of financial instruments:

Cash and Cash Equivalents and interest bearing time deposits in banks. The carrying amounts of these financial instruments approximate their fair value.

Securities. Fair values for securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

Loans. For variable-rate loans that reprice frequently and have no significant change in credit risk, fair values are based on carrying values. Fair values for certain fixed-rate residential mortgage, commercial real estate and commercial loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality.

Loans held for Sale. Fair values of loans held for sale are based on commitments on hand from investors or prevailing market prices.

Federal Home Loan Bank Stock. Fair value of the Company's investment in Federal Home Loan Bank stock is based on its redemption value, which is its cost of $100 per share.

Deposits. The fair values disclosed for demand, NOW, money-market and savings deposits are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). Fair values for fixed-rate time deposits are estimated using a discounted cash flow calculation that applies interest rates currently being offered on time deposits to a schedule of aggregated expected monthly maturities of time deposits.

Federal Home Loan Bank Advances. Fair value of the advances from the Federal Home Loan Bank are estimated using a discounted cash flow analysis based on the Company's current incremental borrowing rate for similar types of borrowings.

Other Borrowings. The carrying amounts of other borrowings approximates their fair value.

(continued)

(1) Summary of Significant Accounting Policies, Continued

Fair Values of Financial Instruments, Continued.

Accrued Interest. The carrying amounts of accrued interest approximate their fair values.

Off-Balance-Sheet Financial Instruments. Fair values for off-balance-sheet lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing.

Recent Pronouncements. In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 157, Fair Value Measurements ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. This statement is effective for the Company as of January 1, 2008. Management is in the process of evaluating the impact of SFAS 157 and does not anticipate it will have any effect on the Company's consolidated financial condition or results of operations.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities ("SFAS 159"). SFAS 159 provides the Company with an option to report selected financial assets and liabilities at fair value. This statement is effective for the Company as of January 1, 2008. Management is in the process of evaluating the impact of SFAS 159 and does not anticipate it will have any effect on the Company's consolidated financial condition or results of operations.

In December 2007, the FASB issued SFAS No. 141(R), *Business Combinations* ("SFAS 141(R)"). SFAS 141(R) is effective for fiscal years beginning after December 15, 2008 and early implementation is not permitted. SFAS 141(R) requires the acquiring entity in a business combination to recognize all (and only) the assets acquired and liabilities assumed in the transaction; establishes the acquisition date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose to investors and other users all of the information they need to evaluate and understand the nature and financial effect of the business combination. Acquisition related costs including finder's fees, advisory, legal, accounting, valuation and other professional and consulting fees are required to be expensed as incurred. Management is in the process of evaluating the impact of SFAS 141(R) and does not anticipate it will have any effect on the Company's current consolidated financial condition or results of operations.

(continued)

(2) Securities

Securities have been classified according to management's intent. The carrying amount and fair value of securities are as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Value
Available for Sale:				
At December 31, 2007:				
U.S. government agency securities	$ 14,993	48	—	15,041
Mortgage-backed securities	5,496	19	(19)	5,496
	$ 20,489	67	(19)	20,537
At December 31, 2006:				
U.S. government agency securities	12,000	—	(19)	11,981
Mortgage-backed securities	1,871	—	(15)	1,856
	$ 13,871	—	(34)	13,837

In December 2006, the Company transferred securities with a book value of approximately $13,871,000 from the held to maturity category to the available for sale category at its then fair value resulting in unrealized losses of approximately $21,000 net of tax benefit. The net unrealized loss was recorded in accumulated other comprehensive loss. Due to this transfer, the Company will be prohibited from classifying securities as held to maturity for a period of two years.

The scheduled maturities of securities available for sale at December 31, 2007 are as follows (in thousands):

	Amortized Cost	Approximate Fair Value
Due in less than one year	$ 4,993	5,008
Due from one to five years	10,000	10,033
Due from five to ten years	—	—
Mortgage-backed securities	5,496	5,496
	$ 20,489	20,537

At December 31, 2007 and 2006, securities with a carrying value of approximately $6.5 million and $8.0 million, respectively, were pledged for other borrowings and public funds.

