POWER EFFICIENCY CORP
Form 10-K
March 31, 2010

Securities and Exchange Commission
Washington, D.C. 20549

FORM 10-K

x	Annual report under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2009

o	Transition report under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from __________ to __________

Commission File Number: 000-31805

Power Efficiency Corporation
(Exact name of registrant as specified in its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	22-3337365 (I.R.S. Employer Identification No.)
3960 Howard Hughes Pkwy, Ste 460 Las Vegas, NV (Address of Principal Executive Offices)	89169 (Zip Code)

(702) 697-0377
(Issuer's Telephone Number, Including Area Code)

Securities Registered under Section 12(g) of the Exchange Act:

Common Stock, $.001 Par Value
(Title of Class)

Check whether the Company: (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 Company was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-K contained in this form, and no disclosure will be contained, to the best of Company's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 and Regulations S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o

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

Large accelerated filer o	Accelerated filer o	Non-accelerated filer o	Smaller reporting company x

Indicate by check mark whether the Company is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

As of June 30, 2009, the aggregate market value of the common stock held by non-affiliates of the issuer was $4,952,150. This amount is based on the closing price of $0.15 per share for the Company’s common stock as of such date.

On March 31, 2010 there were 44,825,883 shares of the Company’s common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

None.

In this report, references to “we”, “us” or “our” collectively refer to Power Efficiency Corporation.

SPECIAL CAUTIONARY NOTICE REGARDING FORWARD-LOOKING STATEMENTS

This report and the documents incorporated into this report contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (the “PSLRA”), including, but not limited to, statements relating to the Company’s business objectives and strategy. Such forward-looking statements are based on current expectations, management beliefs, certain assumptions made by the Company’s management, and estimates and projections about the Company’s industry. Words such as “anticipates,” “expects,” “intends,” “plans,” “believes,” “seeks,” “estimates,” “forecast likely,” “predicts,” “projects,” “judgment,” variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions that are difficult to predict with respect to timing, extent, likelihood and degree of occurrence. Therefore, actual results and outcomes may differ materially from those expressed, forecasted, or contemplated by any such forward-looking statements.

Factors that could cause actual events or results to differ materially include, but are not limited to, the following: continued market acceptance of the Company’s products; the Company’s ability to expand and/or modify its products on an ongoing basis; general demand for the Company’s products, intense competition from other developers, manufacturers and/or marketers of energy reduction and/or power saving products; the Company’s negative net tangible book value; the Company’s negative cash flow from operations; delays or errors in the Company’s ability to meet customer demand and deliver products on a timely basis; the Company’s lack of working capital; the Company’s need to upgrade its facilities; changes in laws and regulations affecting the Company and/or its products; the impact of technological advances and issues; the outcomes of pending and future litigation and contingencies; trends in energy use and consumer behavior; changes in the local and national economies; and other risks inherent in and associated with doing business in an engineering and technology intensive industry. See “Management’s Discussion and Analysis or Plan of Operation.” Given these uncertainties, investors are cautioned not to place undue reliance on any such forward-looking statements.

Unless required by law, the Company undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise. However, readers should carefully review the risk factors set forth in other reports or documents that the Company files from time to time with the Securities and Exchange Commission (the “SEC”), particularly Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and any Current Reports on Form 8-K.

GLOSSARY OF TERMS

Set forth below are technical terms used in the discussion in this document and explanations of the meanings of those terms.

Alternating Current (AC)	A type of electrical current, the direction of which is reversed at regular intervals or cycles; in the U.S. the standard is 120 reversals or 60 cycles per second; typically abbreviated as AC.
Ampere (amp)	A unit of measure for an electrical current; the amount of current that flows in a circuit; abbreviated as amp.
Current (Electrical)	The flow of electrical energy (electricity) in a conductor, measured in amperes.
Cycle	In an alternating current, the current goes from zero potential (or voltage) to a maximum in one direction, back to zero, and then to a maximum potential (or voltage) in the other direction. The number of complete cycles per second determines the current frequency; in the U.S. the standard for alternating current is 60 cycles.
Efficiency	Efficiency is the ratio of work (or energy) output to work (or energy) input, and cannot exceed 100 percent.
Energy	The capability of doing work.
Horsepower (HP)	A unit for measuring the power of motors or the rate of doing work. One horsepower equals 33,000 foot-pounds of work per minute or 746 watts.
Induction	The production of an electric current in a conductor by the variation of a magnetic field in its vicinity.
Induction Motor	The simplest and most rugged electric motor, it consists of a wound stator and a rotor assembly. The AC induction motor is so named because the electric current flowing in its secondary member (the rotor) is induced by the alternating current flowing in its primary member (stator). The power supply is connected only to the stator. The combined electromagnetic efforts of the two currents produce the force to create rotation.
Inrush Current	The current that flows at the instant of connection of a motor to the power source. Usually expressed as a multiple of motor full-load current.
Kilowatt (kW)	A standard unit of electrical power equal to one thousand watts.
Load	The demand on an energy producing system. The energy consumption or requirement of a piece or group of equipment.
Motor	A machine supplied with external energy that is converted into force and/or motion.
Power	The rate at which work is done, typically measured in watts or horsepower.
Power Factor	The ratio of watts to volt-amperes of an AC electric circuit.

Soft-start	Soft-start is the regulation of the supply voltage from an initial low value to full voltage during the starting process.
Torque (Motor)	The rotating force provided by a motor. The units of torque may be expressed as pound-foot, pound-inch (English system), or newton-meter (metric system).

Torque (Starting)	This torque is what is available to initially get the load moving and begin its acceleration.
Transformer	An electromagnetic device that changes the voltage of alternating current electricity; it consists of an induction coil having a primary and secondary winding and a closed iron core.
Voltage	The amount of electromotive force, measured in volts that exists between two points.
Watt	The amount of power required maintaining a current of one ampere at a pressure of one volt when the two are in phase with each other. One horsepower is equal to 746 watts.

PART I

Item 1. Description of Business.

(a) Business Development

Formation

Power Efficiency Corporation (the “Company”) was incorporated in Delaware on October 19, 1994. From inception through 1997, the Company was a development stage entity that was engaged in the design, development, marketing and sale of proprietary solid state electrical components designed to reduce energy consumption in alternating current induction motors. Alternating current induction motors are commonly found in industrial and commercial facilities throughout the world.

(b) Business of the Company

The Company’s Principal Products and Technology

In the late 1990s the Company commenced the sale of its initial product, which was based on analog technology and reduces energy consumption in alternating current induction motors in certain applications. This product has been known by several names, including the Power Commander® and Power Genius. In 2005 the Company began development of a digital product that would overcome many of the commercial limitations of the analog product. In 2008, limited models of the first-generation of the digital product were launched. In mid-2009 the Company launched a line of products up to 300 horsepower that had certification from Underwriters Laboratories (“UL”) and its second-generation digital circuitry was launched. Going forward, the Company has chosen to call its products Motor Efficiency Controllers (“MEC”).

The Company has developed patented and patent-pending technologies for effectively controlling the energy usage of an electric motor. The Company’s first United States Patent was granted in 1998. Over the past four years the Company has undertaken extensive study and computer modeling of motors and their energy use, and has developed digital technologies for its controllers. In the process, the Company has discovered what it believes are significant innovations and has completed numerous patent filings around these new inventions. The Company has branded these collective patented and patent pending technologies as E-SAVE Technology® and has a registered trademark on this name.

The Company has developed technologies and products for use on three-phase and single-phase motors. Three-phase power and motors are generally found in industrial and commercial buildings for larger applications than single-phase power and motors.

The Company’s marketing efforts initially focused on the three-phase version but it is also now marketing the single-phase product. The Company’s digital Three-Phase MEC is designed to have the following functionality:

1. Start a motor

2. Provide a soft start for the motor, bringing it gradually from rest to full speed

3. Provide various motor protection capabilities, such as sensing current overload, phase loss, under- and over-voltage, and more.

4. Save energy when the motor is at full speed but is less than fully loaded

The Company's digital Single-Phase MEC is designed to have the following functionality:

1. Start a motor
2. Provide a soft start for the motor, bringing it gradually from rest to full speed
3. Save energy when the motor is at full speed but is less than fully loaded

Three-Phase and Single-Phase MECs are unique particularly because of their energy savings capabilities. The product reduces energy consumption by electric motors by electronically sensing and controlling the amount of energy the motor consumes. A motor with an MEC installed only uses the energy it needs to perform its work task, thereby increasing its efficiency. The result is a reduction of energy consumption typically ranging from 15% - 35% in applications that do not always run at peak load levels. The amount of energy savings depends on a variety of factors, including the load on the motor and the motor's characteristics.

The Company's management believes its Motor Efficiency Controllers offer certain advantages over competing products for the following reasons:

- Motor and Equipment Life: The MEC extends motor life by reducing the stress and strain on the motor and surrounding equipment, and reduces the amperage to the motor, which results in cooler running.

- Successful Utility and Customer Tests: The MEC has been successfully tested by numerous electric utilities and customers. For example, Paragon Consulting Services, a contractor for Nevada Power Company, the electric utility for southern Nevada, performed 8 field tests on escalators and one on an elevator in major Las Vegas casinos. The tests resulted in average energy savings of over 30% on the escalators and 20% on the elevator.

- Utility Incentive Financing: The three-phase product has qualified for rebate incentive financing, most frequently called "rebates", from many electric utilities. This financing is generally paid to the end user of the MEC as an incentive to invest in energy saving products. As such, this financing effectively decreases the cost of the Company's MEC for end users. The utilities that have approved the Company's products for incentive financing include: NV Energy (formerly Nevada Power Company and Sierra Pacific Power Company), the Los Angeles Department of Water and Power, Southern California Edison, Sacramento Municipal Utility District, Anaheim Utilities, the New York Power Authority, Excel Energy and San Diego Gas and Electric.

- Acceptance by Original Equipment Manufacturers: The Company's products have been approved and installed by numerous original equipment manufacturers ("OEMs") in the escalator and granulator industries.

Three-Phase MEC

The Company initially focused its marketing efforts for the Three-Phase MEC in the elevator and escalator industry, although the Company is also actively marketing this product to industrial markets, such as recycling, mining, plastics, and manufacturing. Industries that operate equipment such as conveyor systems, crushing equipment, stamping presses, granulators, grinders, shredders and other motor driven equipment with varying loads, are believed to be viable target markets for the Three-Phase MEC. The Company is seeking to target markets with appropriate applications and market access, using direct sales, OEMs, distributors and independent representatives to address these markets.

Single-Phase Product

Like the Company's three-phase product described above, the Company's single-phase product reduces energy consumption in electric motors by sensing and controlling the amount of energy the motor consumes. Many motors commonly used in home appliances and other consumer goods are single-phase AC motors. Since the single-phase product is much smaller, has a much lower price point, and can be incorporated directly into a broad variety of applications, the Company believes it is a product most suitable for installation at the OEM level.

Product Development

The Company has devoted significant time and resources in the past several years toward developing "digital" versions of its three-phase and single-phase products. Through this process, the Company has transformed its technology so that its key technological breakthroughs are primarily incorporated in algorithms and software on a microchip. The Company believes the digital versions of its products have several distinct advantages over the older analog versions, including:

- Motor starter and motor protection capabilities similar to standard solid state starters sold by large motor control companies. The analog product could not start a motor and provided no motor protection, so the customer had to purchase these items at additional costs for components and installation. The digital MEC instead incorporates all these functions and therefore replaces a standard solid state motor control.

- Increased ease of installation and reduced technical support requirements. For example, instead of approximated and manual adjustments during installation, which can require technical support from the Company, the digitized unit will allow more simplified and precise adjustments by customers and third party installers.

- Reduced product size, which is important for many installations.

- Input-output communications capabilities, so the device can communicate with external control systems.

- Increased functionality. The Company expects to be able to add new functionality to the products. These new functions may include such things as:

- Recording and reporting of actual energy savings;

- Prediction of maintenance problems by reading and reporting on changes in the motor's operating characteristics; and

- More secure intellectual property protection through the use of secured chips and software.

Marketing and Sales

The Company's marketing efforts have historically been concentrated in the elevator and escalator industry, primarily to OEMs of elevator and escalator equipment and end users that own this equipment. With UL approval in mid-2009, the Company has targeted more heavily industrial markets, such as mining aggregates and plastics. End users of the Company's products include retail chains, hotels, airports, transit systems, and mining, plastics and manufacturing companies.

The Company sells products into the elevator and escalator market primarily to and through large OEM resellers. The elevator and escalator market is dominated by four global companies, Otis Elevator, Schindler, ThyssenKrupp and KONE. Collectively these companies are believed to have over 80% of the world market for new equipment and service contracts. The Company has formal supply agreements for North America with ThyssenKrupp and KONE. The Company also sells to and completes projects with Otis Elevator and Schindler.

The Company is focused on penetrating industrial markets through independent representatives and distributors who will in turn sell to OEMs of industrial equipment and end users. The Company significantly increased these industrial market activities in late 2009 after receiving UL certification, since this certification is required by many industrial concerns.

The Company’s longer term goal is to be a high value supplier of technologies, with numerous OEMs and other resellers engaged with high volume sales and/or licensing agreements.

Manufacturing and Distribution

The Company’s products are manufactured internally and by a multi-billion dollar global contract manufacturer, Sanmina SCI (“Sanmina”). The Company’s strategy is to manufacture internally products that sell at lower volumes, such as MECs for very large motors, and to outsource the manufacturing of higher volume products, such as smaller units and circuit boards. The Company believes this strategy allows for high quality production, cost efficiencies, and the capability to rapidly increase production volumes. Management believes this strategy has the ability to meet the Company’s production needs and the Company would be successful in finding alternative manufacturers should Sanmina not be available to manufacture our product.

Competition

Power Efficiency believes the principal competitive factors in the Company’s markets include innovative product development, return on investment from energy savings, product quality, product performance, utility rebate acceptance, established customer relationships, name recognition, distribution and price.

Three-Phase Competition. The Company’s Three-Phase MEC’s principal capabilities include being a motor starter, providing a soft start and protection for the motor, and reducing the motor’s electricity consumption once the motor is at full speed. The Company believes its products are unique primarily because of the last capability – energy savings.

The first capabilities - starting, soft starting and protecting a motor - are commonly found in existing motor control products. There are billions of dollars of motor starters and soft starts sold every year. These products are typically manufactured and marketed by large motor control companies, many of which have longer operating histories, established markets and far greater financial, advertising, research and development, manufacturing, marketing, personnel and other resources than the Company currently has or may reasonably be expected to have in the foreseeable future. This competition may have an adverse effect on the ability of the Company to commence and expand its operations or operate in a profitable manner.

There are also several small companies that reportedly make products that combine motor starting, soft starting and energy savings. The Company is unaware of any large company that makes a product of this nature. Although the Company has not completed any formal market study, the Company believes its Three-Phase MEC has the following competitive advantages over other products:

- It combines soft start features with energy savings features in a single integrated unit that is CSA, UL and CE certified and has achieved energy savings levels of up to 15% to 35% in independent, third party testing;

- Its circuitry is proprietary, protected by one patent. Three additional patent filings on new innovations are pending approval of the U.S. Patent and Trademark Office;

- It has been tested extensively by utilities with documented energy savings and approval for incentive financing rebates;

- It is accepted by OEMs in the escalator and granulator industries.

Single-Phase Competition. There have been several companies that have, with different technologies, attempted to exploit this market due to the enormous opportunity in single-phase motor applications. These products include among others, “Green Plug” (voltage clamping), “Power Planner” (digital microchip) and “Econelectric” (power factor control). The Company has made numerous innovations in the past three years that it believes overcome many of the problems with these and the Company’s earlier designs. The Company has filed for a patent on these innovations and has reduced the product in size and cost to the point it can be sold to OEMs of applicable appliances and other equipment driven by single-phase AC motors.

Premium Efficiency Motors. Motors are rated by their efficiency at full load. However, when motors, including "premium efficiency motors" are lightly loaded, they become very inefficient. Management believes that the energy savings gain attributable to premium efficiency motors is materially lower than that of its MEC on underloaded motor applications. Furthermore, the Company's products are able to save energy on underloaded premium efficiency motors, so that such motors and the Company's technology are not mutually exclusive.

Source of Supply and Availability of Raw Materials

The MEC has been designed to use standard, off-the-shelf, easily acquired components, except for the custom made circuit boards. Such off-the-shelf components are basic items readily available worldwide at competitive prices. They come in standard and miniature versions and offer the Company latitude in product design and production. Although the Company believes most of the key components required for the production of its products are currently available in sufficient production quantities from multiple sources, there can be no assurance they will remain so readily available or at comparable prices.

Customers

The Company currently does business with approximately 20 customers. Of this number, four customers presently account for approximately 71% of the Company's gross revenues. These customers and their respective gross revenue percentages are KONE – 49%; IXYS – 8%; Otis – 7%; and Global PET – 7%. The Company is, and may continue to be, dependent upon a limited number of customers. Accordingly, the loss of one or more of these customers may have a material adverse effect upon the Company's business.

Patents and Proprietary Rights

The Company currently relies on a combination of trade secrets, non-disclosure agreements and patent protection to establish and protect its proprietary rights in its products. There can be no assurance these mechanisms will provide the Company with any competitive advantages. Furthermore, there can be no assurance others will not independently develop similar technologies, duplicate or "reverse engineer" the proprietary aspects of the Company's technology.

The Company has one U.S. patent issued with respect to its products. The "Balanced and Synchronized Phase Detector for an AC Induction Motor Controller," No. 5,821,726, was issued on October 13, 1998 and expires in 2017. This patent covers improvements to the technology under the NASA License Agreement (described below), which were developed by the Company. Management believes this patent protects the Company's intellectual property position beyond the expiration of the NASA License Agreement.

The Company has filed three utility patents on new inventions associated with the development of its digital products. The Company is continually making improvements to its products and technologies, and anticipates making additional patent filings on new inventions when warranted.

The Company has obtained U.S. Trademark registration of the E-Save Technology® mark.

NASA License Agreement

The Company had been the exclusive United States licensee of certain power factor controller technology owned by the United States of America, as represented by NASA. This license agreement covered the United States and its territories and possessions and did not require the Company to pay royalties to NASA in connection with the Company's sale of products employing technology utilizing the licensed patents. The Company's rights under the license agreement were non-transferable and were not to be sublicensed without NASA's consent. The license agreement terminated on December 16, 2002 upon expiration of all of the licensed patents.

The Company believes its products and other proprietary rights do not infringe any proprietary rights possessed by third parties. There can be no assurance, however, that third parties will not assert infringement claims in the future, the defense costs of which could be substantial.

Government Regulation

The Company is not required to be certified by any government agencies. However, most of the Company's products are manufactured to comply with specific codes that meet industry accepted safety standards. Presently, many of the Company's products are certified to comply with UL 508 Industrial Control Equipment and the Company has also received certification meeting CSA (Canadian Standards Association) B44.1/ASME-17.5 Elevator and Escalator Electrical Equipment for many of the Company's products. Many of the Company's products are also CE marked. The Department of Commerce does not require the Company's technology to be certified for export. The Company's industrial code is 421610 and the SIC code is 5063.

Deregulation of Electrical Energy

Sales of the Company's product are not dependent on deregulation of the electrical energy market as the Company's product can be sold in regulated and deregulated markets.

Research and Development

The Company intends to continue its research and development effort to introduce new products based on its energy saving technology. Towards this end, the Company spent $953,004 and $1,016,158 in fiscal years 2009 and 2008, respectively, on research and development activities, virtually none of which was borne by customers. A major focus of the Company's foreseeable research and development activities will be on completing additional features and refinements to the three-phase and single phase products. The Company also anticipates the possibility of working with OEMs that make or purchase motor control equipment, in order to develop products with features or specifications they require.

Effect of Environmental Regulations

The Company is not aware of any federal, state, or local provisions regulating the discharge of materials into the environment or otherwise relating to the protection of the environment with which compliance by the Company has had, or is expected to have, a material effect upon the capital expenditures, earnings, or competitive position of the Company.

Employees

At the date of this document, the Company employs fourteen people. Of this number, two are engaged in accounting and finance, three in operations and general management, three in sales and marketing, and six in product research and development, engineering and manufacturing. At such time as business conditions dictate, the Company may hire additional personnel for, among other things, increased engineering, marketing and sales. The Company has no collective bargaining agreements and considers its relationship with its employees to be good. The Company utilizes consultants in the areas of marketing, product and technology development and finance on a regular basis.

(c) Reports to Security Holders

The Company is a smaller reporting company, and as such files Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q under the scaled disclosure requirements and Current Reports on Form 8-K on a regular basis with the SEC.

The public may read and copy any materials the Company files with the SEC at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC at http://www.sec.gov.

Item 1A. Risk Factors.

RISKS RELATED TO OUR BUSINESS

Unless We Achieve Profitability and Related Positive Cash Flow, We May Not Be Able To Continue Operations, And Our Auditors Have Questioned Our Ability To Continue As A "Going Concern".

The Company has suffered recurring losses from operations, and experienced a deficiency of cash of approximately $3,000,000 and $3,100,000 from operations for the years ended December 31, 2009 and 2008, respectively. For the years ended December 31, 2009 and December 31, 2008, we had net losses of $4,168,708 and $3,948,204, respectively. In our Auditors' Report dated March 31, 2010 on our December 31, 2009 financial statements included in this report, our auditors have stated that these factors raise substantial doubt about our ability to continue as a "going concern". Our financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amount of liabilities that might be necessary should we be unable to continue in existence.

The Company's continuation as a "going concern" is dependent upon achieving profitable operations and related positive cash flow and satisfying our immediate cash needs by external financing until we are profitable. Our plans to achieve profitability include developing new products, obtaining new customers and increasing sales to existing customers. We are seeking to raise additional capital through equity issuance, debt financing and other types of financing, but we cannot guarantee that sufficient capital will be raised.

We Have A Limited Operating History, Have Experienced Recurring Losses And Have Limited Revenue.

To date, and due principally to a lack of working capital, our operations have been limited in scale. Although we have an arrangement with an outsourced production facility to manufacture our products, have established relationships with suppliers, and have received contracts for our products, we may experience difficulties in production scale-up, product distribution, and obtaining and maintaining working capital until such time as our operations have been scaled-up to acceptable commercial levels. We have not had a profitable quarter in the past three years and we cannot guarantee we will ever operate profitably. In addition, we have limited revenue. For the year ended December 31, 2009, our total revenues were $283,990, and for the year ended December 31, 2008, our total revenues were $480,513.

We Do Not Have A Bank Line Of Credit.

At the present time, we do not have a bank line of credit, which further restricts our financial flexibility.

We Will Require Additional Funds To Meet Our Cash Operating Expenses And Achieve Our Current Business Strategy.

The Company continues to have limited working capital and will be dependent upon additional financing to meet capital needs and repay outstanding debt. We cannot guarantee additional financing will be available on acceptable terms, if at all. We also need additional financing to raise the capital required to fully implement our business plan. Our current operating expense level is approximately $250,000 to $300,000 per month. Management is seeking to raise additional capital through equity issuance, debt financing or other types of financing. However, there are no assurances that sufficient capital will be raised.

When our operations require additional financing, if we are unable to obtain it on reasonable terms, we would be forced to restructure, file for bankruptcy or cease operations, any of which could cause you to lose all or part of your investment in us.

Our Management Group Owns Or Controls A Significant Number Of The Outstanding Shares Of Our Common Stock And Will Continue To Have Significant Ownership Of Our Voting Securities For The Foreseeable Future.

As of the date of this report, management controls approximately twenty-two percent (22%) of our issued and outstanding Common Stock and voting equivalents. Additionally, Summit Energy Ventures, LLC ("Summit") owns twelve percent (12%) of our common stock and voting equivalents, which is included in the above number. Summit is controlled by Steven Strasser, our Chairman and CEO, and he has the right to vote all shares owned by Summit. BJ Lackland, our CFO, owns a minority equity interest in Summit. As a result, these persons will have the ability, acting as a group, to greatly influence our affairs and business, including the election of directors and, subject to certain limitations, approval or preclusion of fundamental corporate transactions. This concentration of ownership of our common stock may:

- delay or prevent a change in the control;
- impede a merger, consolidation, takeover, or other transaction involving the Company; or

- discourage a potential acquirer from making a tender offer or otherwise attempting to obtain control of the Company.

The relationships between Summit and our executive officers are discussed in more detail under “Certain Relationships And Related Party Transactions” herein.

Our Business Depends Upon The Maintenance Of Our Proprietary Technology, And We Rely, In Part, On Contractual Provisions To Protect Our Trade Secrets And Proprietary Knowledge.

The Company depends upon its proprietary technology, relying principally upon trade secret and patent law to protect this technology. The Company also regularly enters into confidentiality agreements with key employees, customers, potential customers, and vendors and limits access to and distribution of trade secrets and other proprietary information. However, these measures may not be adequate to prevent misappropriation of our technology. Additionally, our competitors may independently develop technologies substantially equivalent or superior to our technology. In addition, the laws of some foreign countries do not protect our proprietary rights to the same extent as the laws of the United States. We also are subject to the risk of adverse claims and litigation alleging infringement of intellectual property rights of others.

Confidentiality agreements to which we are party may be breached, and we may not have adequate remedies for any breach. Our trade secrets may also be known without breach of such agreements or may be independently developed by competitors. Our inability to maintain the proprietary nature of our technology and processes could allow our competitors to limit or eliminate any competitive advantages we may have.

We Are Dependent On Third-Party Suppliers.

Although we believe most of the key components required for the production of our products are currently available in sufficient production quantities from multiple sources, they may not remain so readily available. It is possible that other components required in the future may necessitate custom fabrication in accordance with specifications developed or to be developed by us. Also, in the event that we, or our contract manufacturer, as applicable, are unable to develop or acquire components in a timely fashion, our ability to achieve production yields, revenues and net income can be expected to be adversely affected. Additionally, we are dependent on Sanmina-Sci to manufacture our higher volume products. While we believe we would be successful in finding alternative manufacturers should this manufacturer not be available to manufacture our product, it could take substantial time and effort to locate such alternatives and, depending on the timing of the loss of Sanmina-Sci, could result in disruption in delivery schedules and harm to our clients, our reputation and future prospects.

We Are Developing And Commercializing New Energy Saving Technologies And Products Which Will Involve Uncertainty And Risks Related To Product Development And Market Acceptance.

Our success is dependent, to a large degree, upon our ability to fully develop and commercialize our technology and gain industry acceptance of our products based upon our technology and its perceived competitive advantages. Accordingly, our prospects must be considered in light of the risks, expenses and difficulties frequently encountered in connection with the establishment of a new business in a highly competitive industry, characterized by frequent new product introductions. We anticipate that we will incur substantial expense in connection with the development and testing of our proposed products and expect these expenses to result in continuing and significant losses until such time, if ever, that we are able to achieve adequate levels of sales or license revenues.

We Have Limited Experience in Direct Sales.

Our products have been distributed primarily through OEMs. We have recently begun pursuing an expanded distribution strategy designed to reduce our reliance on OEMs. Pursuant to this strategy, we are increasing our direct sales efforts into new markets. Our future growth and profitability will depend upon the successful development of business relationships with additional OEMs, growth in direct sales, and sales through select resellers and reps to penetrate the market with our products.

We Currently Depend On A Small Number Of Customers And Expect To Continue To Do So.

The Company currently does business with approximately 20 customers. Of this number, four customers accounted for approximately 71% of our gross revenues in 2009. We are, and may continue to be, dependent upon a small number of customers. Accordingly, the loss of one or more of these customers is likely to have a material adverse effect on our business.

Most Of Our Current And Potential Competitors Have Greater Name Recognition, Financial, Technical And Marketing Resources, And More Extensive Customer Bases And Industry Relationships Than We Do, All Of Which Could Be Leveraged To Gain Market Share To Our Detriment, Particularly In An Environment Of Rapid Technological Change.

We compete against a number of companies in the electric motor energy savings market, many of which have longer operating histories, established markets and far greater financial, advertising, research and development, manufacturing, marketing, personnel and other resources than we currently have or may reasonably expect to have in the foreseeable future. This competition may have an adverse effect on our ability to expand our operations or operate profitably. The motor control industry is also highly competitive and characterized by rapid technological change. Our future performance will depend in large part upon our ability to become and remain competitive and to develop, manufacture and market acceptable products in these markets. Competitive pressures may necessitate price reductions, which can adversely affect revenues and profits. If we are not competitive in our ongoing research and development efforts, our products may become obsolete, or be priced above competitive levels. However, management believes, based upon their performance and price, our products are attractive to customers. We cannot guarantee that competitors will not introduce comparable or technologically superior products, which are priced more favorably than our products.

Changes In Retail Energy Prices Could Affect Our Business.

We have found that a customer's decision to purchase an MEC (or similar product) is primarily driven by the payback on the investment resulting from the increased energy savings. Although management believes that current retail energy prices support an attractive return on investment for our products, the future retail price of electrical energy may not remain at such levels, and price fluctuations reducing energy expense could adversely affect product demand.

Loss Of Key Personnel Could Have Significant Adverse Consequences.

We currently depend on the services of Steve Strasser, and BJ Lackland, our Chief Executive Officer and Chief Financial Officer, respectively. The loss of the services of either of these persons could have an adverse effect on our business. As discussed under "Management", we have entered into long-term employment contracts with Messrs. Strasser and Lackland, but such contracts do not guarantee they will remain with us.

We Do Not Have "Key Man" Life Insurance.

The Company presently does not have any key man life insurance policies. As soon as practicable following the commencement of profitable operations (which may never occur), we intend to purchase key man life insurance on the life of our principal executive officer, Steven Strasser. Upon purchase of such insurance, we intend to pay the premiums and be the sole beneficiary. The lack of such insurance may have a material adverse effect upon our business.

Delaware Law Limits The Liability Of Our Directors.

Pursuant to our Certificate of Incorporation, the Company's directors are not liable to us or our stockholders for monetary damages for breach of fiduciary duty, except for liability in connection with a breach of the duty of loyalty, for acts or omissions not in good faith or which involved intentional misconduct or a knowing violation of law for dividend payments or stock repurchases illegal under Delaware law or any transaction in which a director has derived an improper personal benefit.

Potential Product Liability Claims May Not Be Fully Covered By Insurance.

The Company may be subject to potential product liability claims that could, in the absence of sufficient insurance coverage, have a material adverse impact on us. Presently, we have general liability coverage that includes product liability up to $2,000,000 and umbrella liability up to $4,000,000. Any large product liability suits occurring early in our growth may significantly and adversely affect our ability to expand the market for our products.

RISKS RELATED TO OUR COMMON STOCK AND CAPITAL STRUCTURE

Trading In Our Common Stock Over The Last 12 Months Has Been Limited, So Investors May Not Be Able To Sell As Many Of Their Shares As They Want At Prevailing Prices.

Prices of our common stock are quoted on the OTC Bulletin Board. Approximately 26,000 shares were traded on an average daily trading basis for the 12 months ended December 31, 2009. If limited trading in our common stock continues, it may be difficult for shareholders to sell their shares. Also, the sale of a large block of our common stock could depress the market price to a greater degree than a company that typically has a higher volume of trading of its securities.

The Limited Public Trading Market May Cause Volatility In Our Stock Price.

The Company's common stock is currently quoted on a limited basis on the OTC Bulletin Board under the symbol "PEFF". The quotation of our common stock on the OTC Bulletin Board does not assure that a meaningful, consistent and liquid trading market exists at all times, and in recent years such market has experienced extreme price and volume fluctuations that have particularly affected the market prices of many smaller companies like us. Our common stock is thus subject to this volatility. Sales of substantial amounts of our common stock, or the perception that such sales might occur, could adversely affect prevailing market prices of our common stock.

An Active And Visible Trading Market For Our Common Stock May Not Develop.

The market for our common stock may become inactive in the future. In the absence of an active trading market:

- Investors may have difficulty buying and selling or obtaining market quotations;
- Market visibility for our common stock may be limited; and
- A lack of visibility for our common stock may have a depressive effect on the market price for our common stock.

The OTC Bulletin Board is an inter-dealer, over-the-counter market that provides significantly less liquidity than NASDAQ, and quotes for stocks included on the OTC Bulletin Board are not listed in the financial sections of newspapers, as are those for the NASDAQ Stock Market. The trading price of the common stock is expected to be subject to significant fluctuations in response to variations in quarterly operating results, changes in analysts' earnings estimates, announcements of innovations by the Company or its competitors, general conditions in the industry in which we operate and other factors. These fluctuations, as well as general economic and market conditions, may have a material or adverse effect on the market price of our common stock.

Penny Stock Regulations May Impose Certain Restrictions On Marketability Of Our Securities.

The SEC has adopted regulations which generally define a "penny stock" to be any equity security that has a market price of less than $5.00 per share or an exercise price of less than $5.00 per share, subject to certain exceptions. As a result, our common stock is subject to rules that impose additional requirements on broker-dealers who sell such securities to persons other than established customers and accredited investors (generally those with net worth in excess of $1,000,000 or annual income exceeding $200,000, or $300,000 together with their spouse). For transactions covered by these rules, the broker-dealer must make a special suitability determination for the purchase of such securities and have received the purchaser's written consent to the transaction prior to the purchase. Additionally, for any transaction involving a penny stock, unless exempt, the rules require the delivery, prior to the transaction, of a risk disclosure document relating to the penny stock market. The broker-dealer must also disclose the commission payable to both the broker-dealer and the registered representative, current quotations for the securities and, if the broker-dealer is the sole market maker, the broker-dealer must disclose this fact and the broker-dealer's presumed control over the market. Finally, monthly statements must be sent disclosing recent price information for the penny stock held in the account and information on the limited market in penny stocks. Consequently, the "penny stock" rules may restrict the ability of broker-dealers to sell the Company's securities and may affect the ability of investors to sell the Company's securities in the secondary market and the price at which such purchasers can sell any such securities.

Stockholders should be aware that, according to the Commission, the market for penny stocks has suffered in recent years from patterns of fraud and abuse. Such patterns include:

- Control of the market for the security by one or a few broker-dealers that are often related to the promoter or issuer;
- Manipulation of prices through prearranged matching of purchases and sales and false and misleading press releases;
- "Boiler room" practices involving high pressure sales tactics and unrealistic price projections by inexperienced sales persons;
- Excessive and undisclosed bid-ask differentials and markups by selling broker-dealers; and

- The wholesale dumping of the same securities by promoters and broker-dealers after prices have been manipulated to a desired level, along with the inevitable collapse of those prices with consequent investor losses.

The Company’s management is aware of the abuses that have occurred historically in the penny stock market.

We May Never Pay Cash Dividends On Our Common Stock.

We have not paid or declared any dividends on our common stock and do not anticipate paying or declaring any cash dividends on our common stock in the foreseeable future.

Sales Of Common Stock Under Rule 144 May Adversely Affect The Market Price Of Our Common Stock.

Possible Resales under Rule 144. Of the 44,825,883 shares of the Company's common stock outstanding on the date of this report, 33,295,056 shares are freely trading in the market place (the "Free Trading Shares"). The Free Trading Shares are comprised mostly of shares (1) originally issued in private offerings of common stock from June through March 2007, that were later registered in the Company's S-1 Registration Statement (the "Registration Statement"), declared effective on October 10, 2008 and (2) shares originally issued in transactions exempt from registration under the Securities Act.

The remaining 11,530,927 shares of our common stock outstanding are restricted securities as defined in Rule 144 and under certain circumstances may be resold without registration pursuant to Rule 144. These shares include the 9,968,910 shares held by Summit and Steven Strasser in the aggregate, and 1,661,917 shares held by directors and insiders.

In addition, the Company had approximately 31,387,469 common stock purchase warrants outstanding and approximately 16,479,896 common stock options outstanding as of the date of this report, including the warrants issued in connection with the private offer and sale of preferred stock units in 2008 and 2009 (See Note 18 to the Financial Statements). The shares issuable on exercise of the options and warrants may, under certain circumstances, be available for public sale in the open market under the Registration Statement or pursuant to Rule 144, subject to certain limitations.

In general, pursuant to Rule 144, after satisfying a six month holding period: (i) affiliated stockholder (or stockholders whose shares are aggregated) may, under certain circumstances, sell within any three month period a number of securities which does not exceed the greater of 1% of the then outstanding shares of common stock or the average weekly trading volume of the class during the four calendar weeks prior to such sale and (ii) non-affiliated stockholders may sell without such limitations, provided we are current in our public reporting obligations. Rule 144 also permits the sale of securities by non-affiliates that have satisfied a one year holding period without any limitation or restriction. Any substantial sale of the common stock pursuant to Rule 144 may have an adverse effect on the market price of the Company's shares.

Exercise Of Outstanding Options And Warrants Will Dilute Ownership Of Outstanding Shares.

As of the date of this report, the Company has reserved 71,429 shares of common stock for issuance upon exercise of stock options or similar awards which may be granted pursuant to the 1994 Plan, of which no options are outstanding. Furthermore, we have reserved 25,000,000 shares of our common stock for issuance upon exercise of stock options or similar awards which may be granted pursuant to the 2000 Plan, of which options to purchase an aggregate of 16,479,896 shares are outstanding. The outstanding options under the 2000 Plan have a weighted average exercise price of $0.34. As of the date of this report, we have issued warrants exercisable for 31,387,469 shares of common stock to financial consultants, investors, former employees and other business partners, having a weighted average exercise price of $0.43 and expiring on various dates from February 2010 to December 2014. Exercise of these options and warrants in the future will reduce the percentage of common stock held by the public stockholders. Furthermore, the terms on which we could obtain additional capital during the life of the options and warrants may be adversely affected, and it should be expected that the holders of the options and warrants would exercise them at a time when we would be able to obtain equity capital on terms more favorable than those provided for by such options and warrants.

Our Issuance Of "Blank Check" Preferred Stock Could Adversely Affect Our Common Stockholders.

The Company's Certificate of Incorporation authorizes the issuance of "blank check" preferred stock with such designations, rights and preferences as may be determined from time to time by the board of directors. Accordingly, our Board of Directors is empowered, without stockholder approval, to issue preferred stock with dividends, liquidation, conversion, voting or other rights that could adversely affect the relative voting power or other rights of the holders of our common stock. In the event of issuance, the preferred stock could be used as a method of discouraging, delaying or preventing a change in control of the Company, which could have the effect of discouraging bids for the Company and thereby prevent stockholders from receiving the maximum value for their shares. From August 12, 2009, through January 20, 2010, the Company sold 23,375 shares if its Series C preferred stock, and 32,750 shares of its Series C-1 preferred stock in private offerings of units (See Note 18 to the Financial Statements).

Item 1B. Unresolved Staff Comments.

None

14

Item 2.Description of Property.

The Company's corporate office space is located at 3960 Howard Hughes Pkwy, Suite 460, Las Vegas, Nevada 89169. The office lease calls for rent of $11,292 per month, plus annual increases equal to 3%, through the end of the lease term in February 2011.

The Company leased research and development space at 6380 South Valley View Blvd, Suite 412, Las Vegas, Nevada 89118. The lease calls for rent of $1,995 plus common area maintenance charges, per month, through the end of the lease term in August 2010.

The Company leased manufacturing and warehouse space at 6380 South Valley View Blvd, Suite 402, Las Vegas, Nevada 89118. The lease calls for rent of $1,605 plus common area maintenance charges, per month, through the end of the lease term in August 2010.

Item 3.Legal Proceedings.

The Company is currently involved in a lawsuit against a former director and the company at which he is currently CEO (collectively, the "Defendants"). The Company filed this action against the Defendants for misappropriation of trade secrets, false advertising, defamation/libel and other claims primarily arising from the Defendants' use of the Company's confidential and proprietary information in the development and marketing of motor control products. The Company seeks a temporary restraining order, preliminary injunction, permanent injunction, damages, exemplary damages, attorneys' fees and costs against the Defendants. The Company's complaint was filed on August 6, 2009 in the U.S. District Court, District of Nevada.

PART II

Item 5.Market for Common Equity and Related Stockholder Matters.

Market for Common Stock

The Company's common stock is thinly traded on the National Association of Securities Dealers' Over the Counter Bulletin Board ("OTCBB") under the symbol "PEFF".

The following table sets forth the high and low bid information for quarterly periods in the two twelve month periods ended December 31, 2009 and December 31, 2008

Twelve months Ended December 31, 2009		High	Low
October 1, 2009 — December 31, 2009	$	0.45	0.20
July 1, 2009 — September 30, 2009		0.25	0.11
April 1, 2009 — June 30, 2009		0.30	0.12
January 1, 2009 — March 31, 2009		0.30	0.08

Twelve months Ended December 31, 2008		High	Low
October 1, 2008 — December 31, 2008	$	0.25	0.08
July 1, 2008 — September 30, 2008		0.32	0.19
April 1, 2008 — June 30, 2008		0.39	0.26
January 1, 2008 — March 31, 2008		0.55	0.26

As of March 31, 2010, there were 168 shareholders of record of the Company's common stock. Because many of our shares are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by record holders.

The Company has not paid dividends on its common stock since its incorporation. The Company does not expect to pay cash dividends on its common stock in the foreseeable future. The Company intends to invest funds otherwise available for dividends, if any, on improving the Company's capital assets.

EQUITY COMPENSATION PLAN INFORMATION AS OF MARCH 31, 2010

	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under 2000 Stock Option and Restricted Stock Plan (excluding securities reflected in column (a))(c)
2000 Stock Option and Restricted Stock Plan approved by security holders	16,479,896	$ 0.34	8,520,104
Equity compensation plans not approved by security holders	0	0.00	0
Total	16,479,896	$ 0.34	8,520,104

The Company maintains a Stock Option Equity Compensation Plan. (See Note 12 to the Financial Statements)

Recent Sales of Unregistered Securities

During the period covered by this report we did not issue any securities that were not registered under the Securities Act of 1933, as amended, except previously disclosed in a quarterly report on Form 10-Q or a current report on Form 8-K.

Item 6.Selected Financial Data

We are a "smaller reporting company" as defined by Regulation S-K and as such, are not providing the information contained in this item pursuant to Regulation S-K.

Item 7.Management's Discussion and Analysis of Financial Condition and Results of Operations.

OVERVIEW

The Company generates revenues from a single business segment: the design, development, marketing and sale of proprietary energy efficiency technologies and products for electric motors. The Company's products, called Motor Efficiency Controllers ("MEC"), save up to 35 percent of the electricity used by a motor in appropriate applications. The Company's patented technology platform, called E-Save Technology®, saves energy when a constant speed alternating current induction motor is operating in a lightly loaded condition. Target applications for the Company's three-phase MECs include escalators, MG set elevators, grinders, crushers, saws, stamping presses, and many other types of industrial equipment. The Company has also developed a single-phase MEC targeted at smaller motors, such as those found in clothes washers, dryers, and other appliances and light commercial equipment. The Company has one existing patent and three patents pending on E-Save Technology®.

Analog Three-phase MEC

The Company began generating revenues from sales of its patented analog three-phase MEC line of motor controllers in the late 1990's. The Company sold this product through the second quarter of 2009.

Digital Three-phase MEC

In 2005, the Company began development of a digital version of its three-phase MEC so that the product would be capable of high volume sales through existing distribution channels for motor controls. The digital version is much smaller in size and easier to install than the analog product, is driven by a powerful microprocessor and digital signal processor. The digital MEC is a complete motor control device, meaning is can start, stop, soft start and protect a motor, and is therefore capable of replacing standard motor starters and soft starts that do not save energy. The product can be installed by OEMs at their factories or it can be retrofitted on to existing equipment.

In 2008, the Company launched limited sales of the digital three-phase MEC and initiated testing if the digital product by several OEMs, primarily in the elevator/escalator industry. In the summer of 2009, the Company announced its first OEM agreements and that it had received Underwriters' Laboratories ("UL") certification on a full line of the Company's digital three-phase products. UL certification enables the Company to sell its digital three-phase products to industrial markets. The Company is developing a network of independent sales representatives to penetrate the industrial markets.

Digital Single-phase MEC

In 2006, the Company began development on its digital single-phase product. The digital single phase MEC is targeted at appliances, such as clothes washers and dryers. The Company has one patent pending on its digital single-phase MEC.

Capitalization

As of December 31, 2009, the Company had total stockholders' equity of $801,642 primarily due to (i) the Company's sale of 30,250 shares of Series C and Series C-1 Convertible Preferred Stock in a private offering in December of 2009, (ii) the Company's sale of 140,000 shares of Series B Convertible Preferred Stock in a private offering from October of 2007 through January of 2008, (iii) the Company's sale of 12,950,016 shares of common stock in a private stock offering from November of 2006 through March of 2007, (iv) the Company's sale of 14,500,000 shares of common stock in a private stock offering in July and August of 2005, (v) the Company's sale of 2,346,233 shares of Series A-1 Convertible Preferred stock to Summit Energy Ventures, LLC in June of 2002 and (vi) the conversion of notes payable of approximately $1,047,000 into 982,504 shares of Series A-1 Convertible Preferred Stock in October of 2003. All of the Company's Series A-1 Convertible Preferred Stock was converted into the Company's common stock in 2005.

Because of the nature of our business, the Company makes significant investments in research and development for new products and enhancements to existing products. Historically, the Company has funded its research and development efforts through cash flow primarily generated from debt and equity financings. Management anticipates that future expenditures in research and development will continue at current levels.

The Company's results of operations for the year ended December 31, 2009 were marked by a significant decrease in revenues and an increase in losses from operations that are more fully discussed in the following section "Results of Operations for the Years Ended December 31, 2009 and 2008". Sales cycles for our products are generally lengthy and can range from less than a month to well over one year, depending on customer profile. Larger OEM deals and sales to larger end users generally take a longer period of time, whereas sales through channel partners may be closed within a few weeks. Because of the complexity of this sales process, a number of factors that are beyond the control of the Company can delay the closing of transactions.

RESULTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008

The following table sets forth certain line items in our condensed statement of operations as a percentage of total revenues for the periods indicated:

	Year Ended December 31, 2009	Year Ended December 31, 2008
Revenues	100.0%	100.0%
Cost of revenues	78.8	82.8
Gross profit	21.2	17.2
Costs and expenses:		

Selling, general and administrative	933.0	631.1
Research and development	335.6	211.5
Depreciation and amortization	23.4	15.5
Total expenses	1,292.1	858.1
Loss from operations	(1,270.9)	(840.9)
Other income	(175.6)	21.8
Provision for taxes	(21.4)	(2.6)
Net loss	(1,467.9)	(821.7)
Dividends paid or payable on Series B, Series C and Series C-1 Preferred Stock	447.5	113.6
Net loss attributable to common shareholders	(1,915.5)	(935.3)

REVENUES

Revenues for the year ended December 31, 2009, were approximately $284,000 compared to approximately $481,000 for the year ended December 31, 2008, a decrease of $197,000 or 41%. This decrease is mainly attributable to a decrease in sales in the elevator and escalator market during the year ended December 31, 2009. Specifically, escalator manufacturer and service provider sales fell to approximately $183,000 for the year ended December 31, 2009, from $363,000 for the year ended December 31, 2008. Sales of the analog product to one escalator manufacturer and service provider, which is one of the Company's largest customers, slowed very significantly during this period in anticipation of release of their private label version of our digital product. The digital product has been tested and approved for use on a retrofit and OEM basis by this customer, and a supply agreement was signed during the second quarter of 2009, and the customer's private label version of our digital product was launched at the end of the second quarter of 2009. The digital product offers greater features and functionality compared to the analog product, making it more attractive as an OEM product. Furthermore, industrial sales fell to approximately $78,000 for the year ended December 31, 2009, from approximately $118,000 for the year ended December 31, 2008. Sales of the Company's single-phase product, which is for use on small appliances, totaled approximately $23,000 for the year ended December 31, 2009. There were no comparable sales of the single-phase product in 2008. For the year ended December 31, 2009, industrial and other sales, of which all but one sale consisted of digital units, were approximately 27% of total revenues, escalator and elevator sales, which consisted of a mix of digital units and analog units, were approximately 65% of total revenues, and sales of our single-phase product were approximately 8% of total revenues. For the year ended December 31, 2008, industrial and other sales, which consisted of a mix of digital units and analog units, were approximately 21% of total revenues, and escalator and elevator sales, which consisted mostly of analog units, were approximately 79% of total revenues.

COST OF REVENUES

Cost of revenues for the year ended December 31, 2009 were approximately $224,000 compared to approximately $398,000 for the year ended December 31, 2008, a decrease of $174,000, or 44%. This decrease is mainly attributable to a decrease in sales in both the elevator and escalator and the industrial markets during the year ended December 31, 2009. Also, the Company recorded an inventory obsolescence charge of approximately $41,000 during the year ended December 31, 2008 and no comparable charge was recorded during the year ended December 31, 2009. As a percentage of sales, total cost of revenues decreased to approximately 79% for the year ended December 31, 2009, compared to approximately 82% for the year ended December 31, 2008. The decrease in the costs as a percentage of sales was primarily due to the Company increasing its prices on certain units, which resulted in higher margins during the year ended December 31, 2009, and an increase in the sale of digital units, which have higher average margins than analog units, as well as no inventory obsolescence charges during 2009.

GROSS PROFIT

Gross profit for the year ended December 31, 2009 was approximately $60,000 compared to approximately $83,000 for the year ended December 31, 2008, resulting in a decrease of $23,000 or 28%. This decrease is mainly attributable to a decrease in sales in both the elevator and escalator and the industrial markets during the year ended December 31, 2009, partially offset by the inventory obsolescence charge recorded by the Company during the year ended December 31, 2008, as described above. As a percentage of revenue, gross profit increased to approximately 21% for the year ended December 31, 2009, compared to approximately 17% for the year ended December 31, 2008.

OPERATING EXPENSES

Selling, General and Administrative Expenses

Selling, general and administrative expenses were approximately $2,650,000 for the year ended December 31, 2009, compared to approximately $3,033,000 for the year ended December 31, 2008, a decrease of $383,000 or 13%. The decrease in selling, general and administrative expenses compared to the prior year was primarily due to a decrease in travel expenses, consulting fees, and a decrease in stock based compensation costs related to FASB ASC 718 (SFAS 123(R)). These decreases were partially offset by increases in legal and professional fees, related to the Company's patent attorneys and litigation (see Item 3 – Legal Proceedings), and a change in the Company's independent registered accounting firm.

Research and Development Expenses

Research and development expenses were $953,000 for the year ended December 31, 2009 compared to approximately $1,016,000 for the year ended December 31, 2008, a decrease of $63,000 or 6%. This decrease is mainly attributable to a decrease in the Company's product development and certification costs related to the Company's digital controller for both its single-phase and three-phase products during the year ended December 31, 2009.

Change in Fair Value of Warrant Liability

Warrants issued in connection with a private offering of the Company's common stock completed on July 8, 2005 and August 31, 2005 are being accounted for as liabilities in accordance with FASB ASC 820-10, Fair Value Measurements and Disclosures (Prior authoritative literature: FASB EITF 07-5, Determining Whether an Instrument (or Embedded Feature) Is Indexed to an Entity's Own Stock ("EITF 07-5"), issued January 2009), based on an analysis of the terms and conditions of the warrant agreements.

As a result, the fair value of these warrants (five year warrants to purchase up to 5,696,591 shares of the Company's common stock at an exercise price of $0.44 per share), amounting to $381,856 as of January 1, 2009, was reclassified from equity and reflected as a liability. The fair value of these warrants amounted to $828,827 as of December 31, 2009. The $514,089 increase in the fair value of these warrants during 2009 has been reflected as a non-operating loss in the Statement of Operations for 2009. The warrants are being valued at each reporting period using the Black-Scholes pricing model to determine the fair market value per share. We will continue to mark the warrants to market value each quarter-end until they expire.

Financial Condition, Liquidity, and Capital Resources: For the Year Ended December 31, 2009

The Company has suffered recurring losses from operations, and experienced a deficiency of cash of approximately $3,000,000 and $3,100,000 from operations for the years ended December 31, 2009 and 2008, respectively. For the years ended December 31, 2009 and December 31, 2008, we had net losses of $4,168,708 and $3,948,204, respectively. In our Auditors' Report dated March 31, 2010 on our December 31, 2009 financial statements included in this report, our auditors have stated that these factors raise substantial doubt about our ability to continue as a "going concern". Our financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amount of liabilities that might be necessary should we be unable to continue in existence.

The Company's continuation as a "going concern" is dependent upon achieving profitable operations and related positive cash flow and satisfying our immediate cash needs by external financing until we are profitable. Our plans to achieve profitability include developing new products, obtaining new customers and increasing sales to existing customers. We are seeking to raise additional capital through equity issuance, debt financing and other types of financing, but we cannot guarantee that sufficient capital will be raised.

On March 30, 2010, the Company issued unsecured notes payable to Steven Strasser, the Company's CEO, totaling $125,000. The notes bear interest at 5%, payable upon maturity. The notes mature two months after issuance.

Since inception, the Company has financed its operations primarily through the sale of its securities. In 2009, the Company received a total of approximately $1,210,000 in gross proceeds from a private placement of its Series C and Series C-1 preferred stock and warrants to purchase common stock. In 2008 and 2007, the Company received a total of approximately $8,025,000 in gross proceeds from a private placement of its Series B preferred stock, common stock and warrants to purchase common stock, as to which the Company was required to file a registration statement on Form SB-2 or other relevant registration statement. Of this amount, $1,850,000 was converted from existing debt securities. Also in 2007, the Company grossed approximately $680,000 in cash from the exercise of warrants. As of December 31, 2009 the Company has received a total of approximately $21,515,000 from public and private offerings of its equity securities, received $300,000 from a bridge note with a shareholder (which was converted into 3,000,000 shares of common stock and 1,500,000 warrants with an additional investment of $300,000 on July 8, 2005), received approximately $445,386 under a bank line of credit (which was repaid during 2002), and received $1,000,000 under a line of credit with a shareholder (which was converted to Series A-1 Preferred Convertible shares during 2003). In October 2004 and February 2005, the Company received $1,589,806 in debt financing through a debt offering arranged by a placement agent, Pali Capital. Of this total, $300,000 plus accrued interest was converted from borrowings with the same shareholder as referenced above. In April 2006, the Company received $1,000,000 in debt financing from EMTUCK , LLC, in which the managing member is a management company wholly owned and controlled by Steven Strasser, the Company's CEO. In May 2006, the Company received an additional $500,000 in debt financing from EMTUCK. In November 2006, the Company received $2,000,000 in debt financing. Of this amount, $1,450,000 was converted from borrowings from prior investors. This $2,000,000 note was paid off in full in October of 2007. As of December 31, 2009 the Company had cash of $247,564 and has no outstanding debt securities.

Net cash used for operating activities for the year ended December 31, 2009 was $3,002,386 which primarily consisted of: a net loss of $4,168,708; less bad debt expense of $8,149, depreciation and amortization of $66,589, loss on the disposal of fixed assets of $3,097, warrants and options issued in connection services from vendors, and to employees and consultants of $405,143, change in fair value of warrant liability of $514,089, deferred tax provision of $49,946, decreases in prepaid expenses and other current assets of $10,728, and deposits of $11,292, increases in accounts receivable of $30,133 and inventory of $35,233. In addition, these amounts were partially offset by decreases in deferred rent of $3,750, and increases in accounts payable and accrued expenses of $166,405.

Net cash used for operating activities for the year ended December 31, 2008 was $3,102,847 which primarily consisted of: a net loss of $3,948,204; less bad debt expense of $7,770, inventory obsolescence expense of $40,758, depreciation and amortization of $74,539, warrants and options issued in connection with services from vendors, and to employees and consultants of $765,504, common stock issued for consulting services of $7,960, decreases in accounts receivable of $57,323 and deposits of $84,057, increases in inventory of $155,016 and prepaid expenses of $5,869. In addition, these amounts were partially offset by decreases in accounts payable and accrued expenses of $30,669 and customer deposits of $1,605, and increases in deferred rent of $605.

Net cash used in investing activities for fiscal year 2009 was $32,882, compared to $132,364 in fiscal year 2008. The amount for 2009 consisted of the purchase of fixed assets of $9,601, costs related to patent applications of $24,174, and proceeds from the sale of fixed assets of $893. The amount for 2008 consisted of the purchase of fixed assets of $104,857, and costs related to patent applications of $27,507.

Net cash provided by financing activities for fiscal year 2009 was $1,182,819. The entire amount consisted of the net proceeds from the issuance of equity securities.

Net cash provided by financing activities for fiscal year 2008 was $248,846. The entire amount consisted of the net proceeds from the issuance of equity securities.

The Company expects to increase its operating expenses, particularly in research and development and selling, general and administrative expenses, for the foreseeable future in order to execute its business strategy. As a result, the Company anticipates that operating expenses will constitute a material use of any cash resources.

Cash Requirements and Need for Additional Funds

The Company anticipates a substantial need for cash to fund its working capital requirements. It is the opinion of management that approximately $2.5 - 3 million will be required to cover operating expenses, including, but not limited to, marketing, sales, research and operations during the next twelve months. If the Company is unable to obtain funding on reasonable terms or finance its needs through current operations, the Company will be forced to restructure, file for bankruptcy or cease operations.

Notable changes to expenses are expected to include an increase in the Company’s sales personnel and efforts, and developing more advanced versions of the Company’s technology and products.

Critical Accounting Policies and Estimates

Management’s discussion and analysis of Power Efficiency Corporation’s financial condition and results of operations are based upon the condensed financial statements contained in this Annual Report on Form 10-K, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosure of contingent assets and liabilities. On an on-going basis, management evaluates estimates, including those related to the valuation of inventory and the allowance for uncollectible accounts receivable. We base our estimates on historical experience and on various other assumptions that management believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ materially from these estimates under different assumptions or conditions. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our condensed financial statements.

Inventories

Inventories are valued at the lower of cost (first-in, first-out) or market. The Company reviews inventory for impairments to net realizable value whenever circumstances arise. Such circumstances may include, but are not limited to, the discontinuation of a product line or re-engineering certain components making certain parts obsolete. Management has determined a reserve for inventory obsolescence is not necessary at December 31, 2009 or 2008.

Accounts Receivable

The Company carries its accounts receivable at cost less an allowance for doubtful accounts and returns. On a periodic basis, the Company evaluates its accounts receivable and establishes an allowance for doubtful accounts, based on a history of past write-offs and collections and current credit conditions. Change in customer liquidity or financial condition could affect the collectability of that account, resulting in the adjustment upward or downward in the provision for bad debts, with a corresponding impact to our results of operations.

Fair Value Measurements:

FASB ASC 820-10 (SFAS No. 157) emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, FASB ASC 820-10 (SFAS No. 157) establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy). The Company has applied FASB ASC 820-10 (SFAS 157) to measure the amount of the liability related to its derivative instruments at fair value and to determine fair value for purposes of testing goodwill for impairment.

Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access. Level 2 inputs are inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the asset or liability (other than quoted prices), such as interest rates and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, which is typically based on an entity's own assumptions, as there is little, if any, related market activity. In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

Revenue Recognition

Revenue from product sales is recognized at the time of shipment, when all services are complete. Returns and other sales adjustments (warranty accruals, discounts and shipping credits) are provided for in the same period the related sales are recorded.

Accounting for Stock Based Compensation

The Company accounts for employee stock options as compensation expense, in accordance with FASB ASC 718 (SFAS 123(R)). FASB ASC 718 (SFAS 123(R)) requires companies to expense the value of employee stock options and similar awards, and applies to all outstanding and vested stock-based awards.

In computing the impact, the fair value of each option is estimated on the date of grant based on the Black-Scholes options-pricing model utilizing certain assumptions for a risk free interest rate; volatility; and expected remaining lives of the awards. The assumptions used in calculating the fair value of share-based payment awards represent management's best estimates, but these estimates involve inherent uncertainties and the application of management's judgment. As a result, if factors change and the Company uses different assumptions, the Company's stock-based compensation expense could be materially different in the future. In addition, the Company is required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. In estimating the Company's forfeiture rate, the Company analyzed its historical forfeiture rate, the remaining lives of unvested options, and the amount of vested options as a percentage of total options outstanding. If the Company's actual forfeiture rate is materially different from its estimate, or if the Company reevaluates the forfeiture rate in the future, the stock-based compensation expense could be significantly different from what we have recorded in the current period. The impact of applying FASB ASC 718 (SFAS 123(R)) approximated $405,000 and $766,000 in additional compensation expense during the periods ended December 31, 2009 and 2008, respectively. Such amounts are included in research and development expenses and selling, general and administrative expense on the statement of operations.

Product Warranties

The Company typically warrants its products for two years. Estimated product warranty expenses are accrued in cost of sales at the time the related sale is recognized. Estimates of warranty expenses are based primarily on historical warranty claim experience. Warranty expenses include accruals for basic warranties for products sold. While management believes our estimates are reasonable, an increase or decrease in submitted warranty claims could affect warranty expense and the related current and future liability.

Provision for Income Taxes

The Company utilizes the asset and liability method of accounting for income taxes pursuant to FASB ASC 740 Accounting for Income Taxes (Prior authoritative literature FASB SFAS No. 109, Accounting for Income Taxes (“SFAS 109”)), which requires the recognition of deferred tax assets and liabilities for both the expected future tax impact of differences between the financial statement and tax basis of assets and liabilities, and for the expected future tax benefit to be derived from tax loss and tax credit carryforwards. FASB ASC 740 (SFAS 109) additionally requires the establishment of a valuation allowance to reflect the likelihood of realization of deferred tax assets. We have reported net operating losses for consecutive years, and do not have projected taxable income in the near future. This significant evidence causes our management to believe a full valuation allowance should be recorded against the deferred tax assets.

FASB ASC 740-10-25-10 Definition of Settlement in FASB Interpretation No. 48 (Prior authoritative literature FIN 48-1 Definition of Settlement in FASB Interpretation No. 48 (“FIN 48-1”) issued May 2007) provides guidance on how to determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. FASB ASC 740-10-25-10 (FIN 48-1) is effective retroactively to January 1, 2007. Under FASB ASC 740 (FIN 48), the impact of an uncertain tax position taken or expected to be taken on an income tax return must be recognized in the financial statements at the amount that is more likely than not to be sustained upon audit by the relevant taxing authority. An uncertain income tax position will not be recognized in the financial statements unless it is more likely than not of being sustained. The implementation of FASB ASC 740 (FIN 48) and FASB ASC 740-10-25-10 (FIN 48-1) did not have a material impact on the Company’s financial position, results of operations or cash flows.

Goodwill

FASB ASC 350, Goodwill and Other Intangible Assets (Prior authoritative literature: FASB SFAS No. 142, Goodwill and Other Intangible Assets (“SFAS 142”)) requires that goodwill shall not be amortized. At a minimum, goodwill is tested for impairment, on an annual basis by the Company, or when certain events indicate a possible impairment, utilizing a two-step test, as described in FASB ASC 350 (SFAS 142).

The Company’s most recent impairment analysis was performed on December 31, 2009, on the Company’s single reporting unit. Using the Company’s market capitalization (based on Level 1 inputs), management determined that the estimated fair market value substantially exceeded the company’s book value. As of December 31, 2009, the Company’s market capitalization was $13,896,024, and the Company’s book value was $801,642. As of December 31, 2008, the Company’s market capitalization was $8,651,088, and the Company’s book value was $4,046,747. Based on this, no impairment exists as of December 31, 2009 and 2008. Circumstances may arise in which the Company will perform an impairment test in addition to its annual tests. A significant impairment could have a material adverse affect on our financial condition and results of operations.

New Accounting Pronouncements:

In October 2009, the Financial Accounting Standards Board issued Accounting Standards Update 2009-13, "Revenue Recognition (Topic 605) Multiple-Deliverable Revenue Arrangements, a consensus of the FASB Emerging Issues Task Force ("ASU 2009-13"). ASU 2009-13 amends existing accounting guidance for separating consideration in multiple-deliverable arrangements. ASU 2009-13 establishes a selling price hierarchy for determining the selling price of a deliverable. The selling price used for each deliverable will be based on vendor-specific objective evidence if available, third-party evidence if vendor-specific evidence is not available, or estimated selling price if neither vendor-specific evidence nor third-party evidence is available. ASU 2009-13 eliminates residual method of allocation and requires that arrangement consideration be allocated at the inception of the arrangement to all deliverables using the "relative selling price method." The relative selling price method allocates any discount in the arrangement proportionately to each deliverable on the basis of each deliverable's selling price. ASU 2009-13 requires that a vendor determine its best estimate of selling price in a manner that is consistent with that used to determine the price to sell the deliverable on a stand-alone basis. ASU 2009-13 is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, with earlier adoption permitted. We do not believe the adoption of ASU 2009-13 will have any material impact on our financial statements.

In January 2010, the FASB issued accounting standards update (ASU) No. 2010-06, Fair Value Measurements and Disclosures (Topic 820)—Improving Disclosures about Fair Value Measurements (ASU No. 2010-06). ASU No. 2010-06 requires: (1) fair value disclosures of assets and liabilities by class; (2) disclosures about significant transfers in and out of Levels 1 and 2 on the fair value hierarchy, in addition to Level 3; (3) purchases, sales, issuances and settlements be disclosed on gross basis on the reconciliation of beginning and ending balances of Level 3 assets and liabilities; and (4) disclosures about valuation methods and inputs used to measure the fair value of Level 2 assets and liabilities. ASU No. 2010-06 becomes effective for the first financial reporting period beginning after December 15, 2009, except for disclosures about purchases, sales, issuances and settlements of Level 3 assets and liabilities which will be effective for fiscal years beginning after December 15, 2010. We are currently assessing what impact, if any, ASU No. 2010-06 will have on our fair value disclosures; however, we do not believe the adoption of the guidance provided in this codification update to have a material impact on our financial statements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are a "smaller reporting company" as defined by Regulation S-K and as such, are not providing the information contained in this item pursuant to Regulation S-K.

Item 8. Financial Statements and Supplementary Data.

The financial statements of the Company and the notes related to the financial statements, together with the independent registered public accounting firms' reports thereon, are set forth beginning on pages F-1 of this report.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None

Item 9A. Controls and Procedures.

(a) Evaluation of Disclosure Controls and Procedures.

Under the supervision and with the participation of its Chief Executive Officer and Chief Financial Officer, management has evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this report pursuant to Rule 13a-15(b) under the Securities Exchange Act of 1934 (the Exchange Act). Based on that evaluation, the Chief Executive Officer, and Chief Financial Officer have concluded that, as of the end of the period covered by this report, due to the material weakness in financial reporting, the Company's disclosure controls and procedures are not effective in ensuring that information required to be disclosed in the Company's Exchange Act reports is (1) recorded, processed, summarized and reported in a timely manner, and (2) accumulated and communicated to the Company's management, including its Chief Executive Officer, and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

(b) Changes in Internal Control Over Financial Reporting.

During the quarter ended December 31, 2009, there were no significant changes in the Company's internal controls or in other factors that could materially affect these controls subsequent to the date of their evaluation; however management determined that there were material weaknesses in the Company's internal controls as of December 31, 2009. Accordingly, corrective actions were required.

(c) Management's Report on Internal Control Over Financial Reporting

Our Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), are responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”).

Internal control over financial reporting is promulgated under the Exchange Act as a process designed by, or under the supervision of, our CEO and CFO 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 dispositions 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 or disposition of our assets that could have a material effect on the financial statements.

Readers are cautioned that internal control over financial reporting, no matter how well designed, has inherent limitations and may not prevent or detect misstatements. Therefore, even effective internal control over financial reporting can only provide reasonable assurance with respect to the financial statement preparation and presentation.

Our management, under the supervision and with the participation of our CEO and CFO, has evaluated the effectiveness of our internal controls over financial reporting as defined in Exchange Act Rules 13a-15(f) and15d-15(f) as of the end of the period covered by this Report based upon the framework in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on such evaluation, our management concluded that there were material weaknesses in internal controls over financial reporting and has made an assessment that our internal control over financial reporting is not effective as of December 31, 2009.

A “material weakness” is defined as a significant deficiency or combination of significant deficiencies that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. A “significant deficiency” is defined as a control deficiency, or combination of control deficiencies, that adversely affects the Company’s ability to initiate, authorize, record, process, or report external financial information reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Company’s annual or interim financial statements that is more than inconsequential will not be prevented or detected.

Management identified the following material weaknesses in the Company’s internal control over financial reporting as of December 31, 2009:

- As of December 31, 2009, there was a material internal control weakness in the Company’s determination of the fair values of its warrant liability. This was identified as a result of errors identified in the Company’s warrant valuation model. The Company calculated its warrant values utilizing an estimated volatility rate. During the audit for the year ended December 31, 2009, the Company’s independent registered accounting firm determined that the estimated volatility rate the Company used was incorrect. The Company reviewed and revised its estimated volatility rate and warrant valuation model, which resulted in material differences in the Company’s warrant liability and related fair market value adjustments on warrant liability for the year ended December 31, 2009. The Company determined that the error was not material to prior quarters. The Company has elected to provide corrected unaudited quarterly financial data presented in Note 18 to the Financial Statements, beginning on page F-31 of this report.

- As of December 31, 2009, there was a material internal control weakness in the Company’s accounting for deferred income taxes. This was identified as a result of errors identified during the audit in the Company’s tax provision. Previously, the Company did not recognize a deferred tax liability related to its amortization of goodwill for tax purposes. The Company reviewed and revised its tax provision to include this deferred tax liability as of January 1, 2009 and for the year ended December 31, 2009. The Company determined that the error was not material to prior years. The corrected unaudited quarterly financial data presented in Note 18 to the Financial Statements, beginning on page F-31 of this report has also been corrected for this matter.