(continued)

(2) Securities, Continued

Securities with gross unrealized losses at December 31, 2007, aggregated by investment category and length of time that individual securities have been in a continuous loss position, is as follows (in thousands):

	Over Twelve Months	
	Gross Unrealized Losses	Fair Value
Mortgage-backed securities	$ (19)	2,978

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

The unrealized losses on thirteen investment securities available for sale were caused by interest rate changes. It is expected that the securities would not be settled at a price less than par value of the investments. Because the decline in fair value is attributable to changes in interest rates and not credit quality, and because the Company has the ability and intent to hold these investments until a market price recovery or maturity, these investments are not considered other-than-temporarily impaired.

The Company had no sales of securities during 2007 or 2006.

(3) Loans

The components of loans are as follows (in thousands):

	At December 31,	
	2007	2006
Commercial real estate	$ 80,652	58,146
Residential real estate and home equity	28,784	16,527
Construction	39,722	18,611
Commercial	13,889	12,751
Consumer	2,699	1,308
Total loans	165,746	107,343
Allowance for loan losses	(2,046)	(1,345)
Net deferred loan costs	351	291
Loans, net	$164,051	106,289

(continued)

(3) Loans, Continued

An analysis of the change in the allowance for loan losses follows (in thousands):

	Year Ended December 31, 2007	2006
Beginning balance	$1,345	564
Provision for loan losses	701	781
Ending balance	$2,046	1,345

The Company had no impaired loans, nonaccrual loans or loans which were over ninety days past due but still accruing interest in 2007 or 2006. During January 2008 a loan totaling $749,000 became nonaccrual.

(4) Premises and Equipment

A summary of premises and equipment follows (in thousands):

	At December 31, 2007	2006
Land	$ 3,849	2,967
Buildings	1,852	1,346
Leasehold improvements	596	584
Furniture, fixtures and equipment	2,278	1,904
Construction in process	1,837	380
Total, at cost	10,412	7,181
Less accumulated depreciation and amortization	(809)	(457)
Premises and equipment, net	$ 9,603	6,724

The Company has entered into a contract for $529,000 to construct a banking facility on SR200 in Ocala, Florida. Construction is expected to be completed during 2008.

The Company has entered into a contract for $1,097,000 to construct a banking facility on SE Maricamp Rd in Ocala, Florida. The amount remaining at December 31, 2007 was $1,047,000. Construction is expected to be completed during 2008.

The Company has entered into a contract for $1,242,000 to construct a banking facility on SW 34th Street in Gainesville, Florida. Construction is expected to be completed during 2008.

(continued)

(4) Premises and Equipment, Continued

The Company leases its Ocala corporate headquarters facility under an operating lease. This lease is for a term of five years, contains an escalation clause, requires monthly lease payments and common area maintenance charges with options to renew through 2025. Rent expense under this operating lease during the years ended December 31, 2007 and 2006 was $80,000. The Company offsets occupancy expense with sub-leases on various suites in the building. This provided rental income, net of operating expenses, for 2007 and 2006 of $35,000 and $49,000 respectively. The Bank also leased the Alachua branch from a related party for nine months in 2007 before purchasing in October 2007. Rent expense under this operating lease was $26,000 in 2007. The future minimum lease payments, which include certain renewal options, as of December 31, 2007 are as follows (in thousands):

Year Ending December 31,	Expense	Income
2008	$ 106	106
2009	80	39
2010	96	8
2011	100	6
2012	100	4
2013 and thereafter	1,262	—
	$1,744	163

(5) Deposits

A schedule of maturities of time deposits at December 31, 2007 follows (in thousands):

Year Ending December 31,	Amount
2008	$ 90,865
2009	16,346
2010	4,622
2011	2,111
2012	2,208
	$116,152

(continued)

(6) Other Borrowings

The Company enters into repurchase agreements with customers that sweep funds from deposit accounts into investment accounts. These investment accounts are not federally insured and are treated as borrowings. These agreements require the Company to pledge securities as collateral for these borrowings. At December 31, 2007 and 2006, the outstanding balance of such borrowings totaled approximately $4.8 million and $5.3 million respectively and the Company pledged securities with a carrying value of approximately $5.5 million and $8.0 million respectively as collateral for these agreements.