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

Item 9B. Other Information.

None.

PART III

Item 10. Directors, Executive Officers, and Corporate Governance.

INFORMATION ABOUT THE COMPANY'S EXECUTIVE OFFICERS AND DIRECTORS

The following table lists the current executive officers and directors and, in the case of directors, their length of service on the board. Each director is elected to hold office for a term expiring at the first annual meeting of stockholders held following such director's election and until his successor has been elected and qualified, or until his prior resignation or removal. All of the Company's current directors were either appointed by the plurality of votes cast by the holders of our common stock present, or represented, at the 2009 Annual Meeting of the Stockholders in July 2009, or elected by the board. On March 29, 2010, Gregory Curhan resigned from the Board of Directors. Mr. Curhan’s resignation is not as a result of any disagreement with the Company on any matter relating to the Company’s operations, policies or practices.

Name	Age	Director Since	Position
Steven Z. Strasser	61	2002	Chairman, Chief Executive Officer
John (BJ) Lackland	39	2002	Director, Chief Financial Officer, and Secretary
George Boyadjieff	71	2006	Director, Senior Technical Advisor
Douglas M. Dunn	67	2006	Director
Richard Morgan	64	2007	Director
Gary Rado	70	2005	Director
Kenneth Dickey	68	2009	Director, Consultant

Director Independence

Pursuant to SEC rules, a majority of our Board of Directors is comprised of independent directors, as defined under Section 121(A) of the New York Stock Exchange Constitution and Rules. Messrs. Boyadjieff, Dickey, Dunn, Morgan and Rado are independent directors. Our audit committee is comprised of Messrs. Dunn, Morgan and Rado; and our compensation committee is comprised of Messrs. Boyadjieff, Dickey and Rado, all of whom are independent directors.

Steven Strasser – Chairman and Chief Executive Officer. Prior to becoming the Company’s CEO in October 2004, Mr. Strasser was the Managing Director, founder and majority owner of Summit Energy Ventures LLC, currently the largest stockholder in Power Efficiency Corporation. Summit is a private equity firm focused on investments in companies with energy efficiency technologies. At Summit, Mr. Strasser spent four years, from 2001 through 2005, evaluating and investing in energy technology companies and serving on the boards of portfolio companies. Mr. Strasser has been a director since August 2002.

From 1984 through 2000, Mr. Strasser was the founder and CEO of Northwest Power Enterprises. Over its seventeen-year history, Northwest Power Enterprises and its predecessor companies were involved in multiple aspects of the energy development business. Mr. Strasser received law degrees from McGill University, Montreal, Canada and the University of Washington, Seattle, Washington.

John (BJ) Lackland – Director, Chief Financial Officer, and Secretary. Mr. Lackland became the Company’s CFO in October 2004. Mr. Lackland has been the Vice President and Director Summit Energy Ventures since 2001, a private equity firm that is the largest stockholder in Power Efficiency Corporation. Summit focuses on investments in companies with energy efficiency technologies. At Summit, Mr. Lackland evaluated and invested in energy technology companies and served on the boards of portfolio companies. Prior to joining Summit, Mr. Lackland was the Director of Strategic Relations at Encompass Globalization, where he was in charge of strategic alliances and mergers and acquisitions. Prior to Encompass, he was the Director of Strategic Planning and Corporate Development at an Internet business development consulting company, where he was in charge of strategic planning and investor relations. Mr. Lackland has been an independent consultant to Fortune 1,000 companies and startups. Mr. Lackland also worked at The National Bureau of Asian Research, an internationally acclaimed research company focusing on U.S. policy toward Asia, where he led economic and political research projects for Microsoft, Dell, Compaq and U.S. government agencies. Mr. Lackland has been a director since August 2002.

Mr. Lackland earned an M.B.A. from the University of Washington Business School, an M.A. in International Studies (Asian Studies) from the University of Washington's Jackson School of International Studies, and a B.A. in Politics, Philosophy and Economics from Claremont McKenna College.

George Boyadjieff — Director and Senior Technical Advisor. Mr. Boyadjieff has been a director of the Company since May 2006, and Senior Technical Advisor of the Company since April 2005. Mr. Boyadjieff is the retired CEO of the former Varco International, a New York Stock Exchange traded oil service company with over $1.3 billion in annual revenues at the time of Mr. Boyadjieff's retirement. Varco has recently merged with National Oil Well to become National Oil Well Varco (NOV). Mr. Boyadjieff joined Varco in 1969 as Chief Engineer and was appointed CEO in 1991. Currently Mr. Boyadjieff is a director of Southwall Technologies, a Silicon Valley hi-tech firm. Mr. Boyadjieff joined Southwall in December 2004.

Mr. Boyadjieff holds over 50 US patents related to oil and gas well drilling equipment. Mr. Boyadjieff holds BS and MS degrees in Mechanical Engineering from the University of California at Berkeley and is a graduate of the University of California at Irvine executive program.

Dr. Douglas Dunn — Dr. Dunn has had an extensive career in research, business and academic leadership. Dr. Dunn served as dean of Carnegie Mellon University's Graduate School of Industrial Administration (now the Tepper School of Business) from July 1996 through June 2002, after which he retired. He began his career at AT&T Bell Laboratories, and his corporate experienced culminated in senior positions as a corporate officer leading Federal Regulatory Matters, Regional Government Affairs, and Visual Communications and Multimedia Strategy for AT&T. Dr. Dunn is a board member of Universal Stainless & Alloy Products, Inc. (NasdaqNM: USAP). He holds a Ph.D. in business from the University of Michigan, an MS in industrial management and a BS in physics from the Georgia Institute of Technology.

Richard Morgan – Mr. Morgan is currently Of Counsel to the law firm of Lionel, Sawyer & Collins, and is the Dean Emeritus and a former Professor of Law at the William S. Boyd School of Law at the University of Nevada, Las Vegas, a position he held from September 1, 1997 through June 30, 2007. Mr. Morgan is an experienced legal educator, having served as dean at both the Arizona State University College of Law and the University of Wyoming College of Law. Mr. Morgan earned his B.A. in Political Science at the University of California, Berkeley in 1967. In 1971 he received his J.D. from UCLA, where he was an editor of the UCLA Law Review. He practiced with the Los Angeles law firm of Nossaman, Krueger & Marsh in the corporate/securities areas from 1971 to 1980. He was a professor at the Arizona State University College of Law from 1980 to 1987 and served as associate dean from 1983 to 1987. He was dean at the University of Wyoming College of Law from 1987 to 1990 and returned to the Arizona State University College of Law in 1990, where he served as dean and professor of law until 1997.

Gary Rado – Mr. Rado retired in 2002 after being the President of Casio Inc. USA for 3 years. He joined Casio in 1996 as an EVP to spearhead the move into the digital camera business. Before joining Casio, Mr. Rado was with Texas Instruments Inc. for 21 years. He was the Division Manager of the Consumer Products Division Worldwide and ran the division for 7 years, including two years while based in Europe. This division was responsible for home computer, calculator, and educational products. Mr. Rado earned a Bachelors of Science in Business Administration from Concord College in 1963.

Kenneth Dickey– Mr. Dickey is the co-founder of The Institute of Strategic Mapping, and has spent his extensive career learning how superior results can be achieved from very average businesses and how to translate this winning process into an understandable, reusable format. Mr. Dickey has been retired since February 2002. From October 1999 to February 2002, Mr. Dickey was Vice President Sales-Marketing for Safetronics, where he developed sales and marketing strategies, completed Safetronic's acquisition of Fincor Electric, a manufacturer of variable frequency drives, and ran that business unit. Prior to this, Mr. Dickey was the President/CEO of Cleveland Motion Control, Dynact Inc., and Motion Science, Inc., from February 1997 to October 1999. Prior to this, Mr. Dickey served as

Senior Vice-President Sales for Reliance Electric/Rockwell Automation from 1994 thru 1996. His responsibilities included Sales/Marketing with 76 sales offices (located in the Americas), which generated more than $900 million in revenue. He also spent 9 years as the Operating General Manager of the Industrial Motor Division at Reliance Electric from 1986 to 1994. Mr. Dickey earned his Bachelor of Science degree in Finance from the University of Akron and an Executive MBA from Case-Western Reserve University.

On March 29, 2010, Gregory Curhan resigned from the Board of Directors. Mr. Curhan's resignation is not as a result of any disagreement with the Company on any matter relating to the Company's operations, policies or practices.

Board of Directors and Committees of the Board

Our business affairs are conducted under the direction of our board of directors. The role of our board of directors is to effectively govern our affairs for the benefit of our stockholders and, to the extent appropriate under governing law, of other constituencies, which include our employees, customers, suppliers and creditors. Our board strives to ensure the success and continuity of our business through the selection of a qualified management team. It is also responsible for ensuring that our activities are conducted in a responsible ethical manner. Our board of directors has two standing committees – an audit committee and a compensation committee.

Our board of directors met eight times in 2009.

We do not have a policy that requires directors to attend our annual meetings of stockholders. All but one of the directors attended the 2009 Meeting of Stockholders on July 16, 2009.

Audit Committee

Douglas Dunn, Richard Morgan and Gary Rado currently serve on our audit committee. Messrs. Dunn, Morgan and Rado are each independent directors as required by Section 301 of the Sarbanes-Oxley Act of 2002, Rule 10A(3)(b)(1) of the Securities Exchange Act of 1934 and Section 121(A) of the New York Stock Exchange Constitution and Rules. Raymond Skiptunis served as the Chairman of our audit committee from January 1 through April 20, 2009. Dr. Dunn, the current Chairman of our audit committee, qualifies as a financial expert. Our audit committee, among other things:

- selects the independent auditors, considering independence and effectiveness;
- receives the written disclosures and the letter from the independent accountant required by applicable requirements of the Public Company Accounting Oversight Board regarding the independent accountant's communications with the audit committee concerning independence, and has discussed with the independent accountant the independent accountant's independence;
- discusses the scope and results of the audit with the independent auditors and reviews with management and the independent auditors our interim and year-end operating results;
- discusses with the independent accountant the matters required to be discussed by Statement on Auditing Standards No. 114 (Communications with Audit Committees);
- considers the adequacy of our internal accounting controls and audit procedures;
- reviews and approves all audit and non-audit services to be performed by the independent auditors; and
- administers the whistleblower policy.

The audit committee has the sole and direct responsibility for appointing, evaluating and retaining our independent auditors and for overseeing their work.

Compensation Committee

Kenneth Dickey, Gary Rado and George Boyadjieff currently serve on our compensation committee. Messrs. Dickey, Rado and Boyadjieff are independent directors as required by SEC Rules and as defined in Section 121(A) of the American Stock Exchange Constitution and Rules. Mr. Dickey serves as the Chairman of our compensation committee. Our compensation committee, among other things:

- recommends to the board of directors the compensation level of the executive officers;
- reviews and makes recommendations to our board of directors with respect to our equity incentive plans;
- establishes and reviews general policies relating to compensation and benefits of our employees.

Committee Interlocks and Insider Participation

None of our executive officers currently serve as a member of the board of directors or compensation committee of any entity that has one or more executive officers serving on our board of directors or compensation committee.

SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16 of the Securities Exchange Act of 1934, as amended, requires that all executive officers and directors of the Company and all persons who beneficially own more than ten percent of the Company's common stock file an initial report of their ownership of the Company's securities on Form 3 and report changes in their ownership of the Company's securities on Form 4 or Form 5. These filings must be made with the Securities and Exchange Commission and the National Association of Securities Dealers with a copy sent to the Company. To our knowledge, all executive officers, directors and all persons who beneficially own more than ten percent of the Company's common stock have timely filed these filings.

CODE OF CONDUCT

The Company adopted a code of conduct on August 8, 2008. In early 2006, the Company developed and implemented an official Employee Manual that requires ethical behavior from its employees, and defines the consequences of unethical behavior by its employees.

Item 11. Executive Compensation.

Summary Compensation Table

The following table summarizes compensation information for the last two fiscal years for (i) Mr. Steven Z. Strasser, our Principal Executive Officer and (ii) John (BJ) Lackland, our Principal Financial Officer, who were serving as executive officers at the end of the fiscal year and who we refer to collectively, the Named Executive Officers.

SUMMARY COMPENSATION TABLE

Name and principal position	Year	Salary ($)	Bonus ($)	Stock Awards ($)	Option Awards ($)	Non-Equity Incentive Plan Compensation ($)	Nonqualified Deferred Compensation Earnings ($)	All Other Compensation ($)	Total ($)
Steven Z. Strasser(1)	2009	$ 304,730	-	-	-	-	-	-	$ 304,730
Chairman and Chief	2008	$ 311,208							

20

	Years ended December 31,				
		As Restated(1)			
(in thousands, except per share data)	2011	2010	2009	2008	2007
SELECTED RATIOS:					
Return on average common equity	12.67 %	2.12 %	(34.51)%	0.98 %	10.73 %
Return on average assets	0.74	0.13	(2.05)	0.08	0.93
Efficiency ratio	59.24	60.79	109.95	56.05	60.51
Average common equity to average assets	5.84	5.97	5.92	7.89	8.65
Yield on average interest-earning assets	5.21	5.19	5.15	6.04	7.63
Cost of interest-bearing liabilities	1.27	1.66	2.41	3.20	4.71
Net interest rate spread	3.94	3.53	2.74	2.84	2.92
Net interest rate margin	4.12	3.76	3.06	3.20	3.61
Nonperforming loans to total loans	1.89	2.46	2.10	1.61	0.71
Nonperforming assets to total assets	2.82	2.98	2.69	1.98	0.73
Net chargeoffs to average loans	0.94	1.83	1.42	0.76	0.13
Allowance for loan losses to total loans	1.80	2.26	2.35	1.54	1.27
Dividend payout ratio - basic	14.07	56.00	(5.62)	144.02	15.29

(1) See Note 24 - Restatement of Consolidated Financial Statements for more information.

ITEM 7: MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Introduction

The objective of this section is to provide an overview of the results of operations and financial condition of the Company for the three years ended December 31, 2011. It should be read in conjunction with the Consolidated Financial Statements, Notes and other financial data presented elsewhere in this report, particularly the information regarding the Company's business operations described in Item 1.

Executive Summary

This overview of management's discussion and analysis highlights selected information in this document and may not contain all of the information that is important to you. For a more complete understanding of trends, events, commitments, uncertainties, liquidity, capital resources and critical accounting estimates, you should carefully read this entire document.

2011 Operating Results

For 2011, we reported net income of $25.4 million compared to net income of $5.6 million in 2010. After deducting preferred stock dividends, net income available to common shareholders was $22.9 million, or $1.34 per diluted share, compared to net income available to common shareholders of $3.1 million, or $0.21 per diluted share in 2010.

Acquisitions

On January 7, 2011, the Bank acquired certain assets and assumed certain liabilities of Legacy, a full service community bank that was headquartered in Scottsdale, Arizona. The acquisition consisted of tangible assets with fair values of approximately $128.0 million and liabilities of approximately $130.4 million. In addition, the Bank also acquired approximately $55.6 million of discretionary and $13.6 million of non-discretionary trust assets. The FDIC will reimburse the Bank for 80% of all losses on Covered Assets. In conjunction with the Legacy acquisition, the Company provided the FDIC with a Value Appreciation Instrument (“VAI”) whereby 372,500 units were awarded to the FDIC at an exercise price of $10.63 per unit. The units were exercisable at any time from January 14, 2011 until January 6, 2012. The FDIC exercised the units on January 20, 2011 at a settlement price of $11.8444. A cash payment of $452,364 was made to the FDIC on January 21, 2011.

On August 12, 2011, the Bank acquired certain assets and assumed certain liabilities of FNBO, a full service community bank that was headquartered in Olathe, Kansas. The acquisition consisted of tangible assets at fair value of approximately $481.6 million and liabilities with a fair value of approximately $516.2 million. The FDIC will reimburse the Bank for 80% of losses up to $112.6 million, 0% of losses between $112.6 million and $148.9 million and 80% of losses in excess of $148.9 million with respect to the Covered Assets. In conjunction with the FNBO acquisition, the Company provided the FDIC with a VAI whereby 1.0 million units were awarded to the FDIC at an exercise price of $13.59 per unit. The units were exercisable any time from August 19, 2011 until August 10, 2012. The units were exercised on October 31, 2011 at a settlement price of $15.8393. A cash payment of approximately $2.2 million was made to the FDIC on November 1, 2011. The acquisition of FNBO added approximately $1.4 million of pre-tax earnings, or $0.05 of diluted earnings per share in 2011, including $900,000 of acquisition and conversion related costs.

On October 21, 2011, the Bank purchased certain assets and assumed certain deposit liabilities from BankLiberty of Liberty, Missouri. The Bank assumed $43.0 million in deposits associated with the BankLiberty branch located at 11401 Olive Boulevard, in the St. Louis suburb of Creve Coeur, Missouri. The deposits consisted of $2.6 million in demand deposits, $21.9 million in money market and other interest bearing deposits, and $18.6 million in certificates of deposit. The Bank also paid a deposit premium of $323,000 on these deposits and purchased $150,000 of personal property in the branch. The Bank executed a full-service sublease on approximately 6,556 square feet at the above address. Enterprise will operate the location as a full-service branch of the Bank.

See Note 2 - Acquisitions and Note 6 - Portfolio Loans for more information.

Below are highlights of our Banking and Wealth Management segments. For more information on our segments, see Item 8, Note 20 - Segment Reporting. Unless otherwise noted, this discussion excludes discontinued operations.

Banking

For 2011, the Banking segment recorded net income of $29.1 million compared to net income of $10.4 million for 2010. Excluding the non-tax deductible goodwill impairment of $45.4 million, the Banking segment recorded net income of $2.2 million for 2009. Below is a summary of 2011:

- Loan demand - Portfolio loans were $2.2 billion at December 31, 2011, including $300.6 million of loans covered under FDIC shared-loss agreements ("Covered loans"). Portfolio loans, excluding the Covered loans ("Non-covered loans"), increased $130.7 million, or 7%, from December 31, 2010. We expect similar Non-covered loan growth in 2012 as business activity continues to improve and additional capacity from new hires takes effect.

Excluding Covered loans, Commercial and industrial loans increased $169.3 million, or 29%, since December 31, 2010, while Construction and residential real estate loans decreased $68.6 million, or, 18%, over the same time frame.

	December 31,					
(in thousands)	2011			2010		
Commercial and industrial	763,202	35	%	593,938	31	%
Commercial real estate - Investor Owned	477,154	22	%	444,724	24	%
Commercial real estate - Owner Occupied	334,416	15	%	331,544	18	%
Construction and land development	140,147	6	%	190,285	10	%
Residential real estate	171,034	8	%	189,484	10	%
Consumer & other	11,121	1	%	16,376	1	%
Portfolio loans covered under FDIC loss share	300,610	13	%	121,570	6	%
Total loan portfolio	2,197,684	100	%	1,887,921	100	%

- Deposit growth – Total deposits at December 31, 2011 were $2.8 billion, an increase of $493.6 million, or 21%, over December 31, 2010. Excluding brokered certificates of deposit, “core” deposits increased $523.0 million, or 24%, to $2.7 billion from December 31, 2010. Noninterest-bearing demand deposits increased $219.4 million, or 60%, in 2011 and represented 21% of total deposits at December 31, 2011, up from 16% at December 31, 2010. Management believes a portion of the growth in noninterest-bearing demand deposits is the result of the FDIC deposit guarantee and relatively low rates on non-guaranteed accounts. The Company has maintained a favorable deposit mix, with core deposits representing 96% of total deposits at December 31, 2011, compared to 93% in the prior year.

The FNB acquisition added $423.1 million in deposits in the third quarter of 2011. These deposits included $66.9 million in noninterest-bearing demand deposits, $123.6 million in money market and other interest-bearing transaction accounts, and $232.6 million in certificates of deposit.

- Asset quality – Nonperforming loans were $41.6 million, or 1.89%, of portfolio loans at December 31, 2011. The allowance for loan losses was $39.6 million, or 1.80%, of portfolio loans versus $42.8 million, or 2.26% of portfolio loans, at the end of 2010. In 2011, net charge-offs were $19.2 million, or 0.94% of average loans compared to $34.0 million of net charge-offs, or 1.83% of average loans in 2010.

Provision for loan losses not covered under FDIC loss share was $13.3 million for 2011 compared to $33.7 million for 2010. The decrease in provision was primarily due to fewer loan risk rating downgrades. Excluding the Covered loans, the Company's watch list credits as a percentage of total loans declined almost a full percentage point in 2011. The Company continues to monitor loan portfolio risk closely. See Provision for Loan Losses and Nonperforming Assets below for more information. The Company recorded $2.8 million in provision for loan losses covered under FDIC loss share agreements in 2011. This impact was partially offset through noninterest income by an increase in the FDIC loss share receivable.

- Net Interest Rate Margin – Our fully tax-equivalent net interest rate margin was 4.12% for 2011 versus 3.76% for 2010. The net interest margin was favorably impacted by lower deposit costs, and the net interest income generated by the loans acquired in the FDIC-assisted acquisitions in 2010 and 2011. For 2011, the net interest rate margin, less the FDIC loss share loans, related nonearning assets and acquired deposits, was 3.42% compared to 3.53% for 2010.

We expect our 2012 net interest margin will be 4% or more based on a better earning asset mix, the full year impact of the FNBO acquisition and continued discipline on funding costs. We expect continued volatility in the yield on Covered loans, especially due to unanticipated prepayment activity. In 2011, there was approximately $14.3 million of accelerated discount recognized in interest income on Covered loans due primarily to prepayments. After recognizing any related offsets to the indemnification asset through noninterest income, pre-tax earnings were positively impacted by $6.8 million in 2011. In addition, the quarterly re-measurement of cash flows from Covered loans can impact the prospective yield on Covered loans and adjustments to the indemnification asset.

- Noninterest expenses and efficiency ratio – Noninterest expense increased $15.5 million, or 25%, in 2011. The increase over the prior year period was primarily due to increases in salaries and benefits, occupancy, data processing and other operating expenses related to the 2011 acquisitions. The Company's efficiency ratio, which measures noninterest expense as a percentage of total revenue, for 2011 was 59.2% compared to 60.8% for 2010.

Wealth Management

The Wealth Management segment is comprised of Enterprise Trust and our state tax credit brokerage activities. Wealth Management is a strategic line of business consistent with our Company mission of “guiding our clients to a lifetime of financial success.” It is a driver of fee income and is intended to help us diversify our dependency on bank spread income.

For 2011, the Wealth Management segment recorded net income of $1.3 million compared to a net loss of $178,000 in 2010.

- Trust revenues - Revenues from the Trust division increased $427,000, or 7%, over 2010. The increase in Trust revenue was primarily attributable to the impact of the additional Legacy and FNBO trust business. Trust assets under administration were $1.6 billion at December 31, 2011 compared to $1.5 billion at December 31, 2010, a 7% increase over one year ago.

- State tax credit brokerage activities - In 2011, revenue from state tax credit brokerage activities were $3.6 million, a $1.4 million, or 62% increase over 2010. The increase is primarily due to a $1.7 million increase from the sale of state tax credits.

RESULTS OF CONTINUING OPERATIONS ANALYSIS

Net Interest Income

Comparison of 2011 vs. 2010

Net interest income is the primary source of the Company's revenue. Net interest income is the difference between interest income on earning assets, such as loans and securities, and the interest expense on interest-bearing deposits and other borrowings used to fund interest earning and other assets. The amount of net interest income is affected by changes in interest rates and by the amount and composition of interest-earning assets and interest-bearing liabilities, such as the mix of fixed vs. variable rate loans. When and how often loans and deposits mature and re-price also impacts net interest income.

Net interest spread and net interest rate margin are utilized to measure and explain changes in net interest income. Interest rate spread is the difference between the yield on interest-earning assets and the rate paid for interest-bearing liabilities that fund those assets. The net interest rate margin is expressed as the percentage of net interest income to average interest-earning assets. The net interest rate margin exceeds the interest rate spread because noninterest-bearing sources of funds (net free funds), principally demand deposits and shareholders' equity, also support earning

24

assets.

Net interest income (on a tax-equivalent basis) increased $29.0 million, or 34%, from $85.0 million for 2010 to $114.0 million for 2011. Total interest income increased $26.7 million while total interest expense decreased $2.3 million.

Average interest-earning assets were $2.8 billion in 2011, an increase of $505.4 million, or 22%, from 2010. Loans accounted for the majority of the growth, increasing by $198.7 million, or 11%, to $2.1 billion. Securities and short-term investments increased $306.7 million, or 75% to $714.3 million from 2010. Interest income increased $30.9 million due to volume and decreased by $4.2 million due to the impact of rates, for a net increase of $26.7 million versus 2010.

Average interest-bearing liabilities increased $419.7 million, or 21%, to $2.4 billion compared to $2.0 billion for 2010. The increase in interest-bearing liabilities primarily resulted from a $397.8 million increase in interest-bearing deposits. For 2011, interest expense on interest-bearing liabilities increased $4.3 million due to volume while the impact of declining rates decreased interest expense on interest-bearing liabilities by $6.5 million, for a net decrease of $2.3 million versus 2010. See “Liquidity and Capital Resources” for more information.

For the year ended December 31, 2011, the tax-equivalent net interest rate margin was 4.12% compared to 3.76% for 2010. The net interest margin was favorably impacted by lower deposit costs and the net interest income generated by the loans acquired in the Legacy and FNBO acquisitions. For 2011, the net interest rate margin, less the FDIC loss share loans, related nonearning assets and acquired deposits, was 3.42% compared to 3.53% for 2010.

Comparison of 2010 vs. 2009
Net interest income (on a tax-equivalent basis) increased $13.6 million, or 19%, from $71.4 million for 2009 to $85.0 million for 2010. Total interest income decreased $2.8 million while total interest expense decreased $16.4 million.

Average interest-earning assets were $2.3 billion in 2010, a decrease of $73.8 million, or 3%, from 2009. Loans accounted for the majority of the reduction, decreasing by $245.1 million, or 12%, to $1.9 billion. The decrease in loans was partially offset by an increase in securities and short-term investments of $171.3 million, or 72% to $407.7 million. Interest income decreased $4.4 million due to volume declines and increased by $1.6 million due to the impact of rates, for a net decrease of $2.8 million versus 2009.

Average interest-bearing liabilities decreased $67.9 million, or 3%, to $2.0 billion compared to $2.0 billion for 2009. The decrease in interest-bearing liabilities resulted from a $199.3 million decrease in borrowed funds. The decrease in borrowed funds was partially offset by a $131.3 million increase in interest-bearing deposits. For 2010, interest expense on interest-bearing liabilities decreased $4.8 million due to volume while the impact of declining rates decreased interest expense on interest-bearing liabilities by $11.6 million, for a net decrease of $16.4 million versus 2009. See “Liquidity and Capital Resources” for more information.

For the year ended December 31, 2010, the tax-equivalent net interest rate margin was 3.76% compared to 3.06% for 2009. The net interest margin was favorably impacted by lower deposit costs and the net interest income generated by the loans acquired in the Home National asset purchase.

Average Balance Sheet

The following table presents, for the periods indicated, certain information related to our average interest-earning assets and interest-bearing liabilities, as well as, the corresponding interest rates earned and paid, all on a tax equivalent basis.

	For the years ended December 31,								
	2011			2010			2009		
(in thousands)	Average Balance	Interest Income/Expense	Average Yield/ Rate	Average Balance	Interest Income/Expense	Average Yield/ Rate	Average Balance	Interest Income/Expense	Average Yield/ Rate
Assets									
Interest-earning assets:									
Taxable loans (1)	$1,786,601	$95,520	5.35 %	$1,751,459	$95,798	5.47 %	$2,043,202	$109,413	5.35 %
Tax-exempt loans (2)	32,935	2,542	7.72	30,564	2,621	8.58	53,826	4,868	9.04
Covered loans (3)	232,363	32,926	14.17	71,152	10,924	15.35	1,244	38	3.05
Total loans	2,051,899	130,988	6.38	1,853,175	109,343	5.90	2,098,272	114,319	5.45
Taxable investments in debt and equity securities	473,620	11,510	2.43	276,493	7,458	2.70	172,815	5,778	3.34
Non-taxable investments in debt and equity securities (2)	22,434	1,086	4.84	5,132	245	4.77	634	37	5.84
Short-term investments	218,287	562	0.26	126,058	380	0.30	62,976	136	0.22
Total securities and short-term investments	714,341	13,158	1.84	407,683	8,083	1.98	236,425	5,951	2.52
Total interest-earning assets	2,766,240	144,146	5.21	2,260,858	117,426	5.19	2,334,697	120,270	5.15
Noninterest-earning assets:									
Cash and due from banks	15,801			11,800			23,959		
Other assets	357,993			227,038			146,674		
Allowance for loan losses	(43,887)			(45,673)			(43,093)		
Total assets	$3,096,147			$2,454,023			$2,462,237		
Liabilities and Shareholders' Equity									
Interest-bearing liabilities:									
Interest-bearing transaction accounts	$212,257	$811	0.38 %	$190,275	$847	0.45 %	$122,563	$662	0.54 %

Money market accounts	997,415	7,987	0.80	701,360	6,245	0.89	636,350	6,079	0.96
Savings	27,106	112	0.41	10,022	35	0.35	9,147	35	0.38
Certificates of deposit	847,057	12,748	1.50	784,369	15,740	2.01	786,631	23,427	2.98
Total interest-bearing deposits	2,083,835	21,658	1.04	1,686,026	22,867	1.36	1,554,691	30,203	1.94
Subordinated debentures	85,081	4,515	5.31	85,081	4,954	5.82	85,081	5,171	6.08
Borrowed funds	208,128	3,982	1.91	186,283	4,590	2.46	385,567	13,471	3.49
Total interest-bearing liabilities	2,377,044	30,155	1.27	1,957,390	32,411	1.66	2,025,339	48,845	2.41
Noninterest bearing liabilities:									
Demand deposits	494,609			305,887			250,435		
Other liabilities	10,844			12,115			9,089		
Total liabilities	2,882,497			2,275,392			2,284,863		
Shareholders' equity	213,650			178,631			177,374		
Total liabilities & shareholders' equity	$3,096,147			$2,454,023			$2,462,237		
Net interest income		$113,991			$85,015			$71,425	
Net interest spread			3.94 %			3.53 %			2.74 %
Net interest rate margin (4)			4.12			3.76			3.06

(1) Average balances include non-accrual loans. The income on such loans is included in interest but is recognized only upon receipt. Loan fees, net of amortization of deferred loan origination fees and costs, included in interest income are approximately $1,029,000, $1,440,000 and $1,626,000 for the years ended December 31, 2011, 2010, and 2009, respectively.

26

(2) Non-taxable income is presented on a fully tax-equivalent basis using a 36% tax rate. The tax-equivalent adjustments were $1,306,000, $1,032,000, and $1,784,000 for the years ended December 31, 2011, 2010, and 2009, respectively.
(3) Covered loans are loans covered under FDIC shared-loss agreements and are recorded at fair value.
(4) Net interest income divided by average total interest-earning assets.

Rate/Volume
The following table sets forth, on a tax-equivalent basis for the periods indicated, a summary of the changes in interest income and interest expense resulting from changes in yield/rates and volume.

	2011 compared to 2010			2010 compared to 2009		
	Increase (decrease) due to			Increase (decrease) due to		
(in thousands)	Volume(1)	Rate(2)	Net	Volume(1)	Rate(2)	Net
Interest earned on:						
Taxable loans	$1,902	$(2,180)	$(278)	$(15,915)	$2,300	$(13,615)
Nontaxable loans (3)	194	(273)	(79)	(2,007)	(240)	(2,247)
Covered loans	22,907	(905)	22,002	10,149	737	10,886
Taxable investments in debt and equity securities	4,855	(803)	4,052	2,960	(1,280)	1,680
Nontaxable investments in debt and equity securities (3)	838	3	841	216	(8)	208
Short-term investments	244	(62)	182	175	69	244
Total interest-earning assets	$30,940	$(4,220)	$26,720	$(4,422)	$1,578	$(2,844)
Interest paid on:						
Interest-bearing transaction accounts	$92	$(128)	$(36)	$317	$(132)	$185
Money market accounts	2,422	(680)	1,742	596	(430)	166
Savings	70	7	77	3	(3)	—
Certificates of deposit	1,182	(4,174)	(2,992)	(67)	(7,620)	(7,687)
Subordinated debentures	—	(439)	(439)	—	(217)	(217)
Borrowed funds	497	(1,105)	(608)	(5,656)	(3,225)	(8,881)
Total interest-bearing liabilities	4,263	(6,519)	(2,256)	(4,807)	(11,627)	(16,434)
Net interest income	$26,677	$2,299	$28,976	$385	$13,205	$13,590

(1) Change in volume multiplied by yield/rate of prior period.
(2) Change in yield/rate multiplied by volume of prior period.
(3) Nontaxable income is presented on a fully-tax equivalent basis using a 36% tax rate.
NOTE: The change in interest due to both rate and volume has been allocated to rate and volume changes in proportion to the relationship of the absolute dollar amounts of the change in each.

Provision for loan losses.
The provision for loan losses not covered under FDIC loss share was $13.3 million for 2011 compared to $33.7 million for 2010 and $40.4 million for 2009. The decline in the provision for loan losses since 2011 is due to lower levels of adverse risk rating changes and trends in nonperforming loans.

For Covered loans, the Company re-measures contractual and expected cashflows on a quarterly basis. When the re-measurement process results in a decrease in expected cash flows due to an increase in expected credit losses, impairment is recorded. As a result of this impairment, the FDIC loss share receivable is increased to reflect anticipated future cash to be received from the FDIC. The amount of the increase is determined based on the specific loss share agreement, but is generally 80% of the losses. In the third quarter of 2011, an impairment of $2.7 million was recorded in the provision for loan losses covered under FDIC loss share for certain loan pools covered under loss share which was partially offset through noninterest income by an increase in the FDIC loss share receivable. In the fourth quarter of

27

2011, this impairment reversed, but was offset by impairment on other loan pools covered under loss share. The FDIC loss share receivable was adjusted accordingly.

See the sections below captioned “Loans” And “Allowance for Loan Losses” for more information on our loan portfolio and asset quality.

Noninterest Income

The following table presents a comparative summary of the major components of noninterest income.

(in thousands)	Years ended December 31, 2011	2010	2009	Change 2011 over 2010	Change 2010 over 2009
Wealth Management revenue	$6,841	$6,414	$4,524	$427	$1,890
Service charges on deposit accounts	5,091	4,739	5,012	352	(273)
Other service charges and fee income	1,679	1,128	963	551	165
Sale of other real estate	862	79	(436)	783	515
State tax credit activity, net	3,645	2,250	1,035	1,395	1,215
Sale of securities	1,450	1,987	955	(537)	1,032
Change in FDIC loss share receivable	(3,494)	99	—	(3,593)	99
Extinguishment of debt	—	—	7,388	—	(7,388)
Miscellaneous income	2,434	1,664	436	770	1,228
Total noninterest income	$18,508	$18,360	$19,877	$148	$(1,517)

Comparison 2011 vs. 2010

Noninterest income increased $148,000, or 1% in 2011 compared to 2010. Our ratio of noninterest income to total revenue for 2011 was 14%, compared to 18% in 2010.

Wealth Management revenue from the Trust division increased $427,000, or 7%. The increase in Trust revenue was primarily attributable to the impact of the additional Legacy and FNBO trust business. Assets under administration were $1.6 billion at December 31, 2011, a $104.0 million, or 7% increase from one year ago.

In 2011, we sold $44.6 million of other real estate at a gain of $862,000. In 2010, we sold $26.0 million of other real estate at a gain of $79,000.

Gains from state tax credit brokerage activities were $3.6 million in 2011, compared to $2.3 million in 2010, an increase of $1.4 million. The increase is due to a $1.7 million increase from the sale of state tax credits to clients, and a $905,000 increase in the fair value adjustment on the related interest rate caps used to economically hedge the tax credits partially offset by a $1.2 million negative fair value adjustment on the tax credit assets.

In 2011, the Company purchased approximately $431.4 million in securities primarily in U.S. Government sponsored enterprises and Residential mortgage-backed securities and sold approximately $84.5 million of securities realizing a gain of $1.5 million on these sales.

The decrease in income related to the FDIC loss share receivable was primarily due to loan pay offs in which the losses on the loans were less than expected along with lower loss expectations on certain loan pools. To correlate with the new projected loss amounts, the FDIC loss share receivable must be reduced. In 2012, absent any changes based on the results of the quarterly re-measurement process, the Company anticipates continued lower losses in certain loan pools. These lower loss expectations will reduce the accretion on the FDIC loss share receivable and may result in negative accretion.

The increase in Miscellaneous income was primarily due to $313,000 in fee income earned related to the allocation of New Market Tax Credits to developers and projects along with distributions from private equity fund investments.

Comparison 2010 vs. 2009
The 2009 results include a $7.4 million pre-tax gain from the extinguishment of debt. Excluding the gain on extinguishment of debt, noninterest income increased $5.9 million, or 47%, during 2010.

Wealth Management revenue from the Trust division increased $1.9 million, or 42%. The increase in revenue was attributable to higher account asset values, several estate planning-related insurance sales and generally improving sales momentum in the Trust organization. In 2010, we elected to record Wealth Management revenue on a gross basis resulting in a $971,000 increase in Wealth Management revenue which was offset by a related $971,000 increase in Other expenses. Assets under administration were $1.499 billion at December 31, 2010, a $219 million, or 17% increase from one year ago primarily due to higher asset values from stronger financial markets.

In 2010, we sold $26.0 million of other real estate at a gain of $79,000. In 2009, we sold $22.3 million of other real estate at a loss of $436,000.

Gains from state tax credit brokerage activities were $2.3 million in 2010, compared to $1.0 million in 2009. The increase is due to a $142,000 increase from the sale of state tax credits to clients, and a $3.0 million positive fair value adjustment on the tax credit assets offset by a $1.9 million decrease in the fair value adjustment on the related interest rate caps used to economically hedge the tax credits.

In 2010, the Company elected to reposition a portion of the investment portfolio and sold approximately $127.0 million of securities realizing a gain of $2.0 million on these sales. With the proceeds from securities sales and maturities and excess cash, we purchased approximately $323.8 million in mortgage backed securities, including collateralized mortgage obligations, government sponsored agency debentures, and federally tax free municipal securities.

The increase in Miscellaneous income was primarily due to $776,000 of income on bank-owned life insurance policies, and $524,000 related to two interest rate swaps terminated by the Company in 2009.

Noninterest Expense

The following table presents a comparative summary of the major components of noninterest expense.

(in thousands)	Years ended December 31, 2011	2010	2009	Change 2011 over 2010	Change 2010 over 2009
Employee compensation and benefits	36,839	28,316	25,969	8,523	2,347
Occupancy	5,001	4,297	4,709	704	(412)
Furniture and equipment	1,601	1,393	1,425	208	(32)
Data processing	3,159	2,234	2,147	925	87
Communications	636	554	556	82	(2)
Director related expense	599	607	459	(8)	148
Meals and entertainment	1,747	1,258	1,037	489	221
Marketing and public relations	1,063	902	504	161	398
FDIC and other insurance	4,119	4,402	4,204	(283)	198
Amortization of intangibles	999	420	482	579	(62)
Goodwill impairment charges	—	—	45,377	—	(45,377)
Postage, courier, and armored car	909	769	772	140	(3)
Professional, legal, and consulting	3,138	1,736	2,278	1,402	(542)
Loan, legal and other real estate expense	10,703	9,941	4,788	762	5,153
Other taxes	675	635	566	40	69
Other	6,530	4,748	3,154	1,782	1,594
Total noninterest expense	$77,718	$62,212	$98,427	$15,506	$(36,215)

Comparison 2011 vs. 2010

Noninterest expense increased $15.5 million, or 25%, in 2011. The Company's efficiency ratio, which measures noninterest expense as a percentage of total revenue, for 2011 was 59.2% compared to 60.8% for 2010.

Employee compensation and benefits. Employee compensation and benefits increased $8.5 million, or 30%, over 2010. Employee compensation and benefits increased primarily due to staff additions to support our Kansas and Arizona acquisition activity and higher variable compensation accruals.

All other expense categories. All other expense categories increased $7.0 million, or 21%, over 2010. With the exception of professional, legal and consulting and loan, legal and other real estate expenses, most categories of expenses were relatively flat year over year.

Occupancy expense and data processing increases were due to the addition of new branches as part of our acquisition activity in 2011.

Professional, legal and consulting increased $1.4 million due to litigation defense costs, fees related to the FNBO acquisition, and various consulting expenses related to new business activities and regulatory compliance. Loan, legal and other real estate expenses increased $762,000 due to increased levels of other real estate properties. Other real estate expenses for items such as utilities, legal fees and insurance increased $1.8 million over 2010. These expenses were partially offset by a $930,000 decrease in expenses related to writedowns on other real estate.

In 2012, the Company expects noninterest expenses to average $20 to $22 million per quarter as loan collection expenses on Covered assets remain elevated and the full year impact of compensation expense for the FNBO acquisition and expenses for other new initiatives are realized.

Comparison 2010 vs. 2009
Noninterest expense decreased $36.2 million, or 37%, in 2010. The decrease was primarily due to a $45.4 million

30

goodwill impairment charge associated with the banking segment in 2009. Excluding the goodwill impairment charge, noninterest expenses increased $9.2 million, or 17%. The Company's efficiency ratio, which measures noninterest expense as a percentage of total revenue, for 2010 was 60.8%. Excluding the goodwill impairment charge, the efficiency ratio was 59.3% in 2009.

Employee compensation and benefits. Employee compensation and benefits increased $2.3 million, or 9%, over 2009. Employee compensation and benefits increased primarily due to the recruitment of several prominent St. Louis bankers, higher variable compensation accruals, and staff additions to support our Arizona acquisition activity.

All other expense categories. Excluding the goodwill impairment charge, all other expense categories increased $6.8 million, or 25%, over 2009. With the exception of loan, legal and other real estate expenses, most categories of expenses were relatively flat year over year.

Occupancy expense decreases were due to lower amortization of leasehold improvements in 2010.

Loan, legal and other real estate expenses increased $5.2 million due to increased levels of nonperforming loans and other real estate properties. Approximately, $3.2 million of the increase represents fair value writedowns on other real estate. Other real estate expenses for items such as utilities, legal fees and insurance increased $1.1 million over 2009. Approximately $278,000 of the increase was related to estimated losses attributable to the unadvanced commitments on impaired loans.

In 2010, we elected to record Wealth Management revenue on a gross basis resulting in a $971,000 increase in Other expenses offset by a related $971,000 increase in Wealth Management revenue. Other expenses also include a $250,000 accrual for a potential loss on a depository account.

Discontinued Operations

On January 20, 2010, we sold Millennium Brokerage Group, LLC, a wholly owned life insurance subsidiary, to an investor group led mostly by former managers of Millennium for $4.0 million in cash, resulting in a $1.6 million pre-tax loss recognized in 2009. As a result of the sale, we have reclassified the results of Millennium for 2009 and prior periods to discontinued operations. The amount of the loss on the sale is primarily due to the write-off of the remaining goodwill associated with the Millennium reporting unit.

For 2009, net loss from discontinued operations was $1.3 million, compared to a net loss of $6.2 million from discontinued operations in 2008. The 2008 loss includes $9.2 million of pre-tax goodwill impairment charges and lower levels of paid premium sales and lower sales margins which significantly reduced Millennium's operating results.

Income Taxes

In 2011, the Company recorded income tax expense of $11.9 million on pre-tax income of $37.4 million, resulting in an effective tax rate of 32.0%. The following items were included in Income tax expense (benefit) and impacted the 2011 effective tax rate:

- the expiration of the statute of limitations for the 2007 tax year warranted the release of $306,000 of reserves related to certain state tax positions;
- recognition of federal tax benefits of $729,000 related to low income housing tax credits from limited partnership interests.

In 2010, the Company recorded income tax expense of $0.8 million on pre-tax income of $6.4 million, resulting in an effective tax rate of 12.9%. The following items were included in Income tax expense (benefit) and impacted the 2010 effective tax rate:

- the expiration of the statute of limitations for the 2006 tax year warranted the release of $341,000 of reserves related to certain state tax positions;
- recognition of federal tax benefits of $729,000 related to low income housing tax credits from limited partnership interests.

FINANCIAL CONDITION

Comparison for December 31, 2011 and 2010
Total assets at December 31, 2011 were $3.4 billion compared to $2.8 billion at December 31, 2010, an increase of $577.6 million, or 21%. Acquisitions and organic growth drove the increase which included a $309.8 million increase in portfolio loans, a $231.6 million increase in securities available for sale, and a $96.8 million increase in the FDIC loss share receivable.

At December 31, 2011, portfolio loans totaled $2.2 billion, an increase of $309.8 million, or 16% from December 31, 2010. For the year, the Covered loans increased $179.0 million to $300.6 million, while Non-covered loans increased by $130.7 million, or 7% .

Strong core deposit growth in 2011, led to significant increases in cash. A portion of the cash was used to increase the available for sale securities portfolio. Securities available for sale were $593.2 million at December 31, 2011 compared to $361.5 million at December 31, 2010. In 2011, securities purchases included government sponsored agency debentures, mortgage backed securities, including collateralized mortgage obligations, and federally tax free municipal securities.

At December 31, 2011, the FDIC loss share receivable included $12.5 million due from the FDIC pursuant to the First Amendment to Purchase and Assumption Agreement with the FDIC as Receiver for FNBO. For more information, see the Form 8-K filed with the SEC on March 22, 2012.

At December 31, 2011, Other assets included $21.5 million of bank-owned life insurance and $5.5 million of prepaid FDIC insurance.

At December 31, 2011, deposits were $2.8 billion, an increase of $493.6 million, or 21%, from $2.3 billion at December 31, 2010. The FNB acquisition added $423.1 million in deposits in the third quarter of 2011. These deposits included $66.9 million in noninterest-bearing demand deposits, $123.6 million in money market and other interest-bearing transaction accounts, and $232.6 million in certificates of deposit.

Other borrowings at December 31, 2011 and 2010 represent customer repurchase agreements.

On May 24, 2011, the Company issued 2,743,900 shares, or $35.0 million in common stock through a public offering. The net proceeds to the Company, after deducting underwriting discounts and commissions and offering expenses, was approximately $32.6 million.

On January 25, 2010, the Company completed the sale of 1,931,610 shares, or $15.0 million of its common stock in a private placement offering. The net proceeds to the Company, after deducting underwriting discounts and commissions and offering expenses, was approximately $14.9 million.

Loans
Non-covered portfolio loans less unearned loan fees, increased $130.7 million, or 7%, during 2011. Non-covered Commercial & Industrial loans increased $169.3 million, or 28%, during the year and represent 40% of the loan portfolio at December 31, 2011. The Company's lending strategy emphasizes commercial, residential real estate, and commercial real estate loans to small and medium sized businesses and their owners in the St. Louis, Kansas City and Phoenix metropolitan markets. Consumer lending, including residential real estate, is minimal. Payoffs and paydowns, along with net charge-offs contributed to the decline in loan balances.

A common underwriting policy is employed throughout the Company. Lending to small and medium sized businesses is riskier from a credit perspective than lending to larger companies, but the risk is appropriately considered with higher loan pricing and ancillary income from cash management activities. As additional risk mitigation, the Company will generally hold only $12.0 million or less of aggregate credit exposure (both direct and indirect) with one borrower, in

32

spite of a legal lending limit of over $68 million. There are seven borrowing relationships where we have committed more than $10.0 million with the largest being a $15.0 million line of credit with minimal usage. For the $1.9 billion loan portfolio, the Company's average loan relationship size was just under $1.0 million, and the average note size is approximately $500,000.

The Company also buys and sells loan participations with other banks to help manage its credit concentration risk. At December 31, 2011, the Company had purchased loan participations of $305.8 million ($166.5 million outstanding) and had sold loan participations of $398.7 million ($310.5 million outstanding). Approximately 71 borrowers make up the participations purchased, with an average outstanding loan balance of $1.6 million. Seventeen relationships, or $62.0 million of the $166.5 million in participations purchased, met the definition of a “Shared National Credit”; however, only two of the relationships, or $12.0 million, were considered out of our market.

The following table sets forth the composition of the Company's loan portfolio by type of loans as reported in the quarterly Federal Financial Institutions Examination Council Report of Condition and Income (“Call report”) at the dates indicated.

	December 31,				
(in thousands)	2011	2010	2009	2008	2007
Commercial and industrial	$763,202	$593,938	$553,988	$675,216	$549,479
Real Estate:					
Commercial	811,570	776,268	817,332	887,963	720,072
Construction and land development	140,147	190,285	221,397	378,092	301,710
Residential	171,034	189,484	209,743	235,019	175,258
Consumer and other	11,121	16,376	16,021	25,167	37,759
Total Portfolio loans not covered under FDIC loss share	1,897,074	1,766,351	1,818,481	2,201,457	1,784,278
Portfolio loans covered under FDIC loss share	300,610	121,570	13,644	—	—
Total Loans	$2,197,684	$1,887,921	$1,832,125	$2,201,457	$1,784,278

	December 31,				
(in thousands)	2011	2010	2009	2008	2007
Commercial and industrial	40.2 %	33.6 %	30.5 %	30.7 %	30.8 %
Real Estate:					
Commercial	42.8 %	43.9 %	44.9 %	40.3 %	40.4 %
Construction and land development	7.4 %	10.8 %	12.2 %	17.2 %	16.9 %
Residential	9.0 %	10.7 %	11.5 %	10.7 %	9.8 %
Consumer and other	0.6 %	1.0 %	0.9 %	1.1 %	2.1 %
Total Portfolio loans not covered under FDIC loss share	100.0 %	100.0 %	100.0 %	100.0 %	100.0 %

Commercial and industrial loans are made based on the borrower's character, experience, general credit strength, and ability to generate cash flows for repayment from income sources, even though such loans may also be secured by real estate or other assets. The credit risk related to commercial loans is largely influenced by general economic conditions and the resulting impact on a borrower's operations. Commercial and industrial loans are primarily made to borrowers operating within the manufacturing industry.

Real estate loans are also based on the borrower's character, but more emphasis is placed on the estimated collateral values.

Approximately $305.5 million, or 38%, of the Non-covered commercial real estate loans were owner-occupied by commercial and industrial businesses where the primary source of repayment is dependent on sources other than the underlying collateral. Multifamily properties and other commercial properties on which income from the property is the primary source of repayment represent the balance of this category. The majority of this category of loans is secured by commercial and multi-family properties located within our St. Louis and Kansas City markets. These loans are underwritten based on the cash flow coverage of the property, typically meet the Company's loan to value guidelines, and generally require either the limited or full guaranty of principal sponsors of the credit.

Real estate construction loans, relating to residential and commercial properties, represent financing secured by raw ground or real estate under development for eventual sale. Approximately $42.5 million of these loans include the use of interest reserves and follow standard underwriting guidelines. Construction projects are monitored by the officer and a centralized independent loan disbursement function is employed. Given the weak demand and stress in both the residential and commercial real estate markets, the Company reduced the level of these loan types in 2011.

Residential real estate loans include residential mortgages, which are loans that, due to size, do not qualify for conventional home mortgages that the Company sells into the secondary market, second mortgages and home equity lines. Residential mortgage loans are usually limited to a maximum of 80% of collateral value.

Consumer and other loans represent loans to individuals on both a secured and unsecured basis. Credit risk is mitigated by thoroughly reviewing the creditworthiness of the borrowers prior to origination.

Following is a further breakdown of our loan categories using Call report codes at December 31, 2011 and 2010:

	% of portfolio 2011			2010
	Portfolio Loans not Covered under FDIC loss share	Portfolio Loans Covered under FDIC loss share	Total	Total
Real Estate:				
Construction & Land Development	7 %	22 %	9 %	12 %
Commercial Owner Occupied				
Commercial & Industrial	16 %	18 %	16 %	17 %
Other	2 %	3 %	2 %	2 %
Total	18 %	21 %	18 %	19 %
Commercial Investor Owned				
Retail	8 %	13 %	9 %	8 %
Commercial Office	7 %	7 %	7 %	7 %
Multi-Family Housing	3 %	2 %	3 %	3 %
Churches/ Schools/ Nursing Homes/ Other	3 %	— %	3 %	3 %
Industrial/ Warehouse	4 %	3 %	4 %	4 %
Total	25 %	25 %	26 %	25 %
Residential:				
Owner Occupied	6 %	15 %	7 %	7 %
Investor Owned	3 %	4 %	3 %	4 %
Total	9 %	19 %	10 %	11 %
Total Real Estate	59 %	87 %	63 %	67 %
Non Real Estate				
Commercial & Industrial	40 %	12 %	36 %	32 %
Consumer & Other	1 %	1 %	1 %	1 %
Total Non Real Estate	41 %	13 %	37 %	33 %
Total	100 %	100 %	100 %	100 %

The following descriptions focus on the Non-covered portion of the loan portfolio.

The Non-covered Construction and Land Development category represents $140.1 million, or 7%, of the total loan portfolio. Within that category, there was $10.0 million of loans secured by raw ground, $66.6 million of commercial construction, and $63.5 million of residential construction. Of the $140.1 million in loans in the Non-covered Construction and Land Development category, approximately $49 million was included on the Watch List.

The Non-covered Commercial construction component of the portfolio consisted of approximately 49 loan relationships with an average outstanding loan balance of $1.1 million. The largest loans were a $9.1 million line of credit secured by commercially zoned land in St. Louis, and a $4.5 million fixed line secured by commercially zoned land in Kansas City.

The Non-covered Residential construction component of the portfolio consists of single family housing development properties primarily in our St. Louis and Kansas City markets. There were approximately 87 loan relationships in this category with an average outstanding loan balance of $435,000. The largest loan was a $2.9 million residential development in the Kansas City market.

The largest segments of the non-owner occupied components of the commercial real estate portfolio are retail and commercial office permanent loans. At December 31, 2011, the Company had $147.0 million of Non-covered non-owner occupied permanent loans secured by retail properties. There were approximately 62 loan relationships in this category with an average outstanding loan balance of $1.5 million. The largest loans outstanding at year end were an $7.8 million loan secured by various retail properties in Kansas City, a $6.8 million loan secured by a hotel in Arizona, and a $6.4 million loan secured by a retail shopping center in Kansas City.

At December 31, 2011, the Company $134.7 million of Non-covered non-owner occupied permanent loans secured by commercial office properties. There were approximately 71 loan relationships with an average outstanding loan balance of $1.5 million. The largest loans outstanding at year end were an $8.6 million loan secured by a single tenant office building in Kansas City, a $7.9 million loan secured by a medical office building in the St. Louis region and a $5.9 million loan secured by a multi-tenant office property in Kansas City.

Vacancy rates for commercial office space in the St. Louis and Kansas City markets totaled 17.3% and 16.3%, respectively at year end, as compared to the national commercial office vacancy rate of 17.3%.

Factors that are critical to managing overall credit quality are sound loan underwriting and administration, systematic monitoring of existing loans and commitments, early identification of potential problems, an adequate allowance for loan losses, and sound non-accrual and charge-off policies.

Significant loan concentrations are considered to exist for a financial institution when there are amounts loaned to numerous borrowers engaged in similar activities that would cause them to be similarly impacted by economic or other conditions. At December 31, 2011, no significant concentrations exceeding 10% of total loans existed in the Company's loan portfolio, except as described above.

Loans at December 31, 2011 mature or reprice as follows:

	Loans Maturing or Repricing			
(in thousands)	In One Year or Less	After One Through Five Years	After Five Years	Total
Fixed Rate Loans (1) (2)				
Commercial and industrial	$94,696	$156,331	$31,980	$283,007
Real estate:				
Commercial	187,761	396,882	46,390	631,033
Construction and land development	57,882	19,530	2,498	79,910
Residential	42,587	70,243	1,657	114,487
Consumer and other	3,362	2,136	—	5,498
Portfolio loans covered under FDIC loss share	68,076	80,767	11,587	160,430
Total	$454,364	$725,889	$94,112	$1,274,365
Variable Rate Loans (1)				
Commercial and industrial	$310,157	$142,079	$27,959	$480,195
Real estate:				
Commercial	66,414	98,938	15,185	180,537
Construction and land development	48,142	9,888	2,207	60,237
Residential	20,255	11,085	25,207	56,547
Consumer and other	5,397	226	—	5,623
Portfolio loans covered under FDIC loss share	53,508	39,965	46,707	140,180
Total	$503,873	$302,181	$117,265	$923,319
Loans (1) (2)				
Commercial and industrial	$404,853	$298,410	$59,939	$763,202
Real estate:				
Commercial	254,175	495,820	61,575	811,570
Construction and land development	106,024	29,418	4,705	140,147
Residential	62,842	81,328	26,864	171,034
Consumer and other	8,759	2,362	—	11,121
Portfolio loans covered under FDIC loss share	121,584	120,732	58,294	300,610
Total	$958,237	$1,028,070	$211,377	$2,197,684

(1) Loan balances include unearned loan (fees) costs, net.
(2) Not adjusted for impact of interest rate swap agreements.

Fixed rate loans comprise approximately 58% of the loan portfolio at December 31, 2011 and 61% at December 31, 2010. Variable rate loans are based on the prime rate or the London Interbank Offered Rate ("LIBOR"). The Bank's "prime rate" has been 4.00% since late 2008 when the Federal Reserve lowered the targeted Fed Funds rate to 0.25%. Some of the variable rate loans also use the "Wall Street Journal Prime Rate" which has been 3.25% since late 2008. Most loan originations have one to three year maturities. While the loan relationship has a much longer life, the shorter maturities allow the Company to revisit the underwriting and pricing on each relationship periodically. Management monitors this mix as part of its interest rate risk management. See "Interest Rate Risk" section.

Of the $254.2 million of commercial real estate loans maturing in one year or less, $154.6 million, or 61%, represents loans secured by non-owner occupied commercial properties.

37

Allowance for Loan Losses
The loan portfolio is the primary asset subject to credit risk. Credit risk is controlled and monitored through the use of lending standards, a thorough review of potential borrowers, and ongoing review of loan payment performance. Active asset quality administration, including early problem loan identification and timely resolution of problems, further ensures appropriate management of credit risk. Credit risk management for each loan type is discussed briefly in the section entitled “Loans.”

The allowance for loan losses represents management's estimate of an amount adequate to provide for probable credit losses in the loan portfolio at the balance sheet date. Various quantitative and qualitative factors are analyzed and provisions are made to the allowance for loan losses. Such provisions are reflected in our consolidated statements of income. The evaluation of the adequacy of the allowance for loan losses is based on management's ongoing review and grading of the loan portfolio, consideration of past loss experience, trends in past due and nonperforming loans, risk characteristics of the various classifications of loans, existing economic conditions, the fair value of underlying collateral, and other factors that could affect probable credit losses. Assessing these numerous factors involves significant judgment and could be significantly impacted by changes in economic conditions. Management considers the allowance for loan losses a critical accounting policy. See “Critical Accounting Policies” for more information.

In determining the allowance and the related provision for loan losses, three principal elements are considered:
1) specific allocations based upon probable losses identified during a quarterly review of the loan portfolio,
2) allocations based principally on the Company's risk rating formulas, and
3) a qualitative adjustment based on subjective factors.

The first element reflects management's estimate of probable losses based upon a systematic review of specific loans considered to be impaired. These estimates are based upon collateral exposure, if they are collateral dependent for collection. Otherwise, discounted cash flows are estimated and used to assign loss. At December 31, 2011 the allocated allowance for loan losses on individually impaired loans was $10.7 million, or 26% of the total impaired loans. At December 31, 2010, the allocated allowance for loan losses on individually impaired loans was $9.1 million, or 20% of the total impaired loans.

The second element reflects the application of our loan rating system. This rating system is similar to those employed by state and federal banking regulators. Loans are rated and assigned a loss allocation factor for each category that is based on a loss migration analysis using the Company's loss experience and heavily weighting the most recent 12 months. The higher the rating assigned to a loan, the greater the loss allocation percentage that is applied.

The qualitative adjustment is based on management's evaluation of conditions that are not directly reflected in the determination of the formula and specific allowances. The evaluation of the inherent loss with respect to these conditions is subject to a higher degree of uncertainty because they may not be identified with specific problem credits or portfolio segments. The conditions evaluated in connection with the qualitative adjustment include the following:
- general economic and business conditions affecting our markets;
- asset quality trends (including trends in nonperforming loans expected to result from existing conditions); and
- loan review findings.

Executive management reviews these conditions quarterly in discussion with our entire lending staff. To the extent that any of these conditions is evidenced by a specifically identifiable problem credit or portfolio segment as of the evaluation date, management's estimate of the effect of such conditions may be reflected as a specific allowance, applicable to such credit or portfolio segment. Where any of these conditions is not evidenced by a specifically identifiable problem credit or portfolio segment as of the evaluation date, management's evaluation of the probable loss related to such condition is reflected in the qualitative adjustment.

The allocation of the allowance for loan losses by loan category is a result of the analysis above. The allocation methodology applied by the Company, designed to assess the adequacy of the allowance for loan losses, focuses on changes in the size and character of the loan portfolio, changes in levels of impaired and other nonperforming loans, the risk inherent in specific loans, concentrations of loans to specific borrowers or industries, existing economic conditions, and historical losses on each portfolio category. Because each of the criteria used is subject to change, the allocation of the allowance for loan losses is made for analytical purposes and is not necessarily indicative of the trend of future loan losses in any particular loan category. The total allowance is available to absorb losses from any segment of the portfolio. Management continues to target and maintain the allowance for loan losses equal to the allocation methodology plus a qualitative adjustment, as determined by economic conditions and other qualitative and quantitative factors affecting the Company's borrowers, as described above.

For Covered loans, the Company re-measures contractual and expected cash flows on a quarterly basis. When the re-measurement process results in a decrease in expected cash flows, impairment is recorded as a provision for loan losses covered under FDIC loss share. As a result of impairment, the FDIC loss share receivable is increased to reflect future cash to be received from the FDIC. The amount of the increase is recorded in noninterest income and is determined based on the specific loss share agreement, but is generally 80% of the losses. At December 31, 2011, the allowance for loan losses includes $1.6 million for Covered loans.

Management believes that the allowance for loan losses is adequate at December 31, 2011.

In 2012, the Company expects similar levels of net chargeoffs, (excluding Covered loans), given the continued softness in real estate values and activities in our markets.

The following table summarizes changes in the allowance for loan losses arising from loans charged off and recoveries on loans previously charged off, by loan category, and additions to the allowance charged to expense.

	At December 31,				
(in thousands)	2011	2010	2009	2008	2007
Allowance at beginning of year, for loans not covered under FDIC loss share	$42,759	$42,995	$33,808	$22,585	$17,475
(Disposed) acquired allowance for loan losses	—	—	—	(50)	2,010
Release of allowance related to loan participations sold	—	—	(1,383)	—	—
Loans charged off:					
Commercial and industrial	5,488	3,865	3,663	3,783	238
Real estate:					
Commercial	2,429	15,482	5,710	1,384	43
Construction and land development	10,627	12,148	15,086	8,044	705
Residential	1,613	4,391	5,931	2,367	1,418
Consumer and other	5	274	42	31	125
Total loans charged off	20,162	36,160	30,432	15,609	2,529
Recoveries of loans previously charged off:					
Commercial and industrial	583	157	62	64	347
Real estate:					
Commercial	729	1,001	66	—	15
Construction and land development	415	314	28	241	25
Residential	303	536	422	56	17
Consumer and other	62	181	12	11	105
Total recoveries of loans	2,092	2,189	590	372	509
Net loan chargeoffs for loans not covered under FDIC loss share	18,070	33,971	29,842	15,237	2,020
Provision for loan losses not covered under FDIC loss share	13,300	33,735	40,412	26,510	5,120
Allowance at end of year, for loans not covered under FDIC loss share	$37,989	$42,759	$42,995	$33,808	$22,585
Allowance at beginning of year, for loans covered under FDIC loss share	$—	$—	$—	$—	$—
Loans charged off covered under FDIC loss share	1,168	—	—	—	—
Recoveries of loans covered under FDIC loss share	—	—	—	—	—
Net loan chargeoffs for loans covered under FDIC loss share	1,168	—	—	—	—
Provision for loan losses covered under FDIC loss share	2,803	—	—	—	—
Allowance at end of year, for loans covered under FDIC loss share	$1,635	$—	$—	$—	$—
Total Allowance at end of year	$39,624	$42,759	$42,995	$33,808	$22,585

Excludes loans covered under FDIC loss share					
Average loans	$1,819,536	$1,782,023	$2,097,028	$2,001,073	$1,599,596
Total portfolio loans	1,897,074	1,766,351	1,818,481	2,201,457	1,784,278
Net chargeoffs to average loans	0.99 %	1.91 %	1.42 %	0.76 %	0.13 %
Allowance for loan losses to loans	2.00	2.42	2.36	1.54	1.27
Includes loans covered under FDIC loss share					
Average loans	$2,051,899	$1,853,175	$2,098,272	$2,001,073	$1,599,596
Total portfolio loans	2,197,684	1,887,921	1,832,125	2,201,457	1,784,278
Net chargeoffs to average loans	0.94 %	1.83 %	1.42 %	0.76 %	0.13 %
Allowance for loan losses to loans	1.80	2.26	2.35	1.54	1.27

The following table is a summary of the allocation of the allowance for loan losses for the five years ended December 31, 2011:

	December 31, 2011			2010			2009			2008			2007		
(in thousands)	Allowance	Percent by Category to Total Loans		Allowance	Percent by Category to Total Loans		Allowance	Percent by Category to Total Loans		Allowance	Percent by Category to Total Loans		Allowance	Percent by Category to Total Loans	
Commercial and industrial	$11,945	34.7	%	$12,727	31.5	%	$9,715	30.2	%	$6,431	30.7	%	$4,582	30.8	%
Real estate:															
Commercial	13,048	36.9	%	10,689	41.1	%	19,600	44.7	%	11,085	40.3	%	7,229	40.4	%
Construction and land development	5,847	6.4	%	8,407	10.1	%	4,289	12.1	%	7,886	17.2	%	5,418	16.9	%
Residential	3,931	7.8	%	5,485	10.0	%	3,859	11.4	%	2,762	10.7	%	2,632	9.8	%
Consumer and other	14	0.5	%	93	0.9	%	45	0.9	%	188	1.1	%	438	2.1	%
Portfolio loans covered under FDIC loss share	1,635	13.7	%	—	6.4	%	—	0.7	%	—	—	%	—	—	%
Qualitative adjustment	3,204			5,358			5,487			5,456			2,286		
Total allowance	$39,624	100.0	%	$42,759	100.0	%	$42,995	100.0	%	$33,808	100.0	%	$22,585	100.0	%

Nonperforming assets

Nonperforming loans are defined as loans on non-accrual status, loans 90 days or more past due but still accruing, and restructured loans that are still accruing interest or in a non-accrual status. Restructured loans involve the granting of a concession to a borrower experiencing financial difficulty involving the modification of terms of the loan, such as changes in payment schedule or interest rate. Nonperforming assets include nonperforming loans plus foreclosed real estate.

Nonperforming loans exclude credit-impaired loans acquired in FDIC-assisted transactions. These purchased credit-impaired loans are accounted for on a pool basis, and the pools are considered to be performing. See Item 8, Note 6 - Portfolio Loans for more information on these loans.

Loans are placed on non-accrual status when contractually past due 90 days or more as to interest or principal payments. Additionally, whenever management becomes aware of facts or circumstances that may adversely impact the collectibility of principal or interest on loans, it is management's practice to place such loans on non-accrual status immediately, rather than delaying such action until the loans become 90 days past due. Previously accrued and uncollected interest on such loans is reversed. Income is recorded only to the extent that a determination has been made that the principal balance of the loan is collectable and the interest payments are subsequently received in cash, or for a restructured loan, the borrower has made six consecutive contractual payments. If collectability of the principal is in doubt, payments received are applied to loan principal.

Loans past due 90 days or more but still accruing interest are also included in nonperforming loans. Loans past due 90 days or more but still accruing are classified as such where the underlying loans are both well secured (the collateral value is sufficient to cover principal and accrued interest) and are in the process of collection.

The Company's nonperforming loans meet the definition of “impaired loans” in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”). As of December 31, 2011, 2010, and 2009, the Company had 41, 43, and 39 impaired loan relationships, respectively.