(7) Federal Home Loan Bank Advances

The maturity and interest rate of the Federal Home Loan Bank (“FHLB”) advances at December 31, 2007 are as follows ($ in thousands):

Maturity	Interest Rate	At December 31, 2007	At December 31, 2006
2007	5.25%	$ —	2,000
2016	4.47%	5,000	5,000
2016	4.71%	3,000	3,000
2017	4.22%	5,000	—
		$13,000	10,000

The Company has entered into a collateral agreement with the FHLB which consists of a blanket floating lien on the entire loan portfolio and the pledge of all the Company’s FHLB stock. The two advances with 2016 maturity dates have call features benefiting the issuer with call dates of May 23, 2008 and August 29, 2008 respectively. The advance with 2017 maturity date has a call features benefiting the issuer with a call date of May 19, 2008.

(8) Income Taxes

Allocation of the Federal and state income taxes (benefit) is as follows (in thousands):

	Year Ended December 31, 2007	Year Ended December 31, 2006
Deferred:		
Federal	$ 42	(170)
State	7	(29)
Income taxes (benefit)	$ 49	(199)

(continued)

(8) Income Taxes, Continued

The reasons for the differences between the statutory Federal income tax rate and the effective tax rate are summarized as follows ($ in thousands):

	Year Ended December 31,			
	2007		2006	
	Amount	% of Pretax Earnings	Amount	% of Pretax Loss
Income taxes (benefit) at statutory rate	$ 18	34.0%	$ (191)	(34.0)%
Increase (decrease) resulting from:				
State taxes, net of Federal tax benefit	5	9.6	(20)	(3.6)
Share-based compensation	18	34.6	—	
Other nondeductible expenses	8	16.0	12	2.2
Income taxes (benefit)	$ 49	94.2%	$ (199)	(35.4)%

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below (in thousands).

	At December 31,	
	2007	2006
Deferred tax assets:		
Net operating loss carryforwards	$ 529	637
Organizational and start-up costs	191	207
Allowance for loan losses	702	427
Unrealized loss on securities available for sale	—	14
Other	17	9
Deferred tax assets	1,439	1,294
Deferred tax liabilities:		
Accrual to cash conversion	(51)	(61)
Premises and equipment	(205)	(47)
Deferred loan costs	(256)	(196)
Unrealized gains on securities available for sale	(18)	—
Deferred tax liabilities	(530)	(304)
Net deferred tax asset	$ 909	990

At December 31, 2007, the Bank has approximately $1,406,000 of net operating loss carryforwards available to offset future taxable income. These carryforwards will begin to expire in 2025.

(continued)

(9) Off-Balance-Sheet Financial Instruments

The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments are commitments to extend credit, unused lines of credit and standby letters of credit and may involve, to varying degrees, elements of credit risk in excess of the amount recognized in the consolidated balance sheet. The contract amounts of these instruments reflect the extent of involvement the Company has in these financial instruments.

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

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

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. These letters of credit are primarily issued to support third-party borrowing arrangements and generally have expiration dates within one year of issuance. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. At December 31, 2007, the Company held collateral supporting substantially all of these commitments and management does not anticipate any potential losses if these letters of credit are funded.