The following table presents the categories of nonperforming assets and certain ratios as of the dates indicated:

	December 31,									
(in thousands)	2011		2010		2009		2008		2007	
Non-accrual loans	$30,885		$38,477		$37,441		$35,487		$12,720	
Loans past due 90 days or more and still accruing interest	755		—		—		—		—	
Restructured loans	9,982		7,880		1,099		—		—	
Total nonperforming loans	41,622		46,357		38,540		35,487		12,720	
Foreclosed property (1)	17,217		25,373		22,918		13,868		2,963	
Other bank owned assets	—		850		—		—		—	
Total nonperforming assets (1)	$58,839		$72,580		$61,458		$49,355		$15,683	
Excludes assets covered under FDIC loss share										
Total assets	$3,377,779		$2,800,199		$2,365,655		$2,493,767		$2,141,329	
Total portfolio loans	1,897,074		1,766,351		1,818,481		2,201,457		1,784,278	
Total loans plus foreclosed property	1,914,291		1,792,574		1,841,399		2,215,325		1,787,241	
Nonperforming loans to total loans	2.19	%	2.62	%	2.12	%	1.61	%	0.71	%
Nonperforming assets to total loans plus foreclosed property	3.07		4.05		3.34		2.23		0.88	
Nonperforming assets to total assets (1)	1.74		2.59		2.60		1.98		0.73	
Includes assets covered under FDIC loss share										
Total assets	$3,377,779		$2,800,199		$2,365,655		$2,493,767		$2,141,329	
Total portfolio loans	2,197,684		1,887,921		1,832,125		2,201,457		1,784,278	
Total loans plus foreclosed property	2,251,372		1,924,979		1,857,209		2,215,325		1,787,241	
Nonperforming loans to total loans	1.89	%	2.46	%	2.10	%	1.61	%	0.71	%
Nonperforming assets to total loans plus foreclosed property	4.23		4.33		3.43		2.23		0.88	
Nonperforming assets to total assets	2.82		2.98		2.69		1.98		0.73	
Allowance for loan losses to nonperforming loans	95.00	%	92.00	%	112.00	%	95.00	%	178.00	%

(1) Excludes assets covered under FDIC shared-loss agreements, except for their inclusion in total assets

Nonperforming loans

Nonperforming loans at December 31, 2011 and 2010 based on Call Report codes were as follows:

(in thousands)	2011	2010
Construction, Real Estate/Land Acquisition and Development	$14,767	$9,934
Commercial Real Estate - Investor Owned	11,127	10,935
Commercial Real Estate - Owner Occupied	4,572	2,024
Residential Real Estate	5,522	12,188
Commercial & Industrial	5,634	11,276
Consumer & Other	—	—
Total	$41,622	$46,357

The following table summarizes the changes in nonperforming loans by quarter for 2011 and 2010.

	2011				
(in thousands)	4th Qtr	3rd Qtr	2nd Qtr	1st Qtr	Total year
Nonperforming loans beginning of period	$48,038	$43,118	$43,487	$46,357	$46,357
Additions to nonaccrual loans	7,276	14,618	6,204	18,187	46,285
Additions to restructured loans	3,803	2,314	2,508	297	8,922
Chargeoffs	(5,558)	(4,959)	(5,679)	(3,966)	(20,162)
Other principal reductions	(7,545)	(3,372)	(3,992)	(6,445)	(21,354)
Moved to Other real estate	(1,203)	(2,932)	(159)	(7,014)	(11,308)
Moved to performing	(3,944)	—	—	(3,929)	(7,873)
Loans past due 90 days or more and still accruing interest	755	(749)	749	—	755
Nonperforming loans end of period	$41,622	$48,038	$43,118	$43,487	$41,622

	2010				
(in thousands)	4th Qtr	3rd Qtr	2nd Qtr	1st Qtr	Total Year
Nonperforming loans beginning of period	$51,955	$46,550	$55,785	$38,540	$38,540
Additions to nonaccrual loans	15,877	19,373	15,440	39,663	90,353
Additions to restructured loans	3,430	2,286	454	611	6,781
Chargeoffs	(7,860)	(7,023)	(8,314)	(12,963)	(36,160)
Other principal reductions	(7,288)	(1,881)	(4,580)	(2,739)	(16,488)
Moved to Other real estate	(8,743)	(7,122)	(11,350)	(5,564)	(32,779)
Moved to Other bank owned assets	—	—	—	(955)	(955)
Moved to performing	(1,014)	(228)	—	(1,693)	(2,935)
Loans past due 90 days or more and still accruing interest	—	—	(885)	885	—
Nonperforming loans end of period	$46,357	$51,955	$46,550	$55,785	$46,357

At December 31, 2011, the nonperforming loans represent 41 relationships. The largest of these is a $4.5 million commercial real estate loan. Five relationships comprise 44% of the nonperforming loans. Approximately 52% of the nonperforming loans were in the St. Louis market, 47% were in the Kansas City market and 1% in the Phoenix market.

At December 31, 2010, the nonperforming loans represent 43 relationships. The largest of these is a $4.1 million commercial real estate loan. Five relationships comprise 45% of the nonperforming loans. Approximately 57% of the nonperforming loans were in the St. Louis market and 43% were in the Kansas City market.

At December 31, 2009, the nonperforming loans represent 39 relationships. The largest of these is a $4.0 million commercial real estate loan. Five relationships comprise 41% of the nonperforming loans. Approximately 52% of the nonperforming loans were in the Kansas City market, 47% were in the St. Louis market and less than 1% were in the Phoenix market.

At December 31, 2008, of the total nonperforming loans, $23.6 million, or 67%, related to five relationships: $10.6 million secured by a partially completed retail center; $3.5 million secured by commercial ground; $4.7 million secured by a medical office building; $2.8 million secured by a single family residence; and $1.9 million secured by a residential development. The remaining nonperforming loans consisted of 20 relationships. Eighty-four percent of the total nonperforming loans are located in the Kansas City market.

At December 31, 2007, of the total nonperforming loans, $7.3 million, or 57%, were related to eight residential homebuilders in St. Louis and Kansas City. The two largest related to a residential builder in Kansas City totaling $2.2 million and a single-family rehab builder in Kansas City totaling $1.6 million. The remaining nonperforming loans consisted of 11 relationships, nearly all of which were related to the soft residential housing markets in St. Louis and Kansas City.

In 2012, the Company expects similar or lower levels of new Non-covered, nonperforming loans compared to 2011, thereby continuing a trend from 2010.

Other real estate

Other real estate at December 31, 2011 was $53.7 million, an increase of $17.5 million over 2010. Approximately $36.5 million, or 68% of total Other real estate, is covered by an FDIC shared-loss agreement. At December 31, 2011, Other real estate represented 100 properties. The largest single component of Other real estate is commercial ground with a book value of $3.6 million that is covered under FDIC loss share. Thirteen properties comprise 50% of the Other real estate. At December 31, 2011, Other real estate was comprised of 14% residential lots, 6% completed homes, and 80% commercial real estate. Of the total Other real estate, approximately 44%, or 42 properties, are located in the Kansas City region, 26%, or 17 properties, are located in the St. Louis region and 30%, or 39 properties, are located in the Arizona region. All Arizona Other real estate and 31 properties or $20.2 million, of the Kansas City Other real estate are covered under FDIC loss share.

The following table summarizes the changes in Other real estate by quarter for 2011 and 2010.

	2011				
(in thousands)	4th Qtr	3rd Qtr	2nd Qtr	1st Qtr	Total Year
Other real estate beginning of period	$72,563	$42,790	$51,305	$36,208	$36,208
Additions and expenses capitalized to prepare property for sale	1,203	2,932	159	7,014	11,308
Additions from FDIC assisted transactions	1,250	41,793	3,298	12,826	59,167
Writedowns in fair value	(1,998)	(2,714)	(2,944)	(703)	(8,359)
Sales	(19,330)	(12,238)	(9,028)	(4,040)	(44,636)
Other real estate end of period	$53,688	$72,563	$42,790	$51,305	$53,688

	2010				
(in thousands)	4th Qtr	3rd Qtr	2nd Qtr	1st Qtr	Total Year
Other real estate beginning of period	$34,685	$25,884	$20,947	$25,084	$25,084
Additions and expenses capitalized to prepare property for sale	8,743	7,122	11,350	5,564	32,779
Additions from FDIC assisted transactions	4,871	5,469	—	113	10,453
Writedowns in fair value	(2,406)	(1,750)	(1,364)	(574)	(6,094)
Sales	(9,685)	(2,040)	(5,049)	(9,240)	(26,014)
Other real estate end of period	$36,208	$34,685	$25,884	$20,947	$36,208

The writedowns in fair value were recorded in Loan legal and other real estate expense based on current market activity shown in the appraisals. In 2011, the Company realized a net gain of $862,000 on the sale of other real estate and recorded these gains as part of Noninterest income. Management believes it is prudent to sell these properties, rather than wait for an improved real estate market.

Potential problem loans

Potential problem loans, which are not included in nonperforming loans, amounted to approximately $60.6 million, or 3.19% of total Non-covered loans outstanding at December 31, 2011, compared to $85.4 million, or 4.83% of total Non-covered loans outstanding at December 31, 2010. Potential problem loans represent those loans where payment of principal and interest is up-to-date and the loans are therefore, fully performing, but where some doubts exist as to the borrower's ability to continue to comply with present repayment terms. Given this level of potential problem loans and continued softness in the local real estate markets, combined with the Company's demonstrated ability to work through this adverse credit cycle to-date, we believe the dollar levels of the nonperforming assets, excluding Covered loans, will be flat in 2012 compared to 2011.

Investments
At December 31, 2011, our portfolio of Securities available for sale was $593.2 million, or 18%, of total assets. This portfolio is primarily comprised of residential mortgage-based securities and obligations of U.S. government sponsored enterprises. The size of the investment portfolio is generally 5 to 20% of total assets and will vary within that range based on liquidity. Typically, management classifies securities as available for sale to maximize management flexibility, although securities may be purchased with the intention of holding to maturity. Securities available-for-sale are carried at fair value, with related unrealized gains or losses, net of deferred income taxes, recorded as an adjustment to equity capital.

Our Other investments, at cost primarily consist of the FHLB capital stock, common stock investments related to our trust preferred securities and other private equity investments. At December 31, 2011, of the $ 9.6 million in FHLB capital stock, $3.4 million is required for FHLB membership and $4.6 million is required to support our outstanding advances. Historically, it has been the FHLB's practice to automatically repurchase activity-based stock that became excess because of a member's reduction in advances. The FHLB has the discretion, but is not required, to repurchase any shares that a member is not required to hold.

The table below sets forth the carrying value of investment securities held by the Company at the dates indicated:

	December 31,								
	2011			2010			2009		
(in thousands)	Amount	%		Amount	%		Amount	%	
Obligations of U.S. Government agencies	$—	—	%	$453	0.1	%	27,189	9.2	%
Obligations of U.S. Government sponsored enterprises	126,917	20.9	%	32,119	8.6	%	75,814	25.6	%
Obligations of states and political subdivisions	39,837	6.6	%	17,676	4.7	%	3,408	1.2	%
Residential mortgage-backed securities	426,428	70.1	%	311,298	83.4	%	176,050	59.5	%
FHLB capital stock	9,588	1.6	%	7,633	2.0	%	8,476	2.9	%
Other investments	4,938	0.8	%	4,645	1.2	%	4,713	1.6	%
Total	$607,708	100.0	%	$373,824	100.0	%	$295,650	100.0	%

In 2011, the portfolio grew with additions to the mortgage backed securities, including collateralized mortgage obligations, government sponsored agency debentures, and federally tax free municipal securities. All residential mortgage-backed securities were issued by government sponsored enterprises.

The Company had no securities classified as trading at December 31, 2011, 2010, or 2009.

The following table summarizes expected maturity and tax equivalent yield information on the investment portfolio at December 31, 2011:

	Within 1 year		1 to 5 years		5 to 10 years		Over 10 years		No Stated Maturity		Total	
(in thousands)	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Obligations of U.S. Government sponsored enterprises	2,007	0.46%	69,197	1.38%	55,713	1.58%	—	— %	—	— %	126,917	1.45%
Obligations of states and political	1,026	4.59%	10,644	4.07%	23,979	4.59%	4,188	1.84%	—	— %	39,837	4.16%

subdivisions												
Residential mortgage-backed securities	20,547	0.59%	334,745	2.04%	37,777	2.08%	33,359	1.35%	—	— %	426,428	1.92%
FHLB capital stock	—	— %	—	— %	—	— %	—	— %	9,588	2.30%	9,588	2.30%
Other investments	—	— %	—	— %	—	— %	—	— %	4,938	2.98%	4,938	2.98%
Total	$23,580	0.75%	$414,586	1.98%	$117,469	2.35%	$37,547	1.40%	$14,526	2.53%	$607,708	1.98%

Yields on tax-exempt securities are computed on a taxable equivalent basis using a tax rate of 36%. Expected maturities will differ from contractual maturities, as borrowers may have the right to call or repay obligations with or without prepayment penalties.

Deposits

The following table shows, for the periods indicated, the average annual amount and the average rate paid by type of deposit:

(in thousands)	For the year ended December 31, 2011 Average balance	Weighted average rate		2010 Average balance	Weighted average rate		2009 Average balance	Weighted average rate	
Interest-bearing transaction accounts	$212,257	0.38	%	$190,275	0.45	%	$122,563	0.54	%
Money market accounts	997,415	0.80	%	701,360	0.89	%	636,350	0.96	%
Savings accounts	27,106	0.41	%	10,022	0.35	%	9,147	0.38	%
Certificates of deposit	847,057	1.50	%	784,369	2.01	%	786,631	2.98	%
	2,083,835	1.04	%	1,686,026	1.36	%	1,554,691	1.94	%
Noninterest-bearing demand deposits	494,609	—	%	305,887	—	%	250,435	—	%
	$2,578,444	0.84	%	$1,991,913	1.15	%	$1,805,126	1.67	%

The Bank achieved several deposit related goals in 2011 including strong growth in core relationships, an improvement in the overall mix and a reduction in broker related funds. The year over year increase in deposits was largely comprised of noninterest-bearing demand deposits and money market and savings accounts with higher cost certificates of deposit declining during the year. Strong direct selling efforts, primarily by the commercial banking group coupled with the FNBO acquisition, drove the deposit growth. As deposit rates continued to decline, the Bank positioned its pricing strategy to favor adjustable rate transaction accounts over longer term time deposits. The result was to lower the percentage of time deposits and better position the bank for a prolonged low rate cycle. The Company also undertook an initiative to significantly reduce its reliance on broker funds.

The Company offers a broad range of Treasury Management products and services that benefit businesses ranging from large national clients to the smallest local merchants. Customized solutions and special product bundles are available to clients of all sizes. Responding to ever increasing needs for tightened security and improved functional efficiency, the Company successfully migrated to a new on-line banking platform in 2011. Other recent Treasury enhancements include new mobile technology to improve on-line security and mobile applications for remote deposit and merchant credit card processing.

The FNB acquisition added $423.1 million in deposits in the third quarter of 2011. These deposits included $66.9 million in noninterest-bearing demand deposits, $123.6 million in money market and other interest-bearing transaction accounts, and $232.6 million in certificates of deposit.

Brokered certificates of deposits were $126.6 million at December 31, 2011, a decrease of $30.1 million, or 19% compared to December 31, 2010. For the year ended December 31, 2011, brokered certificates of deposits represented 5% of total deposits compared to 7% for the year ended December 31, 2010. Noninterest-bearing demand deposits represented 21% of total deposits at December 31, 2011 compared to 16% at December 31, 2010.

Maturities of certificates of deposit of $100,000 or more were as follows as of December 31, 2011:

(in thousands)	Total
Three months or less	$95,405
Over three through six months	62,362
Over six through twelve months	120,559
Over twelve months	272,209
Total	$550,535

Liquidity and Capital Resources

Liquidity
The objective of liquidity management is to ensure we have the ability to generate sufficient cash or cash equivalents in a timely and cost-effective manner to meet our commitments as they become due. Typical demands on liquidity are run-off from demand deposits, maturing time deposits which are not renewed, and fundings under credit commitments to customers. Funds are available from a number of sources, such as from the core deposit base and from loans and securities repayments and maturities. Additionally, liquidity is provided from sales of the securities portfolio, fed fund lines with correspondent banks, the Federal Reserve and the FHLB, the ability to acquire large and brokered deposits and the ability to sell loan participations to other banks. These alternatives are an important part of our liquidity plan and provide flexibility and efficient execution of the asset-liability management strategy.

Our Asset-Liability Management Committee oversees our liquidity position, the parameters of which are approved by the Board of Directors. Our liquidity position is monitored monthly by producing a liquidity report, which measures the amount of liquid versus non-liquid assets and liabilities. Our liquidity management framework includes measurement of several key elements, such as the loan to deposit ratio, a liquidity ratio, and a dependency ratio. The Company's liquidity framework also incorporates contingency planning to assess the nature and volatility of funding sources and to determine alternatives to these sources. While core deposits and loan and investment repayments are principal sources of liquidity, funding diversification is another key element of liquidity management and is achieved by strategically varying depositor types, terms, funding markets, and instruments.

For the year ended December 31, 2011, net cash provided by operating activities was $22.1 million less than for 2010. Net cash used in investing activities was $0.4 million for 2011 versus $287.9 million in 2010. The higher net cash used in investing activities in 2010 was primarily due to the asset acquisition of Home National. Net cash used in financing activities was $133.1 million in 2011 versus net cash provided by financing activities of $425.4 million in 2010. The change in cash provided by financing activities was primarily due to a decrease in certificates of deposit (net of acquired balances).

Strong capital ratios, credit quality and core earnings are essential to retaining cost-effective access to the wholesale funding markets. Deterioration in any of these factors could have a negative impact on the Company's ability to access these funding sources and, as a result, these factors are monitored on an ongoing basis as part of the liquidity management process. The Bank is subject to regulations and, among other things, may be limited in its ability to pay dividends or transfer funds to the parent company. Accordingly, consolidated cash flows as presented in the consolidated statements of cash flows may not represent cash immediately available for the payment of cash dividends to the Company's shareholders or for other cash needs.

Parent Company liquidity
The parent company's liquidity is managed to provide the funds necessary to pay dividends to shareholders, service debt, invest in subsidiaries as necessary, and satisfy other operating requirements. The parent company had cash and cash equivalents of $21.2 million and $15.4 million, respectively, at December 31, 2011 and 2010. The parent

company's primary funding sources to meet its liquidity requirements are dividends and payments from the Bank and proceeds from the issuance of equity. We believe our current level of cash at the parent company will be sufficient to meet all projected ongoing cash needs in 2012.

Another source of funding for the parent company includes the issuance of subordinated debentures. As of December 31, 2011, the parent company had $82.6 million of outstanding subordinated debentures as part of nine Trust Preferred Securities Pools. These securities are classified as debt but are included in regulatory capital and the related interest expense is tax-deductible, which makes them a very attractive source of funding. See Item 8, Note 11 - Subordinated Debentures for more information.

Bank liquidity

The Bank has a variety of funding sources available to increase financial flexibility. In addition to amounts currently borrowed at December 31, 2011, the Bank could borrow an additional $139.4 million from the FHLB of Des Moines under blanket loan pledges and has an additional $379.6 million available from the Federal Reserve Bank under a pledged loan agreement. The Bank has unsecured federal funds lines with three correspondent banks totaling $35.0 million.

Investment securities are another important tool to the Bank's liquidity objectives. As of December 31, 2011, the entire investment portfolio was available for sale. Of the $593.2 million investment portfolio available for sale, $287.8 million was pledged as collateral for depository client repurchase agreements, public deposits, treasury, tax and loan notes, and other requirements. The remaining $305.4 million could be pledged or sold to enhance liquidity, if necessary.

The Bank participates in the Certificate of Deposit Account Registry Service, or CDARS, which allows us to provide our customers with access to additional levels of FDIC insurance coverage. The CDARS program is designed to provide full FDIC insurance on deposit amounts larger than the stated maximum by exchanging or reciprocating larger depository relationships with other member banks. Our depositors' funds are broken into smaller amounts and placed with other banks that are members of the network. Each member bank issues CDs in amounts that are eligible for FDIC insurance. CDARS are considered brokered deposits according to banking regulations; however, the Company considers the reciprocal deposits placed through the CDARS program as core funding and does not report the balances as brokered sources in its external financial reports. The Bank must remain “well-capitalized” in order to utilize the CDARS program. At December 31, 2011, the Bank had $14.5 million of reciprocal CDARS deposits outstanding compared to $160.5 million outstanding at December 31, 2010. At December 31, 2011, the Bank also had $53.2 million of reciprocal money market accounts through CDARS.

In addition to the reciprocal deposits available through CDARS, we also have access to the “one-way buy” program, which allows us to bid on the excess deposits of other CDARS member banks. The Company will report any outstanding “one-way buy” funds as brokered funds in its internal and external financial reports. At December 31, 2011, we had no outstanding “one-way buy” deposits.

As long as the Bank remains “well-capitalized”, we have the ability to sell certificates of deposit through various national or regional brokerage firms, if needed. At December 31, 2011, brokered certificate of deposit balances were $126.6 million, and represented 5% of total deposits at December 31, 2011.

Over the normal course of business, the Bank enters into certain forms of off-balance sheet transactions, including unfunded loan commitments and letters of credit. These transactions are managed through the Bank's various risk management processes. Management considers both on-balance sheet and off-balance sheet transactions in its evaluation of the Company's liquidity. The Bank has $591.6 million in unused commitments as of December 31, 2011, including $43.2 million that are covered under FDIC loss share. While this commitment level would be very difficult to fund given the Bank's current liquidity resources, the nature of these commitments is such that the likelihood of funding them is very low.

At December 31, 2011 and 2010, approximately $16.6 million and $9.6 million, respectively, of cash and due from banks represented required reserves on deposits maintained by the Bank in accordance with Federal Reserve Bank requirements.

Capital Resources

On January 25, 2010, we completed the sale of 1,931,610 shares, or $15.0 million, of our common stock in a private placement offering. In the first quarter of 2010, the proceeds of the offering were injected into the Bank to further strengthen the Bank's capital position. On May 24, 2011, we issued 2,743,900 shares, or $35.0 million in common stock through a public offering. The shares in the offering were issued pursuant to a prospectus supplement filed with the Securities and Exchange Commission as part of the Company's effective registration statement. The net proceeds to the Company, after deducting underwriting discounts and commissions and offering expenses, was approximately $32.6 million. At June 30, 2011, approximately $20.0 million of the offering proceeds were injected into the Bank to support expected growth.

As a financial holding company, the Company is subject to “risk-based” capital adequacy guidelines established by the Federal Reserve. Risk-based capital guidelines were designed to relate regulatory capital requirements to the risk profile of the specific institution and to provide for uniform requirements among the various regulators. Currently, the risk-based capital guidelines require the Company to meet a minimum total capital ratio of 8.0% of which at least 4.0% must consist of Tier 1 capital. Tier 1 capital consists of (a) common shareholders' equity (excluding the unrealized market value adjustments on the available-for-sale securities and cash flow hedges), (b) qualifying perpetual preferred stock and related additional paid in capital subject to certain limitations specified by the FDIC, (c) qualifying trust preferred securities, subject to certain limitations specified by the FDIC, and (d) minority interests in the equity accounts of consolidated subsidiaries less (e) goodwill, (f) mortgage servicing rights within certain limits, and (g) certain other intangible assets and investments in subsidiaries. The FDIC also requires a minimum leverage ratio of 3.0%, defined as the ratio of Tier 1 capital to average total assets for banking organizations deemed the strongest and most highly rated by banking regulators. A higher minimum leverage ratio is required of less highly rated banking organizations. Total capital, a measure of capital adequacy, includes Tier 1 capital, allowance for loan losses, and portions of subordinated debentures not eligible for Tier 1 treatment.

The Bank met the definition of “well-capitalized” (the highest category) at December 31, 2011, 2010, and 2009.

The following table summarizes the Company's risk-based capital, tangible common and leverage ratios at the dates indicated:

	At December 31,					
(Dollars in thousands)	2011		2010		2009	
Average common equity to average assets	5.84	%	5.97	%	5.93	%
Tier 1 capital to risk weighted assets	12.40	%	11.73	%	10.67	%
Total capital to risk weighted assets	13.78	%	14.11	%	13.32	%
Tier 1 common equity to risk weighted assets	7.32	%	7.16	%	6.33	%
Leverage ratio (Tier 1 capital to average assets)	8.26	%	8.99	%	8.96	%
Tangible common equity to tangible assets	4.99	%	5.15	%	5.44	%
Tier 1 capital	$276,275		$237,099		$215,099	
Total risk-based capital	$306,996		$285,226		$268,458	

Below are reconciliation's of Tier 1 common equity to risk weighted assets and shareholders' equity to tangible common equity and total assets to tangible assets. These ratios are widely followed by analysts of bank and financial holding companies and management believes they are an important financial measure of capital strength even though they are considered to be non-GAAP measures.

	For the years ended December 31,		
(In thousands)	2011	2010	2009
Shareholders' equity	$239,565	$179,801	$163,912
Less: Goodwill	(30,334)	(2,064)	(2,064)
Less: Intangible assets	(9,285)	(1,223)	(1,643)
Less: Unrealized gains; Plus: Unrealized losses	(3,602)	573	(933)
Plus: Qualifying trust preferred securities	79,874	59,953	55,768
Other	57	59	59
Tier 1 capital	$276,275	$237,099	$215,099
Less: Preferred stock	(33,293)	(32,519)	(31,802)
Less: Qualifying trust preferred securities	(79,874)	(59,953)	(55,768)
Tier 1 common equity	$163,108	$144,627	$127,529
Total risk weighted assets determined in accordance with prescribed regulatory requirements	$2,227,958	$2,021,136	$2,015,390
Tier 1 common equity to risk weighted assets	7.32%	7.16%	6.33%

	For the years ended December 31,		
(In thousands)	2011	2010	2009
Total shareholders' equity	$239,565	$179,801	$163,912
Less: Preferred stock	(33,293)	(32,519)	(31,802)
Less: Goodwill	(30,334)	(2,064)	(2,064)
Less: Intangible assets	(9,285)	(1,223)	(1,643)
Tangible common equity	$166,653	$143,995	$128,404
Total assets	$3,377,779	$2,800,199	$2,365,655
Less: Goodwill	(30,334)	(2,064)	(2,064)
Less: Intangible assets	(9,285)	(1,223)	(1,643)
Tangible assets	$3,338,160	$2,796,912	$2,361,948
Tangible common equity to tangible assets	4.99%	5.15%	5.44%

Risk Management

Market risk arises from exposure to changes in interest rates and other relevant market rate or price risk. The Company faces market risk in the form of interest rate risk through transactions other than trading activities. Market risk from these activities, in the form of interest rate risk, is measured and managed through a number of methods. The Company uses financial modeling techniques to measure interest rate risk. These techniques measure the sensitivity of future earnings due to changing interest rate environments. Guidelines established by the Bank's Asset/Liability Management Committee and approved by the Bank's Board of Directors are used to monitor exposure of earnings at risk. General interest rate movements are used to develop sensitivity as the Company feels it has no primary exposure to a specific point on the yield curve. These limits are based on the Company's exposure to a 100 basis points and 200 basis points immediate and sustained parallel rate move, either upward or downward. In today's low interest rate environment, the Company also monitors its exposure to immediate and sustained parallel rate increases of 300 basis points and 400 basis points.

50

Interest Rate Risk

Our interest rate sensitivity management seeks to avoid fluctuating interest margins to provide for consistent growth of net interest income through periods of changing interest rates. Interest rate sensitivity varies with different types of interest-earning assets and interest-bearing liabilities. We attempt to maintain interest-earning assets, comprised primarily of both loans and investments, and interest-bearing liabilities, comprised primarily of deposits, maturing or repricing in similar time horizons in order to minimize or eliminate any impact from market interest rate changes. In order to measure earnings sensitivity to changing rates, the Company uses a static GAP analysis and earnings simulation model.

The static GAP analysis starts with contractual repricing information for assets, liabilities, and off-balance sheet instruments. These items are then combined with repricing estimations for administered rate (interest-bearing demand deposits, savings, and money market accounts) and non-rate related products (demand deposit accounts, other assets, and other liabilities) to create a baseline repricing balance sheet. In addition, mortgage-backed securities are adjusted based on industry estimates of prepayment speeds.

The following table represents the estimated interest rate sensitivity and periodic and cumulative GAP positions calculated as of December 31, 2011. Significant assumptions used for this table include: loans will repay their contractual repayment schedule; interest-bearing demand accounts and savings accounts are interest sensitive due to immediate repricing, and fixed maturity deposits will not be withdrawn prior to maturity. A significant variance in actual results from one or more of these assumptions could materially affect the results reflected in the table.

(in thousands)	Year 1	Year 2	Year 3	Year 4	Year 5	Beyond 5 years or no stated maturity	Total
Interest-Earning Assets							
Securities available for sale	$196,023	$74,568	$58,823	$35,722	$94,231	$133,815	$593,182
Other investments	—	—	—	—	—	14,527	14,527
Interest-bearing deposits	168,711	—	—	—	—	—	168,711
Federal funds sold	143	—	—	—	—	—	143
Portfolio loans (1)	1,474,205	410,770	164,660	72,723	48,288	27,038	2,197,684
Loans held for sale	6,494	—	—	—	—	—	6,494
Total interest-earning assets	$1,845,576	$485,338	$223,483	$108,445	$142,519	$175,380	$2,980,741
Interest-Bearing Liabilities							
Savings, NOW and Money market deposits	$1,388,953	$—	$—	$—	$—	$—	$1,388,953
Certificates of deposit	430,223	173,680	46,563	97,748	68,647	60	816,921
Subordinated debentures	56,807	28,274	—	—	—	—	85,081
Other borrowings	176,545	—	—	10,000	—	70,000	256,545
Total interest-bearing liabilities	$2,052,528	$201,954	$46,563	$107,748	$68,647	$70,060	$2,547,500
Interest-sensitivity GAP							
GAP by period	$(206,952)	$283,384	$176,920	$697	$73,872	$105,320	$433,241
Cumulative GAP	$(206,952)	$76,432	$253,352	$254,049	$327,921	$433,241	$433,241
Ratio of interest-earning assets to interest-bearing liabilities							

Periodic	0.90	2.40	4.80	1.01	2.08	2.50	1.17
Cumulative GAP as of December 31, 2011	0.90	1.03	1.11	1.11	1.13	1.17	1.17

(1) Adjusted for the impact of the interest rate swaps.

51

At December 31, 2011, the Company was asset sensitive for all periods, except Year 1, based on repricing characteristics. Asset sensitive means that assets will reprice faster than liabilities.

Along with the static GAP analysis, the Company determines the sensitivity of its short-term future earnings to a hypothetical plus or minus 100 and 200 basis point parallel rate shock through the use of simulation modeling. In addition to the assumptions used to create the static GAP, simulation of earnings includes the modeling of the balance sheet as an ongoing entity. Future business assumptions involving administered rate products, prepayments for future rate-sensitive balances, and the reinvestment of maturing assets and liabilities are included. These items are then modeled to project net interest income based on a hypothetical change in interest rates. The resulting net interest income for the next 12-month period is compared to the net interest income amount calculated using flat rates. This difference represents the Company's earnings sensitivity to a plus or minus 100 basis points parallel rate shock.

The resulting simulations for December 31, 2011 demonstrated that the Company's balance sheet was relatively neutral to interest rate changes. The simulations projected that the annual net interest income of the Bank would increase by approximately 0.01% if rates increased by 100 basis points under a parallel rate shock and 1.3% if rates increased 300 basis points. The increase in interest income from short term assets would be offset by higher rates on deposits and re-issuance of maturing debt. The simulations also indicate that net interest income would increase during the second year by 1.3% under a 100 basis point parallel rate shock and 6.6% under a 300 basis point rate shock. The Company also performs rate shock simulations for declining interest rates, however, given the very low level of short term interest rates, the falling interest rate shock simulations are considered irrelevant.

The Company occasionally uses interest rate derivative financial instruments as an asset/liability management tool to hedge mismatches in interest rate exposure indicated by the net interest income simulation described above. They are used to modify the Company's exposures to interest rate fluctuations and provide more stable spreads between loan yields and the rate on their funding sources. At December 31, 2011, the Company had $65.1 million and $80.1 million in notional amount of outstanding interest rate swaps and caps, respectively, to help manage interest rate risk. Derivative financial instruments are also discussed in Item 8, Note 7 - Derivative Financial Instruments.

Contractual Obligations, Off-Balance Sheet Risk, and Contingent Liabilities

Through the normal course of operations, the Company has entered into certain contractual obligations and other commitments. Such obligations relate to funding of operations through deposits or debt issuances, as well as leases for premises and equipment. As a financial services provider, the Company routinely enters into commitments to extend credit. While contractual obligations represent future cash requirements of the Company, a significant portion of commitments to extend credit may expire without being drawn upon. Such commitments are subject to the same credit policies and approval process accorded to loans made by the Company.

The required contractual obligations and other commitments, excluding any contractual interest(1), at December 31, 2011 were as follows:

(in thousands)	Total	Less Than 1 Year	Over 1 Year Less than 5 Years	Over 5 Years
Operating leases	$20,705	$2,419	$8,436	$9,850
Certificates of deposit	816,921	431,361	385,500	60
Subordinated debentures	85,081	—	—	85,081
Federal Home Loan Bank advances	102,000	22,000	10,000	70,000
Commitments to extend credit	547,657	413,063	112,989	21,605
Standby letters of credit	43,973	43,973	—	—

Private equity funds	1,823	—	1,823	—

(1) In the banking industry, interest-bearing obligations are principally utilized to fund interest-earning assets. As such, interest charges on related contractual obligations were excluded from reported amounts as the potential

52

cash outflows would have corresponding cash inflows from interest-earning assets.

As of December 31, 2011, we had liabilities associated with uncertain tax positions of $1.1 million. The table above does not include these liabilities due to the high degree of uncertainty regarding the future cash flows associated with these amounts.

The Company also enters into derivative contracts under which the Company either receives cash from or pays cash to counterparties depending on changes in interest rates. Derivative contracts are carried at fair value on the consolidated balance sheet with the fair value representing the net present value of expected future cash receipts or payments based on market interest rates as of the balance sheet date. The fair value of these contracts changes daily as market interest rates change. Derivative liabilities are not included as contractual cash obligations as their fair value does not represent the amounts that may ultimately be paid under these contracts.

As discussed in Item 8, Note 14 - Litigation and Other Claims and Item 3 - Legal Proceedings, the Company faces risks of litigation. See Note 14 for a description of such litigation and the possible effects on our business.

CRITICAL ACCOUNTING POLICIES

The following accounting policies are considered most critical to the understanding of the Company's financial condition and results of operations. These critical accounting policies require management's most difficult, subjective and complex judgments about matters that are inherently uncertain. Because these estimates and judgments are based on current circumstances, they may change over time or prove to be inaccurate based on actual experiences. In the event that different assumptions or conditions were to prevail, and depending upon the severity of such changes, the possibility of a materially different financial condition and/or results of operations could reasonably be expected. The impact and any associated risks related to our critical accounting policies on our business operations are discussed throughout “Management's Discussion and Analysis of Financial Condition and Results of Operations,” where such policies affect our reported and expected financial results. For a detailed discussion on the application of these and other accounting policies, see Item 8, Note 1 - Significant Accounting Policies.

The Company has prepared all of the consolidated financial information in this report in accordance with U.S. GAAP. The Company makes estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period. Such estimates include the valuation of loans, goodwill, intangible assets, and other long-lived assets, along with assumptions used in the calculation of income taxes, among others. These estimates and assumptions are based on management's best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes to be reasonable under the circumstances. We adjust such estimates and assumptions when facts and circumstances dictate. Decreased real estate values, volatile credit markets, and persistent high unemployment have combined to increase the uncertainty inherent in such estimates and assumptions. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates. Changes in estimates resulting from continuing changes in the economic environment will be reflected in the financial statement in future periods. There can be no assurances that actual results will not differ from those estimates.

Allowance for Loan Losses

The Company maintains an allowance for loan losses (“the allowance”), which is intended to be management's best estimate of probable inherent losses in the outstanding loan portfolio. The allowance is based on management's continuing review and evaluation of the loan portfolio. The review and evaluation combines several factors including: consideration of past loan loss experience; trends in past due and nonperforming loans; risk characteristics of the various classifications of loans; existing economic conditions; the fair value of underlying collateral; and other qualitative and quantitative factors which could affect probable credit losses. Because current economic conditions can change and future events are inherently difficult to predict, the anticipated amount of estimated loan losses, and therefore the adequacy of the allowance, could change significantly. As an integral part of their examination process, various regulatory agencies also review the allowance for loan losses. These agencies may require that certain loan balances be charged off when their credit evaluations differ from those of management, based on their judgments about information available to them at the time of their examination. The Company believes the allowance for loan losses is adequate and properly recorded in the consolidated financial statements. See Provision for Loan Losses above for more information.

Acquisitions and Divestitures
Acquired assets and liabilities are recorded at their estimated fair values at the date of acquisition. Goodwill represents the excess of the purchase price over the fair value of net assets, including the amount assigned to identifiable intangible assets. The purchase price allocation process requires an analysis of the fair values of the assets acquired and the liabilities assumed. When a business combination agreement provides for an adjustment to the cost of the combination contingent on future events, the Company includes that adjustment in the cost of the combination when the contingent consideration is determinable beyond a reasonable doubt and can be reliably estimated. The results of operations of the acquired business are included in the Company's consolidated financial statements from the respective date of acquisition. As a general rule, goodwill established in connection with a stock purchase is nondeductible for tax purposes.

Assets classified as held for sale are reported at the lower of its carrying value at the date the assets are initially classified as held for sale or their fair value less costs to sell. The results of operations of a component that either has been disposed of or held for sale is reported as discontinued operation if:

- the operations and cash flows of the disposal group will be eliminated from the ongoing operations as a result of the disposal transaction; and
- the Company will not have any significant continuing involvement in the operations of the entity after the disposal transaction.

Any incremental direct costs incurred to transact the sale are allocated against the gain or loss on the sale. These costs would include items like legal fees, title transfer fees, broker fees, etc. Any goodwill associated with the portion of the reporting unit that constitutes a business to be disposed of is included in the carrying amount of the business in determining the gain or loss on the sale. Also, any intangible assets or write down to fair value associated with the entity to be disposed of is also included in the carrying amount of the business in determining the gain or loss on the sale. The gain or loss on the sale is classified in the consolidated statements of income as noninterest income.

Loans Acquired Through Transfer
Loans acquired through the completion of a transfer, including loans acquired in a business combination that have evidence of deterioration of credit quality since origination and for which it is probable, at acquisition, that the Company will be unable to collect all contractually required payments receivable are initially recorded at fair value (as determined by the present value of expected future cash flows) with no valuation allowance. The difference between the undiscounted cash flows expected at acquisition and the investment in the loans, or the “accretable yield,” is recognized as interest income on a level-yield method over the life of the loans. Contractually required payments for interest and principal that exceed the undiscounted cash flows expected at acquisition, or the “nonaccretable difference,” are not recognized as a yield adjustment or as a loss accrual or a valuation allowance. The Company aggregates individual loans with common risk characteristics into pools of loans. Increases in expected cash flows subsequent to the initial investment are recognized prospectively through adjustment of the yield on the loans over their remaining lives. Decreases in expected cash flows due to an inability to collect contractual cash flows are recognized as impairment through the provision for loan losses account. Any allowance for loan loss on these pools reflect only losses incurred after the acquisition (meaning the present value of all cash flows expected at acquisition that ultimately are not to be received). Any disposals of loans, including sales of loans, payments in full or foreclosures result in the removal of the loan from the loan pool at the carrying amount with differences in actual results reflected in interest income.

Acquired impaired loans are generally considered accruing and performing as the loans accrete income over the estimated life of the loan when cash flows are reasonably estimable. Accordingly, acquired impaired loans that are contractually past due are still considered to be accruing and performing. If the timing and amount of future cash flows is not reasonably estimable, the loans may be classified as nonaccrual loans and the purchase price discount on those loans is not recorded as interest income until the timing and amount of future cash flows can be reasonably estimable.

Allowance for Loan Losses on Credit-Impaired Acquired Loans
The Company updates its cash flow projections for credit-impaired acquired loans, including loans acquired from the FDIC, on a quarterly basis. Assumptions utilized in this process include projections related to probability of default, loss severity, prepayment and recovery lag. Projections related to probability of default and prepayment are calculated utilizing a loan migration analysis. The loan migration analysis is a matrix of probability that specifies the probability of a loan pool transitioning into a particular delinquency state given its delinquency state at the re-measurement date. Loss severity factors are based upon industry data along with actual charge-off data within the loan pools and recovery lags are based upon the collateral within the loan pools.

Any decreases in expected cash flows after the acquisition date and subsequent measurement periods are recognized by recording an impairment in the provision for loan losses. As a result of impairment, the FDIC loss share receivable is increased to reflect future cash to be received from the FDIC. The amount of the increase is recorded in noninterest income and is determined based on the specific loss share agreement, but is generally 80% of the losses. See Loans Acquired Through Transfer above for further discussion. Any increase in expected future cash flows due to a decrease in expected credit losses will decrease the accretion of the FDIC loss share receivable, prospectively over the remaining life. Increases and decreases to the FDIC loss share receivable are recorded as adjustments to noninterest income.

Goodwill and Other Intangible Assets
Our goodwill impairment test is completed as of December 31 each year or whenever events or changes in circumstances indicate that the Company may not be able to recover the goodwill, or intangible assets, respective carrying amount. Such tests involve the use of various estimates and assumptions. Management believes that the estimates and assumptions utilized are reasonable. However, the Company may incur impairment charges related to goodwill or intangible assets in the future due to changes in business prospects or other matters that could affect our estimates and assumptions.

Goodwill is tested for impairment at the reporting unit level. Reporting units are defined as the same level as, or one level below, an operating segment. An operating segment is a component of a business for which separate financial information is available that management regularly evaluates in deciding how to allocate resources and assess performance. The Company's reporting units are Wealth Management and the Banking operations of Enterprise Bank & Trust. At December 31, 2011 and 2010, the Wealth Management reporting unit had no goodwill.

Businesses must identify potential impairments by comparing the fair value of a reporting unit to its carrying amount, including goodwill. Goodwill impairment does not occur as long as the fair value of the unit is greater than its carrying value. The second step of the impairment test is only required if a goodwill impairment is identified in step one. The second step of the test compares the implied fair market value of goodwill to its carrying amount. If the carrying amount of goodwill exceeds its implied fair market value, an impairment loss is recognized. That loss is equal to the carrying amount of goodwill that is in excess of its implied fair market value.

Intangible assets other than goodwill, such as core deposit intangibles, that are determined to have finite lives are amortized over their estimated remaining useful lives. These assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset.

There are three general approaches commonly used in business valuation: income approach, asset-based approach, and market approach. Within each of these approaches, there are various techniques for determining the value of a business using the definition of value appropriate for the appraisal assignment. Professional judgment is required to determine which valuation methods are the most appropriate. The valuation may utilize one or more of the approaches. Generally, the income approaches determine value by calculating the net present value of the benefit stream generated by the business (discounted cash flow); the asset-based approaches determine value by adding the sum of the parts of the business (net asset value); and the market approaches determine value by comparing the subject company to other companies in the same industry, of the same size, and/or within the same region.

Banking reporting unit

Based on the process described above, the Company recorded a $45.4 million, pre-tax goodwill impairment charge as of March 31, 2009 thus eliminating all goodwill in the Banking segment at that time.

In conjunction with the 2009 and 2011 FDIC-assisted transaction, we recorded $2.1 million and $28.3 million of goodwill, respectively, based on the fair value of the assets purchased and liabilities assumed. The 2011 annual impairment evaluation of the goodwill and intangible balances did not identify any impairment for the Banking reporting unit.

State Tax Credits Held for Sale

The Company purchases the rights to receive 10-year streams of state tax credits at agreed upon discount rates and sells such tax credits to Wealth Management clients and others. All state tax credits purchased prior to 2009 are accounted for at fair value. All state tax credits purchased since 2009 are accounted for at cost. The Company elected not to account for the state tax credits since 2009 at fair value in order to limit the volatility of the fair value changes in our consolidated statements of operations.

The Company is not aware of an active financial market for the 10-year streams of state tax credit financial instruments. However, the Company's principal market for these tax credits consists of Missouri state residents who buy them to reduce their state tax exposure and local and regional accounting firms who broker them. The state tax credits purchased by the Company are held until they are “usable” and then are sold to our clients for a profit.

The Company utilizes a discounted cash flow analysis (income approach) to determine the fair value of the state tax credits purchased prior to 2009. The fair value measurement is calculated using an internal valuation model. The inputs to the fair value calculation include: the amount of tax credits generated each year, the anticipated sale price of the tax credit, the timing of the sale and a discount rate. The discount rate is defined as the LIBOR swap curve at a point equal to the remaining life in years of credits plus a risk premium spread. With the exception of the discount rate, the other inputs to the fair value calculation are observable and readily available. The discount rate is an “unobservable input” and is based on the Company's assumptions. As a result, fair value measurement for these instruments falls within Level 3 of the fair value hierarchy.

At December 31, 2011, the discount rates utilized in our state tax credits fair value calculation ranged from 2.63% to 4.08%. Changes in the fair value of the state tax credits held for sale decreased the State tax credit activity, net in the consolidated statement of operations for the year ended December 31, 2011 by $1.2 million. A rate simulation with a 100 basis point parallel rate shock to the discount rate was run for December 31, 2011. The resulting simulation indicates that if the LIBOR swap curve were to increase by 100 basis points, the fair value of the state tax credits held at fair value would be lower by approximately $699,000. We would expect a portion of this decline would be offset by a change in the value of derivative financial instruments used to economically hedge the state tax credits.

These Level 3 fair value measurements are based primarily upon our own estimates and are calculated based on the current economic and regulatory environment, interest rate risks and other factors. Therefore, the results cannot be determined with precision, cannot be substantiated by comparison to quoted prices in active markets, and may not be realized in a current sale or immediate settlement of the asset or liability. Additionally, there are inherent uncertainties in any fair value measurement technique, and changes in the underlying assumptions used, including the discount rate and estimate of future cash flows, could significantly affect the fair value measurement amounts.

Derivative Financial Instruments

The Company uses derivative financial instruments to assist in managing interest rate sensitivity. The derivative financial instruments used are interest rate swaps and caps. Derivative financial instruments are required to be measured at fair value and recognized as either assets or liabilities in the consolidated financial statements. Fair value represents the payment the Company would receive or pay if the item were sold or bought in a current transaction. As of December 31, 2011, the Company used nondesignated derivative financial instruments to economically hedge changes

56

in the fair value of state tax credits held for sale and changes in the fair value of certain loans accounted for as trading instruments. In addition, the Company also offers an interest-rate hedge program that includes interest rate swaps to assist its customers in managing their interest-rate risk profile. In order to eliminate the interest-rate risk associated with offering these products, the Company enters into derivative contracts with third parties to offset the customer contracts. These customer accommodation interest rate swap contracts are not designated as hedging instruments.

- Cash Flow Hedges - Derivatives designated as cash flow hedges are recorded at fair value. The effective portion of the change in fair value is recorded (net of taxes) as a component of other comprehensive income ("OCI") in shareholders' equity. Amounts recorded in OCI are subsequently reclassified into interest income or expense (depending on whether the hedged item is an asset or liability) when the underlying transaction affects earnings. The ineffective portion of the change in fair value is recorded in noninterest income. Upon dedesignation of a derivative financial instrument from a cash flow hedge relationship, any remaining amounts in OCI are recorded in noninterest income over the expected remaining life of the underlying forecasted hedge transaction. The net interest differential between the hedged item and the hedging derivative financial instrument are recorded as an adjustment to interest income or interest expense of the related asset or liability.

- Fair Value Hedges - For derivatives designated as fair value hedges, the change in fair value of the derivative instrument and related hedged item are recorded in the related interest income or expense, as applicable, except for the ineffective portion, which is recorded in noninterest income in the consolidated statements of income. The swap agreement is accounted for on an accrual basis with the net interest differential being recognized as an adjustment to interest income or interest expense of the related asset or liability.

- Non-Designated Hedges - Certain derivative financial instruments are not designated as cash flow or as fair value hedges for accounting purposes. These non-designated derivatives are entered into to provide interest rate protection on net interest income or noninterest income but do not meet hedge accounting treatment. Changes in the fair value of these instruments are recorded in interest income or noninterest income in the consolidated statements of operations depending on the underlying hedged item.

The judgments and assumptions most critical to the application of this accounting policy are those affecting the estimation of fair value and hedge effectiveness. Changes in assumptions and conditions could result in greater than expected inefficiencies that, if large enough, could reduce or eliminate the economic benefits anticipated when the hedges were established and/or invalidate continuation of hedge accounting. Greater inefficiency and discontinuation of hedge accounting can result in increased volatility in reported earnings. For cash flow hedges, this would result in more or all of the change in the fair value of the related derivative financial instruments being reported in income. In December 2008, the Company discontinued hedge accounting on two prime based loan hedge relationships as a result of the significant decrease in the prime rate. As a result of the dedesignation, the changes in the fair value of the related derivative financial instruments are being reported in income without a corresponding and offsetting change in the fair value for the loans previously hedged.

Deferred Tax Assets and Liabilities
The Company accounts for income taxes under the asset/liability method. Deferred tax assets and liabilities are recognized for future tax effects of temporary differences, net operating loss carry forwards and tax credits. Deferred tax assets are reduced if necessary, by a deferred tax asset valuation allowance. A valuation allowance is established when in the judgment of management, it is more likely than not that such deferred tax assets will not become realizable. In this case, we would adjust the recorded value of our deferred tax assets, which would result in a direct charge to income tax expense in the period that the determination is made. Likewise, we would reverse the valuation allowance when realization of the deferred tax asset is expected.

Effects of New Accounting Pronouncements

See Item 8, Note 23 - New Authoritative Accounting Guidance for information on recent accounting pronouncements and their impact, if any, on our consolidated financial statements.

ITEM 7A: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Please refer to “Risk Factors” included in Item 1A and “Risk Management” included in Management's Discussion and Analysis under Item 7.

ITEM 8: FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Enterprise Financial Services Corp and Subsidiaries

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
Enterprise Financial Services Corp
St. Louis, Missouri

We have audited the accompanying consolidated balance sheets of Enterprise Financial Services Corp and subsidiaries (the "Company") as of December 31, 2011 and 2010, and the related consolidated statements of operations, shareholders' equity and comprehensive income (loss), 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, such consolidated financial statements present fairly, in all material respects, the financial position of Enterprise Financial Services Corp and subsidiaries as of December 31, 2011 and 2010, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 24 to the financial statements, the accompanying 2010 financial statements have been restated to correct misstatements.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2011, based on the criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 23, 2012, as to the effects of the material weakness described in Management's Report on Internal Control over Financial Reporting, which expressed an adverse opinion on the Company's internal control over financial reporting because of a material weakness.

/s/ Deloitte & Touche LLP

St. Louis, MO
April 23, 2012

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
Enterprise Financial Services Corp
St. Louis, Missouri

We have audited the accompanying consolidated statements of operations, shareholders' equity and comprehensive loss, and cash flows of Enterprise Financial Services Corp and subsidiaries (the Company) for the year ended December 31, 2009. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.
We conducted our audits in accordance with 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 results of operations of Enterprise Financial Services Corp and subsidiaries and their cash flows for the year ended December 31, 2009, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG LLP

St. Louis, MO
March 12, 2010

61

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Consolidated Balance Sheets
As of December 31, 2011 and 2010

(In thousands, except share and per share data)	December 31, 2011	As Restated[1] December 31, 2010
Assets		
Cash and due from banks	$20,791	$23,413
Federal funds sold	143	3,153
Interest-bearing deposits (including $2,650 and $1,520 pledged as collateral)	167,209	267,102
Total cash and cash equivalents	188,143	293,668
Interest-bearing deposits greater than 90 days	1,502	1,751
Securities available for sale	593,182	361,546
Mortgage loans held for sale	6,494	5,640
Portfolio loans not covered under FDIC loss share	1,897,074	1,766,351
Portfolio loans covered under FDIC loss share	300,610	121,570
Less: Allowance for loan losses	39,624	42,759
Portfolio loans, net	2,158,060	1,845,162
Other real estate not covered under FDIC loss share	17,217	25,373
Other real estate covered under FDIC loss share	36,471	10,835
Other investments, at cost	14,527	12,278
Fixed assets, net	18,986	20,499
Accrued interest receivable	9,193	7,464
State tax credits, held for sale, including $26,350 and $31,576 carried at fair value, respectively	50,446	61,148
FDIC loss share receivable	184,554	87,792
Goodwill	30,334	2,064
Intangibles, net	9,285	1,223
Other assets	59,385	63,756
Total assets	$3,377,779	$2,800,199
Liabilities and Shareholders' Equity		
Demand deposits	$585,479	$366,086
Interest-bearing transaction accounts	253,504	204,687
Money market accounts	1,084,304	855,522
Savings	51,145	10,181
Certificates of deposit:		
$100 and over	550,535	543,898
Other	266,386	317,347
Total deposits	2,791,353	2,297,721
Subordinated debentures	85,081	85,081
Federal Home Loan Bank advances	102,000	107,300
Other borrowings	154,545	119,333
Accrued interest payable	1,762	1,488
Other liabilities	3,473	9,475
Total liabilities	3,138,214	2,620,398
Shareholders' equity:		
Preferred stock, $0.01 par value; 5,000,000 shares authorized; 35,000 shares issued and outstanding	33,293	32,519

Common stock, $0.01 par value; 30,000,000 shares authorized; 17,849,862 and 14,965,401 shares issued, respectively	178	150
Treasury stock, at cost; 76,000 shares	(1,743)	(1,743)
Additional paid in capital	169,138	133,673
Retained earnings	35,097	15,775
Accumulated other comprehensive income (loss)	3,602	(573)
Total shareholders' equity	239,565	179,801
Total liabilities and shareholders' equity	$3,377,779	$2,800,199

(1) See Note 24 - Restatement of Consolidated Financial Statements for more information.

The accompanying notes are an integral part of the consolidated financial statements.

62

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Consolidated Statements of Operations
Years ended December 31, 2011, 2010 and 2009

	Years ended December 31,		
		As Restated[1]	
(In thousands, except per share data)	2011	2010	2009
Interest income:			
Interest and fees on loans	$130,073	$108,400	$112,548
Interest on debt securities:			
Taxable	11,142	7,031	5,459
Nontaxable	695	157	24
Interest on federal funds sold	2	10	6
Interest on interest-bearing deposits	560	370	130
Dividends on equity securities	368	426	319
Total interest income	142,840	116,394	118,486
Interest expense:			
Interest-bearing transaction accounts	811	847	662
Money market accounts	7,987	6,245	6,079
Savings	112	35	35
Certificates of deposit:			
$100 and over	9,133	9,854	15,592
Other	3,615	5,886	7,835
Subordinated debentures	4,515	4,954	5,171
Federal Home Loan Bank advances	3,550	4,326	4,797
Notes payable and other borrowings	432	264	8,674
Total interest expense	30,155	32,411	48,845
Net interest income	112,685	83,983	69,641
Provision for loan losses not covered under FDIC loss share	13,300	33,735	40,412
Provision for loan losses covered under FDIC loss share	2,803	—	—
Net interest income after provision for loan losses	96,582	50,248	29,229
Noninterest income:			
Wealth Management revenue	6,841	6,414	4,524
Service charges on deposit accounts	5,091	4,739	5,012
Other service charges and fee income	1,679	1,128	963
Gain (loss) on sale of other real estate	862	79	(436)
Gain on state tax credits, net	3,645	2,250	1,035
Gain on sale of investment securities	1,450	1,987	955
Change in FDIC loss share receivable	(3,494)	99	—
Extinguishment of debt	—	—	7,388
Miscellaneous income	2,434	1,664	436
Total noninterest income	18,508	18,360	19,877
Noninterest expense:			
Employee compensation and benefits	36,839	28,316	25,969
Occupancy	5,001	4,297	4,709
Furniture and equipment	1,601	1,393	1,425
Data processing	3,159	2,234	2,147
FDIC and other insurance	4,119	4,402	4,204
Goodwill impairment charge	—	—	45,377
Loan legal and other real estate expense	10,703	9,941	4,788

Other	16,296	11,629	9,808
Total noninterest expense	77,718	62,212	98,427
Income (loss) from continuing operations before income tax expense (benefit)	37,372	6,396	(49,321)
Income tax expense (benefit)	11,949	823	(2,650)
Income (loss) from continuing operations	$25,423	$5,573	$(46,671)
Loss from discontinued operations before income tax benefit	—	—	(408)
Loss on disposal before income tax benefit	—	—	(1,587)
Income tax benefit	—	—	(711)
Loss from discontinued operations	—	—	(1,284)
Net income (loss)	$25,423	$5,573	$(47,955)
Net income (loss) available to common shareholders	$22,899	$3,106	$(50,369)
Basic earnings (loss) per common share:			
From continuing operations	$1.37	$0.21	$(3.82)
From discontinued operations	—	—	(0.10)
Total	$1.37	$0.21	$(3.92)
Diluted earnings (loss) per common share:			
From continuing operations	$1.34	$0.21	$(3.82)
From discontinued operations	—	—	(0.10)
Total	$1.34	$0.21	$(3.92)

(1) See Note 24 - Restatement of Consolidated Financial Statements for more information.

The accompanying notes are an integral part of the consolidated financial statements.

63

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Consolidated Statements of Shareholders' Equity and Comprehensive Income (Loss)
Years ended December 31, 2009, 2010 and 2011

(in thousands, except per share data)	Preferred Stock	Common Stock	Treasury Stock	Additional paid in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance January 1, 2009	$31,116	$129	$(1,743)	$115,112	$68,710	$1,248	$214,572
Net loss	—	—	—	—	(47,955)	—	(47,955)
Change in fair value of available for sale securities, net of tax	—	—	—	—	—	455	455
Reclassification adjustment for realized gain on sale of securities included in net income, net of tax	—	—	—	—	—	(611)	(611)
Reclassification of cash flow hedge, net of tax	—	—	—	—	—	(159)	(159)
Total comprehensive loss							(48,270)
Cash dividends paid on common shares, $0.21 per share	—	—	—	—	(2,694)	—	(2,694)
Cash dividends paid on preferred stock	—	—	—	—	(1,585)	—	(1,585)
Preferred stock accretion of discount	686	—	—	—	(686)	—	—
Preferred stock issuance cost	—	—	—	(130)	—	—	(130)
Issuance under equity compensation plans, net, 81,839 shares	—	1	—	322	—	—	323
Share-based compensation	—	—	—	2,034	—	—	2,034
Excess tax expense related to equity compensation plans	—	—	—	(338)	—	—	(338)
Balance December 31, 2009	$31,802	$130	$(1,743)	$117,000	$15,790	$933	$163,912
Net income (Restated)(1)	—	—	—	—	5,573	—	5,573
Change in fair value of available for sale securities, net of tax	—	—	—	—	—	(79)	(79)
Reclassification adjustment for realized gain on sale of securities included in net income, net of tax	—	—	—	—	—	(1,272)	(1,272)
Reclassification of cash flow hedge, net of tax	—	—	—	—	—	(155)	(155)
Total comprehensive income							4,067
Cash dividends paid on common shares, $0.21 per share	—	—	—	—	(3,121)	—	(3,121)
Cash dividends paid on preferred stock	—	—	—	—	(1,750)	—	(1,750)
Preferred stock accretion of discount	717	—	—	—	(717)	—	—
Issuance under equity compensation plans, net, 74,971 shares	—	—	—	357	—	—	357
Issuance under private stock offering 1,931,610 shares	—	20	—	14,863	—	—	14,883
Share-based compensation	—	—	—	1,947	—	—	1,947

Excess tax expense related to equity compensation plans	—	—	—	(494)	—	—	(494)
Balance December 31, 2010 (Restated)(1)	$32,519	$150	$(1,743)	$133,673	$15,775	$ (573)	$ 179,801
Net income	—	—	—	—	25,423	—	25,423
Change in fair value of available for sale securities, net of tax	—	—	—	—	—	5,207	5,207
Reclassification adjustment for realized gain on sale of securities included in net income, net of tax	—	—	—	—	—	(928)	(928)
Reclassification of cash flow hedge, net of tax	—	—	—	—	—	(104)	(104)
Total comprehensive income							29,598
Cash dividends paid on common shares, $0.21 per share	—	—	—	—	(3,577)	—	(3,577)
Cash dividends paid on preferred stock	—	—	—	—	(1,750)	—	(1,750)
Preferred stock accretion of discount	774	—	—	—	(774)	—	—
Issuance under equity compensation plans, net, 140,561 shares	—	1	—	1,467	—	—	1,468
Issuance under public stock offering 2,743,900 shares	—	27	—	32,585	—	—	32,612
Share-based compensation	—	—	—	1,466	—	—	1,466
Excess tax expense related to equity compensation plans	—	—	—	(53)	—	—	(53)
Balance December 31, 2011	$33,293	$178	$(1,743)	$169,138	$35,097	$ 3,602	$ 239,565

(1) See Note 24 - Restatement of Consolidated Financial Statements for more information.

The accompanying notes are an integral part of the consolidated financial statements.

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Consolidated Statements of Cash Flows
Years ended December 31, 2011, 2010 and 2009

	Years ended December 31,		
		As Restated[1]	
(in thousands)	2011	2010	2009
Cash flows from operating activities:			
Net income (loss)	$25,423	$5,573	$(47,955)
Adjustments to reconcile net income (loss) to net cash provided by operating activities			
Depreciation	2,737	2,936	3,595
Provision for loan losses	16,103	33,735	40,412
Deferred income taxes	(733)	766	(2,545)
Net amortization of debt securities	6,210	3,527	1,415
Amortization of intangible assets	999	420	1,078
Gain on sale of investment securities	(1,450)	(1,987)	(955)
Mortgage loans originated for sale	(72,449)	(93,778)	(91,884)
Proceeds from mortgage loans sold	71,405	91,813	89,636
(Gain) loss on sale of other real estate	(862)	(79)	436
Gain on state tax credits, net	(3,645)	(2,250)	(1,035)
Excess tax expense of share-based compensation	53	494	338
Share-based compensation	1,466	1,947	2,202
Loss on disposal of Millennium Brokerage Group	—	—	1,587
Valuation adjustment on other real estate	4,702	5,632	2,389
Goodwill impairment charge	—	—	45,377
Net accretion of loan discount and indemnification asset	(13,950)	(5,652)	—
Changes in:			
Accrued interest receivable	(50)	286	(168)
Accrued interest payable	(647)	(636)	(375)
Prepaid FDIC insurance	2,904	3,027	(11,472)
Other assets	(2,386)	(2,576)	(3,223)
Other liabilities	(8,699)	6,026	(105)
Net cash provided by operating activities	27,131	49,224	28,748
Cash flows from investing activities:			
Cash received from acquisition of Valley Capital Bank	—	—	15,105
Cash received from sale of Millennium Brokerage Group	—	4,000	—
Cash paid for acquisition of Home National Bank	—	(224,471)	—
Cash received from acquisition of Legacy Bank	8,926	—	—
Cash received from acquisition of The First National Bank of Olathe	112,778	—	—
Cash received from BankLiberty branch purchase	42,591	—	—
Net (increase) decrease in loans	(85,034)	20,920	98,829
Net cash proceeds received from FDIC loss share receivable	41,415	5,009	—
Proceeds from the sale of debt and equity securities, available for sale	84,456	126,987	48,949
Proceeds from the maturity of debt and equity securities, available for sale	164,460	114,112	36,428
Proceeds from the sale of other investments	—	93	—
Proceeds from the redemption of other investments	6,061	6,130	429
Proceeds from the sale of state tax credits held for sale	16,690	9,569	7,709

Proceeds from the sale of other real estate	43,828	17,607	16,034
Payments for the purchase/origination of:			
Available for sale debt and equity securities	(431,374)	(323,834)	(271,954)
Other investments	(1,655)	(7,193)	(2,187)
Bank owned life insurance	—	(20,000)	—
State tax credits held for sale	(1,838)	(15,869)	(15,227)
Fixed assets	(910)	(957)	(552)
Net cash provided by (used in) investing activities	394	(287,897)	(66,437)

	Years ended December 31,		
		As Restated[1]	
(in thousands)	2011	2010	2009
Cash flows from financing activities:			
Net increase in noninterest-bearing deposit accounts	126,953	76,428	39,592
Net (decrease) increase in interest-bearing deposit accounts	(298,933)	279,877	65,686
Proceeds from Federal Home Loan Bank advances	—	52,780	20,000
Repayments of Federal Home Loan Bank advances	(23,254)	(73,580)	(11,857)
(Repayments) proceeds from federal funds purchased	—	—	(19,400)
Net increase in other borrowings	33,484	79,995	12,578
Cash dividends paid on common stock	(3,577)	(3,121)	(2,694)
Excess tax expense of share-based compensation	(53)	(494)	(338)
Cash dividends paid on preferred stock	(1,750)	(1,750)	(1,585)
Preferred stock issuance cost	—	—	(130)
Issuance of common stock	32,612	14,883	—
Proceeds from the issuance of equity instruments	1,468	357	156
Net cash (used in) provided by financing activities	(133,050)	425,375	102,008
Net (decrease) increase in cash and cash equivalents	(105,525)	186,702	64,319
Cash and cash equivalents, beginning of period	293,668	106,966	42,647
Cash and cash equivalents, end of period	$188,143	$293,668	$106,966
Supplemental disclosures of cash flow information:			
Cash paid (received) during the period for:			
Interest	$30,429	$33,048	$49,193
Income taxes	21,621	960	(2,817)
Noncash transactions: (also refer to Note 2 - Acquisitions)			
Transfer to other real estate owned in settlement of loans	$22,913	$37,763	$33,717
Sales of other real estate financed	5,621	8,609	6,258

(1) See Note 24 - Restatement of Consolidated Financial Statements for more information.
The accompanying notes are an integral part of the consolidated financial statements.

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES

Notes to Consolidated Financial Statements

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies used by the Company in the preparation of the consolidated financial statements are summarized below:

Business and Consolidation
Enterprise Financial Services Corp and subsidiaries (the "Company" or "Enterprise") is a financial holding company that provides a full range of banking and wealth management services to individuals and corporate customers located in the St. Louis, Kansas City and Phoenix metropolitan markets through its banking subsidiary, Enterprise Bank & Trust (the "Bank"). The consolidated financial statements include the accounts of the Company, and its subsidiaries, all of which are wholly owned. All intercompany accounts and transactions have been eliminated.

Since 2009, the Bank has entered into four transactions with the Federal Deposit Insurance Corporation ("FDIC") to acquire the following failed banks:

- On December 11, 2009, the Bank entered into an agreement with the FDIC and acquired certain assets and assumed certain liabilities of Valley Capital Bank N.A. ("Valley Capital"), a full service community bank that was headquartered in Mesa, Arizona.
- On July 9, 2010, the Bank entered into a loan sale agreement with the FDIC to purchase the loans originated and other real estate acquired by the Arizona operations of Home National Bank ("Home National"), of Blackwell Oklahoma.
- On January 7, 2011, the Bank entered into an agreement with the FDIC and acquired certain assets and assumed certain liabilities of Legacy Bank ("Legacy"), a full service community bank that was headquartered in Scottsdale, Arizona.
- On August 12, 2011, the Bank entered into an agreement with the FDIC and acquired certain assets and assumed certain liabilities of The First National Bank of Olathe ("FNBO"), a full service community bank that was headquartered in Olathe, Kansas.

On October 21, 2011, the Bank purchased certain assets and assumed certain deposit liabilities associated with a BankLiberty branch located at 11401 Olive Boulevard, in the St. Louis suburb of Creve Coeur, Missouri.

On January 20, 2010, the Company sold its interest in Millennium Brokerage Group, LLC ("Millennium") for $4.0 million in cash. The Company acquired 60% of Millennium in October 2005 and acquired the remaining 40% in December 2007. As a result of the sale, Millennium financial results are reported as discontinued operations for 2010 and 2009.

See Note 2 - Acquisitions for more information on the above transactions.

The Company is subject to competition from other financial and nonfinancial institutions providing financial services in the markets served by the Company's subsidiary. Additionally, the Company and its banking subsidiary are subject to the regulations of certain federal and state agencies and undergo periodic examinations by those regulatory agencies.

Use of Estimates
The consolidated financial statements of the Company and its subsidiaries have been prepared in conformity in accordance with U.S. generally accepted accounting principles ("U.S. GAAP".) In preparing the consolidated financial statements, management is required to make estimates and assumptions, which significantly affect the reported

amounts in the consolidated financial statements. Such estimates include the valuation of loans, goodwill, intangible assets, indemnification assets, and other long-lived assets, along with assumptions used in the calculation of income taxes, among others. These estimates and assumptions are based on management's best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes to be reasonable under the circumstances. Management adjusts such estimates and assumptions when facts and circumstances dictate. Decreased real estate values, volatile credit markets, and persistent high unemployment have combined to increase the uncertainty inherent in such estimates and assumptions. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates. Changes in those estimates resulting from continuing changes in the economic environment will be reflected in the financial statements in future periods.

Cash Flow Information
For purposes of reporting cash flows, the Company considers cash and due from banks, interest-bearing deposits and federal funds sold to be cash and cash equivalents. At December 31, 2011 and 2010, approximately $16.6 million and $9.6 million, respectively, of cash and due from banks represented required reserves on deposits maintained by the Company in accordance with Federal Reserve Bank requirements.

Investments
The Company has classified all investments in debt securities as available for sale.

Securities classified as available for sale are carried at estimated fair value. Unrealized holding gains and losses for available for sale securities are excluded from earnings and reported as a net amount in a separate component of shareholders' equity until realized. All previous fair value adjustments included in the separate component of shareholders' equity are reversed upon sale.

Declines in the fair value of securities below their cost that are deemed to be other-than-temporary are reflected in operations as realized losses. In estimating other-than-temporary impairment losses, management systematically evaluates investment securities for other-than-temporary declines in fair value on a quarterly basis. This analysis requires management to consider various factors, which include (1) the present value of the cash flows expected to be collected compared to the amortized cost of the security, (2) duration and magnitude of the decline in value, (3) the financial condition of the issuer or issuers, (4) structure of the security, and (5) the intent to sell the security or whether its more likely than not that the Company would be required to sell the security before its anticipated recovery in market value.