Standby letters of credit and commitments to extend credit typically result in loans with a market interest rate when funded. A summary of the amounts of the Company's financial instruments with off-balance-sheet risk at December 31, 2007 follows (in thousands):

	Contract Amount
Commitments to extend credit	$ 9,111
Unused lines of credit	$35,199
Standby letters of credit	$ 906

(continued)

(10) Significant Group Concentrations of Credit Risk

The Company grants the majority of its loans to borrowers throughout the northeast Florida area, including Marion and Alachua counties. Although the Company has a diversified loan portfolio, a significant portion of its borrowers' ability to honor their contracts is dependent upon the economy of this area. The Company does not have any significant concentrations to any one industry or customer.

(11) Stock Option Plan

The Company adopted a stock option plan for its employees and directors (the "Plan"). Fifteen percent of the total amount of shares outstanding, up to 450,000 shares (currently 327,522 shares), have been reserved under the Plan. Stock options are granted at an exercise price equal to or greater than the fair market value of the common stock on the date of grant. Options granted to directors vest immediately and for employees, the options primarily vest over two years starting with the date of grant and ending on the second anniversary thereof. At December 31, 2007, 67,685 options remain available for granting. A summary of stock option transactions under the Plan for the years ended December 31, 2007 and 2006 follows:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Options outstanding at December 31, 2005	224,151	$ 10.00		
Options exercised	(5,000)	10.00		
Options forfeited	(1,150)	10.00		
Options outstanding at December 31, 2006	218,001	10.00		
Options exercised	(1,030)	10.18		
Options forfeited	(31,013)	10.00		
Options granted	67,850	10.50		
Options outstanding at December 31, 2007	253,808	$ 10.13	8.38 years	$ —
Options exercisable at December 31, 2007	215,216	$ 10.07	8.14 years	$ —

(continued)

(11) Stock Option Plan, Continued

There were no options granted in 2006. The fair value of each option granted for the year ended December 31, 2007 is estimated on the date of the grant using the Black-Scholes option-pricing model with the following assumptions:

	Year Ended December 31, 2007
Risk-free interest rate	4.22%
Dividend yield	— %
Expected stock volatility	6.54%
Expected life in years	5.50
Per share grant-date fair value of options issued during the year	$ 2.18

As part of its adoption of SFAS 123(R), the Company examined its historical pattern of option exercises in an effort to determine if there were any pattern based on certain employee populations. From this analysis, the Company could not identify any patterns in the exercise of options. As such, the Company used the guidance in Staff Accounting Bulletin No. 107 to determine the estimated life of options issued subsequent to the adoption of SFAS 123(R). Expected volatility is based on historical volatility of similar size financial institutions. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. The dividend yield assumption is based on the Company's history and expectation of dividend payments.

There were 1,030 options exercised during the fiscal year ended December 31, 2007 and 5,000 during the fiscal year ended December 31, 2006. There was no intrinsic value or tax benefit related to these options exercised. At December 31, 2007 there was approximately $74,000 of total unrecognized compensation expense related to the nonvested share-based compensation arrangements granted under the plans. The cost is expected to be recognized over a weighted-average period of twenty-one months. The total fair value of shares vesting and recognized as compensation expense was approximately $96,000 for the year ended December 31, 2007, and the associated income tax benefit recognized was $8,000 for the period ended December 31, 2007.

(12) Employee Benefit Plan

The Company has a 401(k) profit sharing plan available to all employees electing to participate after meeting certain length-of-service requirements. The Company contributed $87,000 to the plan in 2007, and $19,000 in 2006.

(continued)

(13) Related Party Transactions

The Company enters into transactions during the ordinary course of business with officers and directors of the Company and entities in which they hold a significant financial interest. The following summarizes these transactions (in thousands):

	At December 31, 2007	At December 31, 2006
Loan balances at end of year	$6,885	7,180
Deposits held from related parties- Balance at end of year	$7,792	4,197
Management fees and leasing commissions paid during year	$ —	21

The Company entered into a lease with Halachua Properties, LLC, which is owned by certain directors, during 2006 to rent office space for a branch in Alachua, Florida. This lease was for one year and expired in September 2007. During 2007, the Company purchased this property.