Premiums and discounts are amortized or accreted over the expected lives of the respective securities as an adjustment to yield using the interest method. Dividend and interest income is recognized when earned. Realized gains and losses are included in earnings and are derived using the specific identification method for determining the cost of securities sold.

Loans Held for Sale
The Company provides long-term financing of one-to-four-family residential real estate by originating fixed and variable rate loans. Long-term, fixed and variable rate loans are sold into the secondary market with limited recourse. Upon receipt of an application for a real estate loan, the Company determines whether the loan will be sold into the secondary market or retained in the Company's loan portfolio. The interest rates on the loans sold are locked with the buyer and the Company bears no interest rate risk related to these loans. Mortgage loans held for sale are carried at the lower of cost or fair value, which is determined on a specific identification method. The Company does not retain servicing on any loans sold, nor did the Company have any capitalized mortgage servicing rights at December 31, 2011 or 2010. Gains on the sale of loans held for sale are reported net of direct origination fees and costs in the Company's consolidated statements of operations.

Portfolio Loans
Loans are reported at the principal balance outstanding net of unearned fees and costs. Loan origination fees and direct origination costs are deferred and recognized over the lives of the related loans as a yield adjustment using a method, which approximates the interest method.

Interest income on loans is accrued to income based on the principal amount outstanding. The recognition of interest income is discontinued when a loan becomes 90 days past due or a significant deterioration in the borrower's credit has occurred which, in management's opinion, negatively impacts the collectability of the loan. Unpaid interest on such loans is reversed at the time the loan becomes uncollectable and subsequent interest payments received are applied to principal if any doubt exists as to the collectability of such principal; otherwise, such receipts are recorded as interest income. Loans that have not been restructured are returned to accrual status when management believes full collectability of principal and interest is expected. Non-accrual loans that have been restructured will remain in a non-accrual status until the borrower has made six consecutive contractual payments.

Loans Acquired Through Transfer

Loans acquired through the completion of a transfer, including loans acquired in a business combination that have evidence of deterioration of credit quality since origination and for which it is probable, at acquisition, that the Company will be unable to collect all contractually required payments receivable are initially recorded at fair value (as determined by the present value of expected future cash flows) with no valuation allowance. The difference between the undiscounted cash flows expected at acquisition and the investment in the loans, or the “accretable yield,” is recognized as interest income on a level-yield method over the life of the loans. Contractually required payments for interest and principal that exceed the undiscounted cash flows expected at acquisition, or the “nonaccretable difference,” are not recognized as a yield adjustment or as a loss accrual or a valuation allowance. The Company aggregates individual loans with common risk characteristics into pools of loans. Increases in expected cash flows subsequent to the initial investment are recognized prospectively through adjustment of the yield on the loans over their remaining lives. Decreases in expected cash flows due to an inability to collect contractual cash flows are recognized as impairment through the provision for loan losses account. Any allowance for loan loss on these pools reflect only losses incurred after the acquisition (meaning the present value of all cash flows expected at acquisition that ultimately are not to be received). Any disposals of loans, including sales of loans, payments in full or foreclosures result in the removal of the loan from the loan pool at the carrying amount with differences in actual results reflected in interest income.

Impaired Loans

A loan is considered impaired when management believes it is probable that collection of all amounts due, both principal and interest, according to the contractual terms of the loan agreement will not occur. Non-accrual loans, loans past due greater than 90 days and still accruing, and restructured loans qualify as “impaired loans.” Loans are also considered “impaired” when it becomes probable that the Company will be unable to collect all amounts due according to the loan's contractual terms. Restructured loans involve the granting of a concession to a borrower experiencing financial difficulty involving the modification of terms of the loan, such as changes in payment schedule or interest rate.

When measuring impairment, the expected future cash flows of an impaired loan are discounted at the loan's effective interest rate at origination. Alternatively, impairment is measured by reference to an observable market price, if one exists, or the fair value of the collateral for a collateral-dependent loan. Interest income on impaired loans is recorded when cash is received and only if principal is considered to be fully collectible. Loans and leases, which are deemed uncollectable, are charged off and deducted from the allowance for loan losses, while recoveries of amounts previously charged off are credited to the allowance for loan losses.

Impaired loans exclude credit-impaired loans that were acquired in the FDIC-assisted transactions. These purchased credit-impaired loans are accounted for on a pool basis and are generally considered accruing and performing loans as the loans accrete interest income over the estimated life of the loan when cash flows are reasonably estimable. Accordingly, acquired impaired loans that are contractually past due are still considered to be accruing and performing loans. If the timing and amount of future cash flows is not reasonably estimable, the loans may be classified as nonaccrual loans and the purchase price discount on those loans is not recorded as interest income until the timing and amount of future cash flows can be reasonably estimated. See Note 2 - Acquisitions and Note 6 - Portfolio Loans for more information on these loans.

Loan Charge-Offs

Loans are charged-off when the book balance of any loan whose primary and secondary sources of repayment (cash flow, collateral) no longer represent viable collection alternatives and the tertiary source (guarantors) must be sued to induce honoring the guaranty.

Allowance For Loan Losses

The allowance for loan losses is increased by provision charged to expense and is available to absorb charge offs, net of recoveries. Management utilizes a systematic, documented approach in determining the appropriate level of the allowance for loan losses. The level of the allowance reflects management's continuing evaluation of industry concentrations; specific credit risks; loan loss experience; current loan portfolio quality; present economic, political and regulatory conditions; and probable losses inherent in the current loan portfolio. The determination of the appropriate level of the allowance for loan losses inherently involves a degree of subjectivity and requires that we make significant estimates of current credit risks and future trends, all of which may undergo material changes. Changes in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of our control, may require an increase in the allowance for loan losses.

Management believes the allowance for loan losses is adequate to absorb inherent losses in the loan portfolio. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in economic conditions and other factors. In addition, various regulatory agencies, as an integral part of the examination process, periodically review the Bank's loan portfolio. Such agencies may require additions to the allowance for loan losses based on their judgments and interpretations of information available to them at the time of their examinations.

Allowance for Loan Losses on Credit-Impaired Acquired Loans
The Company updates its cash flow projections for credit-impaired acquired loans, including loans acquired from the FDIC, on a quarterly basis. Assumptions utilized in this process include projections related to probability of default, loss severity, prepayment and recovery lag. Projections related to probability of default and prepayment are calculated utilizing a loan migration analysis. The loan migration analysis is a matrix of probability that specifies the probability of a loan pool transitioning into a particular delinquency state given its delinquency state at the re-measurement date. Loss severity factors are based upon industry data along with actual charge-off data within the loan pools and recovery lags are based upon the collateral within the loan pools.

Any decreases in expected cash flows after the acquisition date and subsequent measurement periods are recognized by recording an impairment in the provision for loan losses. As a result of impairment, the FDIC loss share receivable is increased to reflect future cash to be received from the FDIC. The amount of the increase is recorded in noninterest income and is determined based on the specific loss share agreement, but is generally 80% of the losses. See Loans Acquired Through Transfer above for further discussion.

Other Real Estate
Other real estate represents property acquired through foreclosure or deeded to the Company in lieu of foreclosure on loans on which the borrowers have defaulted as to the payment of principal and interest. Other real estate is recorded on an individual asset basis at the lower of cost or fair value less estimated costs to sell. The fair value of other real estate is based upon estimates of future cash flows, market value of similar assets, if available, or independent appraisals. These estimates involve significant uncertainties and judgments and cannot be determined with certainty. As a result, fair value estimates may not be realizable in a current sale or settlement of the other real estate. Subsequent reductions in fair value are expensed.

Gains and losses resulting from the sale of other real estate are credited or charged to current period earnings. Costs of maintaining and operating other real estate are expensed as incurred, and expenditures to complete or improve other real estate properties are capitalized if the expenditures are expected to be recovered upon ultimate sale of the property.

FDIC Loss Share Receivable
As part of the FDIC- assisted transactions, the Bank entered into loss sharing agreements with the FDIC. The FDIC will reimburse the Bank for a percentage of realized losses on loans and foreclosed real estate covered under the agreement (“Covered Assets”). In addition, the Bank will be reimbursed for certain expenses related to the Covered

Assets. At the acquisition date, the fair value of the amount due from the FDIC ("FDIC Loss Share Receivable) was estimated based on expected losses and cash flows on the Covered Assets. The FDIC Loss Share Receivable is measured separately from the related Covered Assets and recorded separately on the balance sheet because it is not contractually embedded in the Covered Assets and is not transferable. Although these assets are contractual receivables from the FDIC, there are no contractual interest rates. See Note 2 - Acquisitions, for further information regarding these transactions.

Subsequent to initial recognition, the FDIC loss share receivable is reviewed quarterly and adjusted for any changes in expected cash flows. These adjustments are measured on the same basis as the related covered assets. Any decrease in expected cash flows due to an increase in expected credit losses will increase the FDIC loss share receivable which will partially offset the impairment on the Covered loans. Any increase in expected future cash flows due to a decrease in expected credit losses will decrease the accretion of the FDIC loss share receivable, prospectively over the remaining life. Increases and decreases to the FDIC loss share receivable are recorded as adjustments to noninterest income.

Fixed Assets

Buildings, leasehold improvements, and furniture, fixtures, equipment, and capitalized software are stated at cost less accumulated depreciation and amortization is computed using the straight-line method over their respective estimated useful lives. Furniture, fixtures and equipment is depreciated over three to ten years and buildings and leasehold improvements over ten to forty years based upon estimated lives or lease obligation periods.

State Tax Credits Held for Sale

The Company has purchased the rights to receive 10-year streams of state tax credits at agreed upon discount rates and sells such tax credits to wealth management customers and others. All state tax credits purchased prior to 2009 are accounted for at fair value. All state tax credits purchased since 2009 are accounted for at cost. The Company elected not to account for the state tax credits purchased since 2009 at fair value in order to limit the volatility of the fair value changes in the Company's consolidated statements of operations.

Cash Surrender Value of Life Insurance

The Company has purchased bank-owned life insurance policies on certain executives. Bank-owned life insurance is recorded at its cash surrender value. Changes in the cash surrender values are included in noninterest income.

Federal Home Loan Bank Stock

The Bank, as a member of the Federal Home Loan Bank of Des Moines (“FHLB”), is required to maintain an investment in the capital stock of the FHLB. The stock is redeemable at par by the FHLB, and is therefore, carried at cost and periodically evaluated for impairment. The Company records FHLB dividends in income on the ex-dividend date.

Goodwill and Other Intangible Assets

The Company tests goodwill for impairment on an annual basis and whenever events or changes in circumstances indicate that the Company may not be able to recover the respective asset's carrying amount. Such tests involve the use of estimates and assumptions. Core deposit intangibles are amortized using an accelerated method over an estimated useful life of approximately 10 years.

The Company must identify potential goodwill impairments by comparing the fair value of a reporting unit to its carrying amount, including goodwill. Goodwill impairment is not indicated as long as the fair value of the reporting unit is greater than its carrying value. The second step of the impairment test is only required if a goodwill impairment is identified in step one. The second step of the test compares the implied fair value of goodwill to its carrying amount. If the carrying amount of goodwill exceeds its implied fair value, an impairment loss is recognized. That loss is equal to the carrying amount of goodwill that is in excess of its implied fair market value.

Impairment of Long-Lived Assets

Long-lived assets, such as fixed assets and purchased intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of are separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposal group classified as held for sale are presented separately in the appropriate asset and liability sections of the balance sheet.

Derivative Financial Instruments and Hedging Activities
The Company uses derivative financial instruments to assist in the management of interest rate sensitivity and to modify the repricing, maturity and option characteristics of certain assets and liabilities. In addition, the Company also offers an interest rate hedge program that includes interest rate swaps to assist its customers in managing their interest rate risk profile. In order to eliminate the interest rate risk associated with offering these products, the Company enters into derivative contracts with third parties to offset the customer contracts.

Derivative instruments are required to be measured at fair value and recognized as either assets or liabilities in the consolidated financial statements. Fair value represents the payment the Company would receive or pay if the item were sold or bought in a current transaction. The accounting for changes in fair value (gains or losses) of a hedged item is dependent on whether the related derivative is designated and qualifies for “hedge accounting.” The Company assigns derivatives to one of these categories at the purchase date: cash flow hedge, fair value hedge, or non-designated derivatives. An assessment of the expected and ongoing hedge effectiveness of any derivative designated a fair value hedge or cash flow hedge is performed as required by the accounting standards. Derivatives are included in other assets and other liabilities in the consolidated balance sheets. Generally, the only derivative instruments used by the Company have been interest rate swaps and interest rate caps.

The following is a summary of the Company's accounting policies for derivative instruments and hedging activities.

- Cash Flow Hedges - Derivatives designated as cash flow hedges are recorded at fair value. The effective portion of the change in fair value is recorded (net of taxes) as a component of other comprehensive income (“OCI”) in shareholders' equity. Amounts recorded in OCI are subsequently reclassified into interest income or expense (depending on whether the hedged item is an asset or liability) when the underlying transaction affects earnings. The ineffective portion of the change in fair value is recorded in noninterest income. Upon dedesignation of a derivative financial instrument from a cash flow hedge relationship, any remaining amounts in OCI are recorded in noninterest income over the expected remaining life of the underlying forecasted hedge transaction. The net interest differential between the hedged item and the hedging derivative financial instrument are recorded as an adjustment to interest income or interest expense of the related asset or liability.

- Fair Value Hedges - For derivatives designated as fair value hedges, the change in fair value of the derivative instrument and related hedged item are recorded in the related interest income or expense, as applicable, except for the ineffective portion, which is recorded in noninterest income in the consolidated statements of income. The swap agreement is accounted for on an accrual basis with the net interest differential being recognized as an adjustment to interest income or interest expense of the related asset or liability.

- Non-Designated Hedges - Certain derivative financial instruments are not designated as cash flow or as fair value hedges for accounting purposes. These non-designated derivatives are intended to provide interest rate protection on net interest income or noninterest income but do not meet hedge accounting treatment. Customer accommodation interest rate swap contracts are not designated as hedging instruments. Changes in the fair value of these instruments are recorded in interest income or noninterest income in the consolidated statements of income depending on the underlying hedged item.

Income Taxes
The Company and its subsidiaries file a consolidated federal income tax return. Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. A valuation allowance is recognized if the Company determines it is more likely than not that all or some portion of the deferred tax asset will not be recognized. In estimating accrued taxes, the Company assesses

the relative merits and risks of the appropriate tax treatment considering statutory, judicial and regulatory guidance in the context of the tax position. Because of the complexity of tax laws and regulations, interpretation can be difficult and subject to legal judgment given specific facts and circumstances. It is possible that others, given the same information, may at any point in time reach different reasonable conclusions regarding the estimated amounts of accrued taxes.

Stock-Based Compensation
Stock-based compensation is recognized as an expense in the financial statements and measured at the grant date fair value for all equity classified awards.

Acquisitions and Divestitures
The Company accounts for business combinations using the acquisition method of accounting. Accordingly, the assets and liabilities of the acquired entities have been recorded at their estimated fair values at the date of acquisition. Goodwill represents the excess of the purchase price over the fair value of net assets, including the amount assigned to identifiable intangible assets.

The purchase price allocation process requires an estimation of the fair values of the assets acquired and the liabilities assumed. When a business combination agreement provides for an adjustment to the cost of the combination contingent on future events, the Company includes an estimate of the acquition-date fair value as part of the cost of the combination. The results of operations of the acquired business are included in the Company's consolidated financial statements from the respective date of acquisition. As a general rule, goodwill established in connection with a stock purchase is non-deductible for tax purposes.

For divestitures, the Company measures an asset (disposal group) classified as held for sale at the lower of its carrying value at the date the asset is initially classified as held for sale or its fair value less costs to sell. The Company reports the results of operations of a component that either has been disposed of or held to sale as discontinued operations if:

- The operations and cash flows of the disposal group will be eliminated from the ongoing operations as a result of the disposal transaction, and
- The Company will not have any significant continuing involvement in the operations of the entity after the disposal transaction.

Any incremental direct costs incurred to transact the sale are allocated against the gain or loss on the sale. These costs would include items like legal fees, title transfer fees, broker fees, etc. Any goodwill and intangible assets associated with the portion of the reporting unit to be disposed of is included in the carrying amount of the business in determining the gain or loss on the sale.

Basic and Diluted Earnings Per Common Share
Basic earnings (loss) per common share is computed by dividing net income by the weighted-average number of common shares outstanding during the applicable period. Diluted earnings per share is computed using the weighted-average number of shares determined for the basic earnings per common share computation plus the dilutive effect of stock compensation using the treasury stock method and convertible preferred stock using the if-converted method.

NOTE 2 - ACQUISITIONS

FDIC-Assisted Transactions
The loans and other real estate acquired are recorded at estimated fair value. As such, there was no allowance for credit losses established related to the acquired loans at the various acquisition dates and no carryover of the related allowance from the failed banks. The loans are accounted for in accordance with guidance for certain loans acquired in a transfer, when the loans have evidence of credit deterioration and it is probable at the date of acquisition that the acquirer will not collect all contractually required principal and interest payments. The difference between contractually required payments and the cash flows expected to be collected at acquisition is referred to as the

non-accretable difference. Subsequent decreases to the expected cash flows will generally result in a provision for loan losses. Subsequent increases in cash flows result in a reversal of the provision for loan losses to the extent of prior charges and an adjustment in accretable yield, which will have a positive impact on interest income, prospectively.

In connection with each acquisition, the Bank also entered into a shared-loss agreement whereby the FDIC will reimburse the Bank for a percentage of all losses incurred on certain loans and other real estate covered under the agreement, including single family residential mortgages and construction loans, as well as commercial loans. The shared-loss agreements are subject to the servicing procedures as specified in the agreement with the FDIC. The shared-loss agreements applicable to single-family residential mortgage loans have terms of ten (10) years, while the shared-loss agreements applicable to all other Covered Assets provide for the sharing of losses for five (5) years, while requiring the Bank to reimburse the FDIC for any recoveries of such shared losses for a period of eight (8) years.

The reimbursable losses from the FDIC are based on the book value of the Covered Assets as determined by the FDIC as of the date of the acquisition. A majority of these loans were valued based on the liquidation value of the underlying collateral because the future cash flows are primarily based on the liquidation of underlying collateral. The expected reimbursements under the shared-loss agreement were recorded as a FDIC loss share receivable at their estimated fair value.

Acquisition of The First National Bank of Olathe
On August 12, 2011, the Bank entered into a purchase and assumption agreement with the FDIC and acquired certain assets and assumed certain liabilities of FNBO headquartered in Olathe, Kansas, a national bank chartered by the Office of the Comptroller of the Currency.

The Company provided the FDIC with a Value Appreciation Instrument ("VAI") whereby 1.0 million units were awarded to the FDIC at an exercise price of $13.59 per unit. The units were exercisable any time from August 19, 2011 until August 10, 2012. The units were exercised on October 31, 2011 at a settlement price of $15.8393. A cash payment of approximately $2.2 million was made to the FDIC on November 1, 2011.

In connection with the acquisition, the Bank entered into shared-loss agreements with the FDIC that cover approximately $388.2 million of Covered Assets. Pursuant to the terms of the shared-loss agreements, the FDIC will reimburse the Bank for 80% of losses up to $112.6 million, 0% of losses between $112.6 million and $148.9 million and 80% of losses in excess of $148.9 million with respect to Covered Assets. The Bank will reimburse the FDIC for 80% of recoveries with respect to losses for which the FDIC has reimbursed the Bank under the shared-loss agreements.

The table below summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition. The Bank initially recorded the tangible assets and liabilities at their preliminary fair value. Subsequent to the initial fair value estimate, additional information was obtained on the credit quality of certain loans, the valuation of Other real estate, the valuation of certain Other assets, the FDIC clawback liability and Other liabilities as of the acquisition date which resulted in refinements to the initial fair value estimates. These fair value estimates are considered preliminary, and are subject to change for up to one year after the closing date of the acquisition as additional information relative to closing date fair values becomes available.

(in thousands)	Preliminary August 12, 2011 Amount	Refinements	Refined August 12, 2011 Amount
Cash and cash equivalents	$73,478	$—	$73,478
Securities available for sale	37,932	—	37,932
Other investments	4,563	—	4,563
Portfolio loans	171,037	415	171,452
Other real estate	44,179	(5,055)	39,124
FDIC receivable	36,674	12,544	49,218
FDIC loss share receivable	96,477	4,743	101,220
Goodwill	43,930	(17,218)	26,712
Core deposit intangible	7,905	—	7,905
Other assets	3,557	1,052	4,609

Total deposits	(508,941)	—	(508,941)
Federal Home Loan Bank Advances	(1,699)	—	(1,699)
Other liabilities	(9,092)	3,519	(5,573)

Acquisition of Legacy
On January 7, 2011, the Bank entered into a purchase and assumption agreement with the FDIC and acquired certain assets and assumed certain liabilities of Legacy, a full service community bank that was headquartered in Scottsdale, Arizona. As part of the acquisition, the Bank also acquired approximately $55.6 million of discretionary and $13.6 million of non-discretionary trust assets.

The Company provided the FDIC with a VAI whereby 372,500 units were awarded to the FDIC at an exercise price of $10.63 per unit. The units were exercisable at any time from January 14, 2011 until January 6, 2012. The FDIC exercised the units on January 20, 2011 at a settlement price of $11.8444. A cash payment of $452,364 was made to the FDIC on January 21, 2011.

In connection with the acquisition, the Bank also entered into a shared-loss agreement whereby the FDIC will reimburse the Bank for 80% of all losses incurred on Covered Assets.

The table below summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition. The Bank initially recorded the tangible assets and liabilities at their preliminary fair value. Subsequent to the initial fair value estimate, additional loans were deemed to be covered under the agreement which resulted in refinements to the initial fair value estimates. Management concluded that the impact of Legacy to the financial results was immaterial and therefore, presenting pro forma financial results was not necessary.

(in thousands)	Preliminary January 7, 2011 Amount	Refinements	Refined January 7, 2011 Amount
Cash and cash equivalents	$8,926	$—	$8,926
Securities available for sale	9,569	—	9,569
Other investments	1,969	—	1,969
Portfolio loans	73,214	—	73,214
Other real estate	8,612	—	8,612
FDIC loss share receivable	24,963	257	25,220
Goodwill	1,815	(257)	1,558
Core deposit intangible	833	—	833
Other assets	466	—	466
Total deposits	(113,620)	—	(113,620)
Federal Home Loan Bank Advances	(16,256)	—	(16,256)
Other liabilities	(491)	—	(491)

Acquisition of Home National
On July 9, 2010, the Bank acquired approximately $256.0 million in Arizona-originated assets from the FDIC in connection with the failure of Home National, an Oklahoma bank with operations in Arizona. As part of the purchase transaction, the Bank and the FDIC entered into a loss sharing agreement on the assets acquired. The Bank did not assume any deposits or acquire any branches or other assets of Home National in the transaction. The FDIC will reimburse the Bank for 80% of all losses on Covered Assets.

The following table summarizes the estimated fair values of the assets acquired at the date of acquisition:

(in thousands)	Amount
Loans	$136,093
Other real estate owned	5,469
FDIC loss share receivable	82,422
Other assets	487

Total	$224,471

Acquisition of Valley Capital
On December 11, 2009, the Bank entered into a loss sharing agreement with the FDIC and acquired certain assets and assumed certain liabilities of Valley Capital, a full service community bank that was headquartered in Mesa, Arizona.

The Bank initially recorded the tangible assets and liabilities at their preliminary fair value. Subsequent to the initial fair value estimate, additional information was obtained on the credit quality of certain loans and the valuation of Other real estate as of the acquisition date which resulted in refinements to the initial fair value estimates.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of the acquisition and the impact of the fair value refinements.

(in thousands)	Preliminary December 11, 2009		Refinements		Refined December 11, 2009	
Cash and cash equivalents	$3,542		$—		$3,542	
Federal funds sold	11,563		—		11,563	
Other investments	59		—		59	
Portfolio loans	14,730		(1,135	)	13,595	
Other real estate	3,455		(1,289	)	2,166	
FDIC loss share receivable	8,519		1,849		10,368	
Goodwill	953		1,111		2,064	
Other assets	567		(536	)	31	
Deposits	(43,355	)	—		(43,355	)
Other liabilities	(33	)	—		(33	)

Other Acquisitions and Divestitures

Acquisition of Creve Coeur, Missouri branch
On October 21, 2011, the Bank purchased certain assets and assumed certain deposit liabilities from BankLiberty of Liberty, Missouri. The Bank assumed $43.0 million in deposits associated with the BankLiberty branch located at 11401 Olive Boulevard, in the St. Louis suburb of Creve Coeur, Missouri. The deposits consisted of $2.6 million in demand deposits, $21.9 million in money market and other interest bearing deposits, and $18.6 million in certificates of deposit. The Bank also paid a deposit premium of $323,000 on these deposits and purchased $150,000 of personal property in the branch. The Bank executed a full-service sublease on approximately 6,556 square feet at the above address. Enterprise will operate the location as a full-service branch of the Bank.

Sale of Millennium - Discontinued Operations
On October 13, 2005, the Company acquired 60% of Millennium, a Tennessee limited liability company, for total consideration of $15.0 million. On December 31, 2007, the Company purchased the remaining 40% interest for cash of $1.5 million. As a result, Millennium became a wholly owned subsidiary of the Company.

On January 20, 2010, the Company sold Millennium for cash of $4.0 million resulting in a $1.6 million pre-tax loss, net of associated costs. The operating results for Millennium, including the loss on sale, have been reclassified and shown as discontinued operations in the consolidated statements of operations for all periods presented. At December 31, 2009, the Company presented the remaining assets of Millennium of $4.0 million as Assets of discontinued operations held for sale in the consolidated balance sheet. The Company does not have any direct significant continuing involvement with Millennium.

NOTE 3 - EARNINGS (LOSS) PER SHARE

Basic earnings (loss) per common share is calculated by dividing net income (loss) available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per common share gives effect to all dilutive potential common shares outstanding during the period using the treasury stock method and convertible preferred stock using the if-converted method. The following table presents a summary of per share data and amounts for the periods indicated.

	Years ended December 31,		
(in thousands, except per share data)	2011	2010	2009
Net income (loss) from continuing operations	$25,423	$5,573	$(46,671)
Net (loss) from discontinued operations	—	—	(1,284)
Net income (loss)	25,423	5,573	(47,955)
Preferred stock dividend	(1,750)	(1,750)	(1,750)
Accretion of preferred stock discount	(774)	(717)	(664)
Net income (loss) available to common shareholders	$22,899	$3,106	$(50,369)
Impact of assumed conversions			
Interest on 9% convertible trust preferred securities, net of income tax	1,485	—	—
Net income available to common shareholders and assumed conversions	$24,384	$3,106	$(50,369)
Weighted average common shares outstanding	16,683	14,747	12,833
Incremental shares from assumed conversions of convertible trust preferred securities	1,439	—	—
Additional dilutive common stock equivalents	23	—	—
Diluted common shares outstanding	18,145	14,747	12,833
Basic earnings (loss) per common share:			
From continuing operations	$1.37	$0.21	$(3.82)
From discontinued operations	—	—	(0.10)
From continuing and discontinued operations	$1.37	$0.21	$(3.92)
Diluted earnings (loss) per common share:			
From continuing operations	$1.34	$0.21	$(3.82)
From discontinued operations	—	—	(0.10)
From continuing and discontinued operations	$1.34	$0.21	$(3.92)

There were 899,493 common stock equivalents (including 324,074 common stock warrants) for fiscal year 2011; 2,707,424 common stock equivalents (including 324,074 common stock warrants) for fiscal year 2010; and 2,757,074 common stock equivalents (including 324,074 common stock warrants) for fiscal year 2009, which were excluded from the earnings per share calculations because their effect was anti-dilutive.

NOTE 4-PREFERRED STOCK AND COMMON STOCK WARRANTS

On December 19, 2008, the Company entered into an agreement with the United States Department of the Treasury (“U.S. Treasury”) under the Capital Purchase Program, pursuant to which the Company sold (i) 35,000 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A (“Senior Preferred Stock”) and (ii) a warrant to purchase 324,074 shares of EFSC common stock (“common stock warrants”), par value $0.01 per share, for an aggregate investment by the U.S. Treasury of $35.0 million.

The proceeds received were allocated between the Senior Preferred Stock and the common stock warrants based upon their relative fair values, which resulted in the recording of a discount on the senior preferred stock upon issuance that reflects the value allocated to the warrants. The discount is being accreted using a level-yield basis over five years, consistent with management's estimate of the life of the preferred stock. The allocated carrying value of the Senior Preferred Stock and common stock warrants on the date of issuance (based on their relative fair values) were $31.1 million and $3.9 million, respectively. Cumulative dividends on the Senior Preferred Stock are payable at 5% per annum for the first five years and at a rate of 9% per annum thereafter on the liquidation preference of $1,000 per share.

The Company is prohibited from paying any dividend with respect to shares of common stock unless all accrued and unpaid dividends are paid in full on the Senior Preferred Stock for all past dividend periods. The Senior Preferred Stock is non-voting, other than class voting rights on matters that could adversely affect the Senior Preferred Stock. The Senior Preferred Stock is callable at par after three years. Prior to the end of three years, according to the terms of the operative agreements, the Senior Preferred Stock may be redeemed with the proceeds from one or more qualified equity offerings of any Tier 1 perpetual preferred or common stock of EFSC of at least $8.8 million (each a “Qualified Equity Offering”), although certain amendments to the Emergency Economic Stabilization Act of 2008 enacted in February of 2009 eliminate this restriction on the means of redeeming the Senior Preferred Stock. The U.S. Treasury may also transfer the Senior Preferred Stock to a third party at any time.

Common Stock Warrants

The common stock warrants have a term of 10 years and are exercisable at any time, in whole or in part, at an exercise price of $16.20 per share (subject to certain anti-dilution adjustments). Assumptions were used in estimating the fair value of common stock warrants. The weighted average expected life of the common stock warrant represents the period of time that common stock warrants are expected to be outstanding. The risk-free interest rate was based on the U.S. Treasury yield curve in effect at the time of grant. The expected volatility was based on the historical volatility of the Company's stock. The following assumptions were used in estimating the fair value for the common stock warrants: a weighted average expected life of 10 years, a risk-free interest rate of 3.1%, an expected volatility of 47.3%, and a dividend yield of 5%. Based on these assumptions, the estimated fair value of the common stock warrants was $3.0 million. As previously noted, based on the common stock warrants' fair value relative to the senior preferred stock fair value, $3.9 million of the $35.0 million of proceeds was recorded to Additional paid in capital in the December 31, 2011 and 2010 consolidated balance sheets.

NOTE 5 - INVESTMENTS

Securities Available-for-Sale
The following table presents the amortized cost, gross unrealized gains and losses and fair value of securities available-for-sale:

(in thousands)	December 31, 2011 Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Obligations of U.S. Government sponsored enterprises	$126,305	$678	$ (66)	$126,917
Obligations of states and political subdivisions	38,489	1,729	(381)	39,837
Residential mortgage-backed securities	422,761	5,269	(1,602)	426,428
	$587,555	$7,676	$ (2,049)	$593,182

(in thousands)	December 31, 2010 Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Obligations of U.S. Government agencies	$444	$9	$ —	$453
Obligations of U.S. Government sponsored enterprises	32,880	9	(770)	32,119
Obligations of states and political subdivisions	18,486	45	(855)	17,676
Residential mortgage-backed securities	310,636	2,656	(1,994)	311,298
	$362,446	$2,719	$ (3,619)	$361,546

At December 31, 2011 and 2010, there were no holdings of securities of any one issuer in an amount greater than 10% of shareholders' equity, other than the U.S. government agencies and sponsored enterprises. The residential mortgage-backed securities are all issued by U.S. government sponsored enterprises. Available for sale securities having a carrying value of $287.8 million and $249.6 million at December 31, 2011 and 2010, respectively, were pledged as collateral to secure deposits of public institutions and for other purposes as required by law or contract provisions.

The amortized cost and estimated fair value of debt securities classified as available for sale at December 31, 2011, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. The weighted average life of the mortgage-backed securities is approximately 4 years.

(in thousands)	Amortized Cost	Fair Value
Due in one year or less	$3,019	$3,033
Due after one year through five years	79,198	79,841
Due after five years through ten years	78,195	79,692
Due after ten years	4,382	4,188
Residential mortgage-backed securities	422,761	426,428
	$587,555	$593,182

The following table represents a summary of available-for-sale investment securities that had an unrealized loss:

	December 31, 2011					
	Less than 12 months		12 months or more		Total	
(in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. government sponsored enterprises	$23,389	$66	$—	$—	$23,389	$66
Obligations of the state and political subdivisions	1,503	8	3,027	373	4,530	381
Residential mortgage-backed securities	86,954	1,598	4,203	4	91,157	1,602
	$111,846	$1,672	$7,230	$377	$119,076	$2,049

	December 31, 2010					
	Less than 12 months		12 months or more		Total	
(in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. government sponsored enterprises	$27,100	$770	$—	$—	$27,100	$770
Obligations of the state and political subdivisions	11,329	420	2,965	435	14,294	855
Residential mortgage-backed securities	133,893	1,994	—	—	133,893	1,994
	$172,322	$3,184	$2,965	$435	$175,287	$3,619

The unrealized losses at both December 31, 2011 and 2010, were attributable to changes in market interest rates since the securities were purchased. Management systematically evaluates investment securities for other-than-temporary declines in fair value on a quarterly basis. This analysis requires management to consider various factors, which include (1) the present value of the cash flows expected to be collected compared to the amortized cost of the security, (2) duration and magnitude of the decline in value, (3) the financial condition of the issuer or issuers, (4) structure of the security, and (5) the intent to sell the security or whether it is more likely than not that the Company would be required to sell the security before its anticipated recovery in market value. At December 31, 2011, management performed its quarterly analysis of all securities with an unrealized loss and concluded no individual securities were other-than-temporarily impaired.

The gross gains and gross losses realized from sales of available-for-sale investment securities were as follows:

	December 31,		
(in thousands)	2011	2010	2009
Gross gains realized	$1,450	$1,987	$955
Gross losses realized	—	—	—
Proceeds from sales	84,456	126,987	48,949

Other Investments, At Cost

As a member of the FHLB system administered by the Federal Housing Finance Board, the Bank is required to maintain a minimum investment in the capital stock of its respective FHLB consisting of membership stock and activity-based stock. The FHLB capital stock of $7.9 million is recorded at cost, and is included in other investments in the consolidated balance sheets, which represents redemption value. The Bank also has a $1.6 million investment in the FHLB of San Francisco. The remaining amounts in Other investments include the Company's investment in unconsolidated trusts used to issue preferred securities to third parties (see Note 11-Subordinated Debentures) and various private equity investments.