(14) Stockholders' Equity and Dividend Restrictions

During the initial offering of common stock, the Company sold units, with each unit containing one share of common stock and one warrant. Each warrant entitles the holder to purchase one share of additional common stock for $10 at any time over a three-year period. Warrants totaling 575,315 in 2007 and 87,940 in 2006 were exercised with 650,857 warrants remaining unexercised as of December 31, 2007.

The Company called 50% of the initial warrant amount in February 2007. The remaining 50% will expire on February 28, 2008 unless called earlier by the Company.

The Company is limited in the amount of dividends it may pay by the amount of dividends the Bank may pay to the Holding Company. The Bank is limited in the amount of cash dividends that may be paid by Florida law. The amount of cash dividends that may be paid is based on the Bank's net earnings of the current year combined with the Bank's retained earnings of the preceding two years, as defined by state banking regulations. However, for any dividend declaration, the Bank must consider additional factors such as the amount of current period net earnings, liquidity, asset quality, capital adequacy and economic conditions. It is likely that these factors would further limit the amount of dividends which the Bank could declare. In addition, bank regulators have the authority to prohibit banks from paying dividends if they deem such payment to be an unsafe or unsound practice.

(continued)

(15) Regulatory Matters

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and percents (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 2007, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2007, the most recent notification from the regulatory authorities categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as adequately capitalized the Bank must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage percents as set forth in the table. There are no conditions or events since that notification that management believes have changed the Bank's category. The Bank's actual capital amounts and percents are also presented in the table ($ in thousands):

	Actual		For Capital Adequacy Purposes		For Well Capitalized Purposes	
	Amount	Percent	Amount	Percent	Amount	Percent
As of December 31, 2007:						
Total Capital (to Risk- Weighted Assets)	$20,844	11.52%	$14,475	8.00%	$18,094	10.00%
Tier I Capital (to Risk- Weighted Assets)	18,798	10.39	7,237	4.00	10,855	6.00
Tier I Capital (to Average Assets)	18,798	9.20*	8,173	4.00*	10,216	5.00*
As of December 31, 2006:						
Total Capital (to Risk- Weighted Assets)	13,888	11.56	9,611	8.00	12,013	10.00
Tier I Capital (to Risk- Weighted Assets)	12,543	10.44	4,806	4.00	7,208	6.00
Tier I Capital (to Average Assets)	12,543	9.35*	5,366	4.00*	6,707	5.00*

* The Bank is required to maintain an 8.00% Tier I capital ratio throughout the first of three years of operations.

(continued)

(16) Fair Value of Financial Instruments

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

	At December 31,			
	2007		2006	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and cash equivalents	$ 3,638	3,638	6,734	6,734
Interest bearing time deposits in banks	2,046	2,046	1,000	1,000
Securities available for sale	20,537	20,537	13,837	13,837
Loans, net	164,051	162,835	106,289	104,356
Loans held for sale	—	—	2,436	2,479
Accrued interest receivable	931	931	648	648
Federal Home Loan Bank stock	836	836	595	595
Financial liabilities:				
Deposits	164,243	164,301	109,072	108,603
Other borrowings	4,807	4,807	5,339	5,339
Federal Home Loan Bank advances	13,000	12,484	10,000	9,981
Accrued interest payable	799	799	400	400
Off-balance-sheet financial instruments	—	—	—	—

(17) Legal Contingencies

Various legal claims arise from time to time in the normal course of business which, in the opinion of management, will not have a material effect on the Company's financial statements.

(continued)

(18) Holding Company Only Financial Information

The Holding Company's unconsolidated financial information is as follows (in thousands):

Condensed Balance Sheets

	At December 31, 2007	At December 31, 2006
Assets		
Cash	$ 539	810
Investment in subsidiary	19,638	13,484
Other assets	82	55
Total assets	$20,259	14,349
Liabilities and Stockholders' Equity		
Other liabilities	8	12
Stockholders' equity	20,251	14,337
Total liabilities and stockholders' equity	$20,259	14,349

Condensed Statements of Operations

	Year Ended December 31, 2007	Year Ended December 31, 2006
Revenues	$ 52	—
Operating expenses, net of income tax benefit	152	75
Net loss before earnings (loss) of subsidiary	(100)	(75)
Earnings (loss) of subsidiary	103	(288)
Net earnings (loss)	$ 3	(363)

(continued)

(18) Holding Company Only Financial Information, Continued

Condensed Statements of Cash Flows

	Year Ended December 31, 2007	2006
Cash flows from operating activities:		
Net loss	$ 3	(363)
Adjustment to reconcile net earnings (loss) to net cash used in operating activities:		
Share-based compensation	96	—
Equity in (earnings) loss of subsidiary	(103)	288
Increase in other assets	(27)	(45)
(Decrease) increase in other liabilities	(4)	11
Net cash used in operating activities	(35)	(109)
Cash flows from investing activity-		
Investment in subsidiary	(6,000)	—
Cash flows from financing activities:		
Net decrease in other borrowings	—	(13)
Common stock warrants and options exercised	5,764	930
Net cash provided by financing activities	5,764	917
Net (decrease) increase in cash	(271)	808
Cash at beginning of the year	810	2
Cash at end of year	$ 539	810
Supplemental disclosure of cash flow information:		
Noncash transaction- Accumulated other comprehensive loss, unrealized loss on securities available for sale of subsidiary, net of tax benefit	$ 51	(21)

Exhibit 31.1

CERTIFICATIONS OF PRINCIPAL EXECUTIVE OFFICER

I, Jon M. Kurtz, certify that:

1. I have reviewed this annual report on Form 10-KSB of Alarion Financial Services, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer, as of, and for, the periods presented in this report;

4. The small business issuer's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the small business issuer and have:

   a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report are conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   c) disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's fourth fiscal quarter that has materially affected or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting.

5. The small business issuer's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of small business issuer's board of directors (or persons performing the equivalent functions):

   a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal controls over financial reporting.

Date: March 27, 2008

By: /s/ Jon M. Kurtz
Jon M. Kurtz
Principal Executive Officer

Exhibit 31.2

CERTIFICATIONS OF CHIEF FINANCIAL OFFICER

I, Matthew Ivers, certify that:

1. I have reviewed this annual report on Form 10-KSB of Alarion Financial Services, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer, as of, and for, the periods presented in this report;
4. The small business issuer's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the small business issuer and have:
   a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report are conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   c) disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's fourth fiscal quarter that has materially affected or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting.
5. The small business issuer's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of small business issuer's board of directors (or persons performing the equivalent functions):
   a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and
   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal controls over financial reporting.

Date: March 27, 2008

By: /s/ Matthew Ivers
Matthew Ivers
Chief Financial Officer

Exhibit 32.1

CERTIFICATIONS PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED PURSUANT TO SECTION 906 OF SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Alarion Financial Services, Inc. (the "Company"), on Form 10-KSB for the period ended December 31, 2007, as filed with the Securities and Exchange Commission (the "Report"), I, Jon M. Kurtz, Principal Executive Officer, President, and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as added by Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. To my knowledge, the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of and for the period covered by the Report.

Date: March 27, 2008

By: /s/ Jon M. Kurtz
Jon M. Kurtz, Principal Executive Officer

Exhibit 32.2

CERTIFICATIONS PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED PURSUANT TO SECTION 906 OF SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Alarion Financial Services, Inc. (the "Company"), on Form 10-KSB for the period ended December 31, 2007, as filed with the Securities and Exchange Commission (the "Report"), I, Matthew Ivers, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as added by Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. To my knowledge, the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of and for the period covered by the Report.

Date: March 27, 2008

By: /s/ Matthew Ivers
Matthew Ivers, Chief Financial Officer