80

NOTE 6 - PORTFOLIO LOANS

Below is a summary of loans by category at December 31, 2011 and 2010:

(in thousands)	December 31, 2011 Portfolio Loans not Covered under FDIC loss share	Portfolio Loans Covered under FDIC loss share	Total
Real Estate Loans:			
Construction and land development	$140,147	$65,990	$206,137
Commercial real estate - Investor Owned	477,154	75,093	552,247
Commercial real estate - Owner Occupied	334,416	63,101	397,517
Residential real estate	171,034	56,828	227,862
Total real estate loans	$1,122,751	$261,012	$1,383,763
Commercial and industrial	763,202	36,423	799,625
Consumer & other	11,459	3,175	14,634
Portfolio Loans	$1,897,412	$300,610	$2,198,022
Unearned loan costs, net	(338)	—	(338)
Portfolio loans, including net unearned loan costs	$1,897,074	$300,610	$2,197,684

(in thousands)	December 31, 2010 Portfolio Loans not Covered under FDIC loss share	Portfolio Loans Covered under FDIC loss share	Total
Real Estate Loans:			
Construction and land development	$190,285	$32,374	$222,659
Commercial real estate - Investor Owned	444,724	39,850	484,574
Commercial real estate - Owner Occupied	331,544	29,803	361,347
Residential real estate	189,484	9,589	199,073
Total real estate loans	$1,156,037	$111,616	$1,267,653
Commercial and industrial	593,938	9,477	603,415
Consumer & other	16,308	477	16,785
Portfolio Loans	$1,766,283	$121,570	$1,887,853
Unearned loan costs, net	68	—	68
Portfolio loans, including net unearned loan costs	$1,766,351	$121,570	$1,887,921

The Company grants commercial, residential, and consumer loans primarily in the St. Louis, Kansas City and Phoenix metropolitan areas. The Company has a diversified loan portfolio, with no particular concentration of credit in any one economic sector; however, a substantial portion of the portfolio is concentrated in and secured by real estate. The ability of the Company's borrowers to honor their contractual obligations is partially dependent upon the local economy and its effect on the real estate market.

Following is a summary of activity for the years ended December 31, 2011, 2010, and 2009 of loans to executive officers and directors or to entities in which such individuals had beneficial interests as a shareholder, officer, or director. Such loans were made in the normal course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other customers and did not involve more than the normal risk of collectability.

(in thousands)	2011	2010	2009
Balance at beginning of year	$13,887	$9,240	$6,047
New loans and advances	9,927	6,411	5,571
Payments and other reductions	(10,401)	(1,764)	(2,378)
Balance at end of year	$13,413	$13,887	$9,240

A summary of activity in the allowance for loan losses and the recorded investment in loans by portfolio class and category based on impairment method for the years ended December 31, 2011 and 2010 is as follows:

(in thousands)	Commercial & Industrial	Commercial Real Estate Owner Occupied	Commercial Real Estate Investor Owned	Construction and Land Development	Residential Real Estate	Consumer & Other	Qualitative Adjustment	Portfolio loans covered under FDIC loss share	Total
Balance at December 31, 2011									
Allowance for Loan Losses:									
Balance, beginning of year	$12,727	$5,060	$5,629	$8,407	$5,485	$93	$5,358	$—	$42,759
Provision charged to expense	4,123	1,878	2,181	7,652	(244)	(136)	(2,154)	2,803	16,103
Losses charged off	5,488	955	1,474	10,627	1,613	5	—	1,168	21,330
Recoveries	583	314	415	415	303	62	—	—	2,092
Balance, end of year	$11,945	$6,297	$6,751	$5,847	$3,931	$14	$3,204	$1,635	$39,624
Allowance for Loan Losses - Ending Balance:									
Individually evaluated for impairment	$3,214	$1,377	$2,315	$2,927	$896	$—	$—	$—	$10,729
Collectively evaluated for impairment	8,731	4,920	4,436	2,920	3,035	14	3,204	1,635	28,895

Loans acquired with deteriorated credit quality	—	—	—	—	—	—	—	—	—
Total	$ 11,945	$ 6,297	$ 6,751	$ 5,847	$ 3,931	$ 14	$ 3,204	$ 1,635	$ 39,624
Loans - Ending Balance:									
Individually evaluated for impairment	$ 5,634	$ 4,572	$ 11,127	$ 14,767	$ 5,522	$—	$—	$—	$41,622
Collectively evaluated for impairment	757,568	329,844	466,027	125,380	165,512	11,121	—	3,489	1,858,941
Loans acquired with deteriorated credit quality	—	—	—	—	—	—	—	297,121	297,121
Total	$ 763,202	$ 334,416	$ 477,154	$ 140,147	$ 171,034	$ 11,121	$—	$ 300,610	$2,197,684

(in thousands)	Commercial & Industrial	Commercial Real Estate Owner Occupied	Commercial Real Estate Investor Owned	Construction and Land Development	Residential Real Estate	Consumer & Other	Qualitative Adjustment	Portfolio loans covered under FDIC loss share	Total
Balance at December 31, 2010									
Allowance for Loan Losses:									
Balance, beginning of year	$ 9,715	$ 5,992	$ 13,608	$ 4,289	$ 3,859	$ 45	$ 5,487	$ —	$ 42,995
Provision charged to expense	6,720	(86)	5,656	15,952	5,481	141	(129)	—	33,735
Losses charged off	3,865	846	14,636	12,148	4,391	274	—	—	36,160
Recoveries	157	—	1,001	314	536	181	—	—	2,189
Balance, end of year	$ 12,727	$ 5,060	$ 5,629	$ 8,407	$ 5,485	$ 93	$ 5,358	$ —	$ 42,759
Allowance for Loan Losses - Ending Balance:									
Individually evaluated for impairment	$ 4,434	$ 219	$ 1,457	$ 650	$ 2,368	$ —	$ —	$ —	$ 9,128
Collectively evaluated for impairment	8,293	4,841	4,172	7,757	3,117	93	5,358	—	33,631
Loans acquired with deteriorated credit quality	—	—	—	—	—	—	—	—	—
Total	$ 12,727	$ 5,060	$ 5,629	$ 8,407	$ 5,485	$ 93	$ 5,358	$ —	$ 42,759
Loans - Ending Balance:									
Individually evaluated for impairment	$ 11,276	$ 2,024	$ 10,935	$ 9,934	$ 12,188	$ —	$ —	$ —	$ 46,357
Collectively evaluated for impairment	582,662	329,520	433,789	180,351	177,296	16,376	—	350	1,720,344

Loans acquired with deteriorated credit quality	—	—	—	—	—	—	—	121,220	121,220
Total	$ 593,938	$ 331,544	$ 444,724	$ 190,285	$ 189,484	$ 16,376	$ —	$ 121,570	$ 1,887,921

A summary of loans individually evaluated for impairment by category at December 31, 2011 and 2010 is as follows:

(in thousands)	December 31, 2011 Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
Commercial & Industrial	$7,517	$128	$5,506	$5,634	$3,214	$6,571
Real Estate:						
Commercial - Owner Occupied	5,099	—	4,572	4,572	1,377	2,711
Commercial - Investor Owned	15,676	914	10,213	11,127	2,315	10,562
Construction and land development	19,685	1,628	13,139	14,767	2,927	16,114
Residential	6,465	2,211	3,311	5,522	896	9,588
Consumer & Other	—	—	—	—	—	—
Total	$54,442	$4,881	$36,741	$41,622	$10,729	$45,546

(in thousands)	December 31, 2010 Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
Commercial & Industrial	$11,591	$412	$10,864	$11,276	$4,434	$5,848
Real Estate:						
Commercial - Owner Occupied	2,668	1,044	980	2,024	219	3,890
Commercial - Investor Owned	15,024	1,960	8,975	10,935	1,457	15,122
Construction and land development	13,391	5,388	4,546	9,934	650	16,898
Residential	12,390	2,650	9,538	12,188	2,368	5,721
Consumer & Other	—	—	—	—	—	92
Total	$55,064	$11,454	$34,903	$46,357	$9,128	$47,571

There was one loan over 90 days past due and still accruing interest at December 31, 2011, and no loans over 90 days past due and still accruing interest at December 31, 2010 or 2009. If interest on impaired loans would have been accrued based upon the original contractual terms, such income would have been $3.0 million, $3.5 million, and $3.3 million for the years ended December 31, 2011, 2010, and 2009, respectively. The cash amount collected and recognized as interest income on impaired loans was $513,000, $78,000, and $112,000 for the years ended December 31, 2011, 2010, and 2009, respectively. The amount recognized as interest income on impaired loans continuing to accrue interest was $429,000, $150,000, and $16,000 for the years ended December 31, 2011, 2010, and 2009, respectively. At December 31, 2011 there were $1.3 million of unadvanced commitments on impaired loans. Other Liabilities include approximately $257,000 for estimated losses attributable to the unadvanced commitments on impaired loans. At December 31, 2010 there were $1.4 million of unadvanced commitments on impaired loans. Other liabilities include approximately $280,000 for estimated losses attributable to the unadvanced commitments on impaired loans.

The recorded investment in impaired loans by category at December 31, 2011 and 2010 is as follows:

	December 31, 2011			
(in thousands)	Non-accrual	Restructured	Loans over 90 days past due and still accruing interest	Total
Commercial & Industrial	$4,475	$1,159	$—	$5,634
Real Estate:				
Commercial - Investor Owned	6,647	4,480	—	11,127
Commercial - Owner Occupied	4,129	443	—	4,572
Construction and land development	10,335	3,677	755	14,767
Residential	5,299	223	—	5,522
Consumer & Other	—	—	—	—
Total	$30,885	$9,982	$755	$41,622

	December 31, 2010			
(in thousands)	Non-accrual	Restructured	Loans over 90 days past due and still accruing interest	Total
Commercial & Industrial	$11,276	$—	$—	$11,276
Real Estate:				
Commercial - Investor Owned	10,516	419	—	10,935
Commercial - Owner Occupied	2,024	—	—	2,024
Construction and land development	9,352	582	—	9,934
Residential	5,309	6,879	—	12,188
Consumer & Other	—	—	—	—
Total	$38,477	$7,880	$—	$46,357

The recorded investment by category for the loans meeting the definition of troubled debt restructures at December 31, 2011 is as follows:

	Year ended December 31, 2011		
(in thousands, except for number of loans)	Number of Loans	Pre-Modification Outstanding Recorded Balance	Post-Modification Outstanding Recorded Balance
Commercial & Industrial	5	$2,102	$1,159
Real Estate:			
Commercial - Owner Occupied	1	443	443
Commercial - Investor Owned	1	4,365	4,480
Construction and land development	2	4,341	3,677
Residential	1	223	223
Consumer & Other	—	—	—
Total	10	$11,474	$9,982

85

The restructured loans resulted from interest rate concessions and changing the terms of the loans. As of December 31, 2011, the Company has allocated $1.7 million of specific reserves to the loans that have been restructured. At December 31, 2011, the Company has a commitment to lend an additional $1.3 million to customers with outstanding loans that has been classified as restructured and has allocated a $250,000 specific reserve to these loans.

The recorded investment by category for the loans that have been restructured and subsequently defaulted during 2011 is as follows:

	Year ended December 31, 2011	
(in thousands, except for number of loans)	Number of Loans	Recorded Balance
Commercial & Industrial	—	$—
Real Estate:		
Commercial - Owner Occupied	—	—
Commercial - Investor Owned	1	418
Construction and land development	2	597
Residential	1	563
Consumer & Other	—	—
Total	4	$1,578

86

The aging of the recorded investment in past due loans by portfolio class and category at December 31, 2011 and 2010 is shown below.

	December 31, 2011				
(in thousands)	30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Portfolio loans not covered under FDIC loss share					
Commercial & Industrial	$4,521	$792	$5,313	$757,889	$763,202
Real Estate:					
Commercial - Owner Occupied	1,945	1,522	3,467	330,949	334,416
Commercial - Investor Owned	2,308	4,209	6,517	470,637	477,154
Construction and land development	1,356	9,786	11,142	129,005	140,147
Residential	299	4,137	4,436	166,598	171,034
Consumer & Other	—	—	—	11,121	11,121
Total	$10,429	$20,446	$30,875	$1,866,199	$1,897,074
Portfolio loans covered under FDIC loss share					
Commercial & Industrial	$879	$9,867	$10,746	$25,677	$36,423
Real Estate:					
Commercial - Owner Occupied	1,438	9,684	11,122	51,979	63,101
Commercial - Investor Owned	2,530	7,021	9,551	65,542	75,093
Construction and land development	2,842	28,745	31,587	34,403	65,990
Residential	1,634	3,341	4,975	51,853	56,828
Consumer & Other	236	7	243	2,932	3,175
Total	$9,559	$58,665	$68,224	$232,386	$300,610
Portfolio loans, total					
Commercial & Industrial	$5,400	$10,659	$16,059	$783,566	$799,625
Real Estate:					
Commercial - Owner Occupied	3,383	11,206	14,589	382,928	397,517
Commercial - Investor Owned	4,838	11,230	16,068	536,179	552,247
Construction and land development	4,198	38,531	42,729	163,408	206,137
Residential	1,933	7,478	9,411	218,451	227,862
Consumer & Other	236	7	243	14,053	14,296
Total	$19,988	$79,111	$99,099	$2,098,585	$2,197,684

(in thousands)	December 31, 2010 30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Portfolio loans not covered under FDIC loss share					
Commercial & Industrial	$5,938	$3,557	$9,495	$584,443	$593,938
Real Estate:					
Commercial - Owner Occupied	914	1,583	2,497	329,047	331,544
Commercial - Investor Owned	2,692	4,348	7,040	437,684	444,724
Construction and land development	802	6,876	7,678	182,607	190,285
Residential	2,496	2,518	5,014	184,470	189,484
Consumer & Other	3	—	3	16,373	16,376
Total	$12,845	$18,882	$31,727	$1,734,624	$1,766,351
Portfolio loans covered under FDIC loss share					
Commercial & Industrial	$777	$258	$1,035	$8,442	$9,477
Real Estate:					
Commercial - Owner Occupied	56	5,550	5,606	24,197	29,803
Commercial - Investor Owned	3,471	1,888	5,359	34,491	39,850
Construction and land development	—	25,844	25,844	6,530	32,374
Residential	679	735	1,414	8,175	9,589
Consumer & Other	190	—	190	287	477
Total	$5,173	$34,275	$39,448	$82,122	$121,570
Portfolio loans, total					
Commercial & Industrial	$6,715	$3,815	$10,530	$592,885	$603,415
Real Estate:					
Commercial - Owner Occupied	970	7,133	8,103	353,244	361,347
Commercial - Investor Owned	6,163	6,236	12,399	472,175	484,574
Construction and land development	802	32,720	33,522	189,137	222,659
Residential	3,175	3,253	6,428	192,645	199,073
Consumer & Other	193	—	193	16,660	16,853
Total	$18,018	$53,157	$71,175	$1,816,746	$1,887,921

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt, such as current financial information, historical payment experience, credit documentation, and current economic factors among other factors. This analysis is performed on a quarterly basis. The Company uses the following definitions for risk ratings:

- Grades 1, 2, and 3 - These grades include loans to borrowers with a continuous record of strong earnings, sound balance sheet condition and capitalization, ample liquidity with solid cash flow and whose management team has experience and depth within their industry.
- Grade 4 – This grade includes loans to borrowers with positive trends in profitability, satisfactory capitalization and balance sheet condition, and sufficient liquidity and cash flow.
- Grade 5 – This grade includes loans to borrowers that may display fluctuating trends in sales, profitability, capitalization, liquidity, and cash flow.
-

Grade 6 – This grade includes loans to borrowers where an adverse change or perceived weakness has occurred, but may be correctable in the near future. Alternatively, this rating category may also include circumstances where the company is starting to reverse a negative trend or condition, or have recently been upgraded from a 7, 8, or 9 rating.

- Grade 7 – Watch credits are companies that have experienced financial setback of a nature that are not determined to be severe or influence ‘ongoing concern’ expectations. Borrowers within this category are expected to turnaround within a 12-month period of time. Although possible, no loss is anticipated, due to strong collateral and/or guarantor support.
- Grade 8 – Substandard credits will include those companies that are characterized by significant losses and sustained downward trends in balance sheet condition, liquidity, and cash flow. Repayment reliance may have shifted to secondary sources. Collateral exposure may exist and additional reserves may be warranted.
- Grade 9 – Doubtful credits include borrowers that may show deteriorating trends that are unlikely to be corrected. Collateral values may appear insufficient for full recovery, therefore requiring a partial charge-off, or debt renegotiation with the borrower. Borrower may have declared bankruptcy or bankruptcy is likely in the near term. All doubtful rated credits will be on non-accrual.

Acquired loans are also subject to the Company’s internal and external credit review and are risk rated using the same criteria as loans originated by the Company. However, risk ratings are not always a clear indicator of the Company's losses on acquired loans as a majority of the losses are recoverable from the FDIC under the loss-sharing agreements.

The recorded investment by risk category of the loans by portfolio class and category at December 31, 2011, which is based upon the most recent analysis performed, and 2010 is as follows:

	December 31, 2011						
(in thousands)	Commercial & Industrial	Commercial Real Estate Owner Occupied	Commercial Real Estate Investor Owned	Construction and Land Development	Residential Real Estate	Consumer & Other	Total
Portfolio loans not covered under FDIC loss share							
Outstanding (1-3)	$104,319	$9,379	$6,662	$ 1,290	$1,943	$2,827	$126,420
Above Average (4)	52,673	59,662	32,592	8,209	13,703	1,597	168,436
Average (5)	386,315	163,067	284,677	47,899	120,200	6,487	1,008,645
Below Average (6)	139,932	44,694	81,755	33,888	12,463	201	312,933
Watch (7)	50,197	40,207	56,370	27,056	4,814	9	178,653
Substandard (8)	27,229	16,225	14,894	21,461	16,419	—	96,228
Doubtful (9)	2,537	1,182	204	344	1,492	—	5,759
Total	$763,202	$334,416	$477,154	$ 140,147	$171,034	$11,121	$1,897,074
Portfolio loans covered under FDIC loss share							
Outstanding (1-3)	$501	$294	$1,606	$ 97	$11,142	$589	$14,229
Above Average (4)	1,066	2,885	69	602	5,510	59	10,191
Average (5)	12,205	31,140	40,975	13,938	24,819	2,381	125,458
Below Average (6)	1,838	6,981	1,217	419	1,305	128	11,888
Watch (7)	2,479	3,638	4,498	7,736	4,766	—	23,117
Substandard (8)	18,334	18,099	26,280	41,013	8,751	11	112,488
Doubtful (9)	—	64	448	2,185	535	7	3,239
Total	$36,423	$63,101	$75,093	$ 65,990	$56,828	$3,175	$300,610
Portfolio loans, total							
Outstanding (1-3)	$104,820	$9,673	$8,268	$ 1,387	$13,085	$3,416	$140,649
Above Average (4)	53,739	62,547	32,661	8,811	19,213	1,656	178,627
Average (5)	398,520	194,207	325,652	61,837	145,019	8,868	1,134,103
Below Average (6)	141,770	51,675	82,972	34,307	13,768	329	324,821
Watch (7)	52,676	43,845	60,868	34,792	9,580	9	201,770
Substandard (8)	45,563	34,324	41,174	62,474	25,170	11	208,716
Doubtful (9)	2,537	1,246	652	2,529	2,027	7	8,998
Total	$799,625	$397,517	$552,247	$ 206,137	$227,862	$14,296	$2,197,684

(in thousands)	December 31, 2010 Commercial & Industrial	Commercial Real Estate Owner Occupied	Commercial Real Estate Investor Owned	Construction and Land Development	Residential Real Estate	Consumer & Other	Total
Portfolio loans not covered under FDIC loss share							
Outstanding (1-3)	$92,940	$19,139	$6,846	$ 1,142	$1,522	$5,930	$127,519
Above Average (4)	48,745	68,443	31,826	8,549	17,400	2,264	177,227
Average (5)	252,938	149,773	259,937	80,400	127,587	7,722	878,357
Below Average (6)	135,174	46,080	91,385	27,931	10,900	117	311,587
Watch (7)	26,549	33,374	38,680	32,519	8,272	9	139,403
Substandard (8)	34,512	14,634	15,812	39,744	23,759	334	128,795
Doubtful (9)	3,080	101	238	—	44	—	3,463
Total	$593,938	$331,544	$444,724	$ 190,285	$189,484	$16,376	$1,766,351
Portfolio loans covered under FDIC loss share							
Outstanding (1-3)	$—	$—	$—	$ —	$—	$77	$77
Above Average (4)	—	—	—	—	105	—	105
Average (5)	3,902	8,287	13,951	1,253	4,047	357	31,797
Below Average (6)	4,719	7,486	7,485	1,483	2,584	43	23,800
Watch (7)	62	3,219	6,943	337	1,351	—	11,912
Substandard (8)	794	10,811	9,209	22,160	1,142	—	44,116
Doubtful (9)	—	—	2,262	7,141	360	—	9,763
Total	$9,477	$29,803	$39,850	$ 32,374	$9,589	$477	$121,570
Portfolio loans, total							
Outstanding (1-3)	$92,940	$19,139	$6,846	$ 1,142	$1,522	$6,007	$127,596
Above Average (4)	48,745	68,443	31,826	8,549	17,505	2,264	177,332
Average (5)	256,840	158,060	273,888	81,653	131,634	8,079	910,154
Below Average (6)	139,893	53,566	98,870	29,414	13,484	160	335,387
Watch (7)	26,611	36,593	45,623	32,856	9,623	9	151,315
Substandard (8)	35,306	25,445	25,021	61,904	24,901	334	172,911
Doubtful (9)	3,080	101	2,500	7,141	404	—	13,226
Total	$603,415	$361,347	$484,574	$ 222,659	$199,073	$16,853	$1,887,921

Portfolio loans covered under FDIC loss share

Purchased loans acquired in a business combination, including loans purchased in our FDIC-assisted transactions, are recorded at estimated fair value on their purchase date without a carryover of the related allowance for loan losses. Purchased credit-impaired loans are loans that have evidence of credit deterioration since origination and it is probable at the date of acquisition that the Company will not collect all contractually required principal and interest payments. Evidence of credit quality deterioration as of the purchase date may include factors such as past due and non-accrual status. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition is referred to as the non-accretable yield. Subsequent decreases to the expected cash flows will generally result in a provision for loan losses. Subsequent increases in cash flows result in a reversal of the provision for loan losses to the extent of prior charges or a reclassification of the difference from non-accretable to accretable with a positive impact on interest income, prospectively. Further, any excess of cash flows expected at acquisition over the estimated fair value is referred to as the accretable yield and is recognized into interest income over the remaining life of the loan when there is a reasonable expectation about the amount and timing of such cash flows. Acquired loans that have common risk characteristics are aggregated into pools. The Company re-measures contractual and expected cash flows, at the pool-level, on a quarterly basis.

Inputs to the determination of expected cash flows include contractual cash flows, cumulative default and prepayment data as well as loss severity and recovery lag information. Cumulative default and prepayment data are calculated via a transition matrix. The transition matrix is a matrix of probability values that specifies the probability of a loan pool transitioning into a loss given its delinquency state (e.g. 0-30 days past due, 31 to 60 days, etc.) at the re-measurement date. Loss severity factors are based upon industry data along with actual charge-off data within the loan pools and recovery lags are based upon experience with the collateral within the loan pools.

The accretable yield is accreted into interest income over the estimated life of the acquired loans using the effective yield method. Other adjustments to the accretable yield include changes in the estimated remaining life of the acquired loans, changes in expected cash flows and changes of indices for acquired loans with variable interest rates.

Changes in the accretable yield for purchased loans were as follows for the years ended December 31, 2011 and 2010:

(in thousands)	December 31, 2011	December 31, 2010
Balance at beginning of period	$46,460	$3,708
Additions	40,380	50,027
Accretion	(23,792)	(7,275)
Other	287	—
Balance at end of period	$63,335	$46,460

Outstanding balances on purchased loans from the FDIC were $496.2 million and $219.5 million as of December 31, 2011 and 2010, respectively. In 2011, the Bank received payments of $41.4 million for loss share claims under the terms of the FDIC shared-loss agreements.

The following tables present information regarding the contractually required payments receivable, the cash flows expected to be collected, and the estimated fair value of the loans acquired in the following 2011 acquisitions, at the closing date of the transaction:

Legacy acquisition

(In thousands)	January 7, 2011 Purchased Credit-Impaired Loans
Contractually required payments (principal and interest):	$106,286
Cash flows expected to be collected (principal and interest):	84,089
Fair value of loans acquired:	73,214

The First National Bank of Olathe acquisition

(In thousands)	August 12, 2011 Purchased Credit-Impaired Loans
Contractually required payments (principal and interest):	$358,085
Cash flows expected to be collected (principal and interest):	200,957
Fair value of loans acquired:	171,452

92

These amounts were determined based upon the estimated remaining life of the underlying loans, which includes the effects of estimated prepayments. A significant portion of the purchased credit-impaired loans were valued based on the liquidation value of the underlying collateral. At December 31, 2011, there was $1.6 million of allowance for credit losses on purchased loans related to FDIC-assisted transactions.

The determination of the initial fair value of loans and other real estate acquired in the transaction and the initial fair value of the related FDIC loss share receivable involve a high degree of judgment and complexity. The carrying value of the acquired loans and other real estate and the FDIC indemnification asset reflect management’s best estimate of the fair value of each of these assets as of the date of acquisition. However, the amount that the Company realizes on these assets could differ materially from the carrying value reflected in these financial statements, based upon the timing and amount of collections on the acquired loans in future periods. To the extent the actual values realized for the acquired loans are different from the estimate, the FDIC loss share receivable will generally be affected in an offsetting manner due to the indemnification obligations of the FDIC, thus limiting the Company's loss exposure.

NOTE 7 - DERIVATIVE FINANCIAL INSTRUMENTS

The Company is a party to various derivative financial instruments that are used in the normal course of business to meet the needs of its clients and as part of its risk management activities. These instruments include interest rate swaps and option contracts. The Company does not enter into derivative financial instruments for trading or speculative purposes.

Interest rate swap contracts involve the exchange of fixed and floating rate interest payment obligations without the exchange of the underlying principal amounts. The Company enters into interest rate swap contracts on behalf of its clients and also utilizes such contracts to reduce or eliminate the exposure to changes in the cash flows or fair value of hedged assets or liabilities due to changes in interest rates. Interest rate option contracts consist of caps and provide for the transfer or reduction of interest rate risk in exchange for a fee.

All derivative financial instruments, whether designated as hedges or not, are recorded on the consolidated balance sheet at fair value within Other assets or Other liabilities. The accounting for changes in the fair value of a derivative in the consolidated statement of operations depends on whether the contract has been designated as a hedge and qualifies for hedge accounting. At December 31, 2011 and 2010, the Company did not have any derivatives designated as cash flow or fair value hedges.

To qualify for hedge accounting treatment, a derivative must be highly effective in mitigating the designated changes in fair value or cash flow of the hedged item. Prior to entering into a hedge, the Company formally documents the relationship between hedging instruments and hedged items, as well as the related risk management objective. The documentation process includes linking derivatives that are designated as fair value or cash flow hedges to specific assets or liabilities in the consolidated balance sheet or to specific forecasted transactions, and defining the effectiveness and ineffectiveness testing methods to be used. The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions have been, and are expected to continue to be, highly effective in offsetting changes in fair values or cash flows of hedged items.

Using derivative instruments means assuming counterparty credit risk. Counterparty credit risk relates to the loss the Company could incur if a counterparty were to default on a derivative contract. Notional amounts of derivative financial instruments do not represent credit risk, and are not recorded in the consolidated balance sheet. They are used merely to express the volume of this activity. The overall credit risk and exposure to individual counterparties is monitored. The Company does not anticipate nonperformance by any counterparties. The amount of counterparty credit exposure are the unrealized gains, if any, on such derivative contracts. As collateral in connection with our interest rate swap agreements, at December 31, 2011, the Company had pledged cash of $2.7 million. At

December 31, 2010, the Company had accepted cash of $530,000, pledged cash of $1.5 million, and accepted pledged securities of $2.2 million. At December 31, 2009, the Company had pledged cash of $1.5 million.

Risk Management Instruments. The Company enters into certain derivative contracts to economically hedge state tax credits and certain loans and certificates of deposit.

- Economic hedge of state tax credits. In November 2008, the Company entered into a series of interest rate caps in order to economically hedge changes in fair value of the State tax credits held for sale. The Company paid $2.1 million at inception of the contracts. No principal payments are exchanged. In February 2010, the Company paid $751,000 for an additional series of interest rate caps. See Note 19-Fair Value Measurements for further discussion of the fair value of the state tax credits.
- Economic hedge of prime based loans. At December 31, 2008, the Bank had two outstanding interest rate swap agreements whereby the Company paid a variable rate of interest equivalent to the prime rate and received a fixed rate of interest. The swaps were designed to hedge the cash flows associated with a portfolio of prime based loans.

At December 31, 2008, the Company had recorded $1.3 million in Other assets in the consolidated balance sheet related to the fair value of the interest rate swaps. The effective portion of the change in the derivatives' gain or loss was reported as a component of Accumulated other comprehensive income, net of taxes. The ineffective portion of the change in the cash flow hedge's gain or loss was recorded in operations. On December 16, 2008, the prime rate used to determine the variable rate payments the Bank made to its counterparty was lowered to a rate less than the Bank's prime rate which was used to determine the variable rate receipts from the prime based borrowers. As a result of the variable rate differential, the Company concluded that the cash flow hedges would not be prospectively effective and dedesignated the related interest rate swaps.
The Company reclassified $638,500 from Accumulated other comprehensive income in the consolidated statement of shareholders' equity and comprehensive income into Noninterest income in the consolidated statement of operations for the year ended December 31, 2008. The Company reclassified $162,000 and $242,000 of remaining hedge-related amounts from Accumulated other comprehensive income to operations in 2011 and 2010, respectively. At December 31, 2011, there are no additional amounts remaining in Accumulated other comprehensive income that will be reclassified into operations.
On February 4, 2009, the swaps were terminated. The Company received cash of $861,000, and realized a loss of $530,000. The loss was included in Miscellaneous income in the 2009 consolidated statement of operations.
The table below summarizes the notional amounts and fair values of the derivative instruments used to manage risk.

	Notional Amount		Asset Derivatives (Other Assets) Fair Value		Liability Derivatives (Other Liabilities) Fair Value	
(in thousands)	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010
Non-designated hedging instruments						
Interest rate cap contracts	$80,050	$314,300	$94	$528	$—	$—

The following table shows the location and amount of gains and losses related to derivatives used for risk management purposes that were recorded in the consolidated statements of operations for 2011, 2010 and 2009.

	Location of Gain or (Loss) Recognized in Operations on Derivative	Amount of Gain or (Loss) Recognized in Operations on Derivative		
(in thousands)		2011	2010	2009
Non-designated hedging instruments				
Interest rate cap contracts	Gain on state tax credits, net	$(435)	$(1,340)	$573
Interest rate swap contracts	Miscellaneous income	162	242	(282)

94

Client-Related Derivative Instruments. As an accommodation to certain customers, the Company enters into interest rate swaps to economically hedge changes in fair value of certain loans. In addition, the Company also offers an interest-rate hedge program that includes interest rate swaps to assist its customers in managing their interest-rate risk profile. In order to eliminate the interest-rate risk associated with offering these products, the Company enters into derivative contracts with third parties to offset the customer contracts. The table below summarizes the notional amounts and fair values of the client-related derivative instruments.

(in thousands)	Notional Amount December 31, 2011	Notional Amount December 31, 2010	Asset Derivatives (Other Assets) Fair Value December 31, 2011	Asset Derivatives (Other Assets) Fair Value December 31, 2010	Liability Derivatives (Other Liabilities) Fair Value December 31, 2011	Liability Derivatives (Other Liabilities) Fair Value December 31, 2010
Non-designated hedging instruments						
Interest rate swap contracts	$65,077	$109,012	$1,095	$1,514	$1,796	$2,607

Changes in the fair value of client-related derivative instruments are recognized currently in operations. The following table shows the location and amount of gains and losses recorded in the consolidated statements of operations for 2011, 2010 and 2009.

(in thousands)	Location of Gain or (Loss) Recognized in Operations on Derivative	Amount of Gain or (Loss) Recognized in Operations on Derivative 2011	2010	2009
Non-designated hedging instruments				
Interest rate swap contracts	Interest and fees on loans	$(620)	$(594)	$(579)

NOTE 8 - FIXED ASSETS

A summary of fixed assets at December 31, 2011 and 2010, is as follows:

(in thousands)	December 31, 2011	2010
Land	$2,236	$2,236
Buildings and leasehold improvements	22,370	21,989
Furniture, fixtures and equipment	13,231	12,579
Capitalized software	200	211
	38,037	37,015
Less accumulated depreciation and amortization	19,051	16,516
Total fixed assets	$18,986	$20,499

Depreciation and amortization of building, leasehold improvements, and furniture, fixtures, equipment and capitalized software included in noninterest expense amounted to $2.7 million, $2.9 million, and $3.6 million in 2011, 2010, and 2009, respectively.

The Company has facilities leased under agreements that expire in various years through 2028. The Company's aggregate rent expense totaled $3.0 million, $2.5 million, and $2.4 million in 2011, 2010, and 2009, respectively. Sublease rental income was $150,000, $126,000, and $122,500 for 2011, 2010, and 2009, respectively. For leases which renew or are subject to periodic rental adjustments, the monthly rental payments will be adjusted based on current market conditions and rates of inflation.

The future aggregate minimum rental commitments (in thousands) required under the leases are shown below:

Year	Amount
2012	2,419
2013	1,946
2014	1,934
2015	1,784
2016	2,772
Thereafter	9,850
Total	$20,705

NOTE 9 - GOODWILL AND INTANGIBLE ASSETS

The table below presents a summary of the goodwill for the years ended December 31, 2011, 2010 and 2009.

	Reporting Unit		
(in thousands)	Millennium	Banking	Total
Balance at January 1, 2009	$3,134	$45,378	$48,512
Goodwill impairment related to Banking operating unit	—	(45,378)	(45,378)
Goodwill from purchase of Valley Capital Bank	—	2,064	2,064
Reclassification to assets held for sale	(3,134)	—	(3,134)
Balance at December 31, 2009	—	2,064	2,064
Balance at December 31, 2010	—	2,064	2,064
Goodwill from purchase of Legacy Bank	—	1,558	1,558
Goodwill from purchase of The First National Bank of Olathe	—	26,712	26,712
Balance at December 31, 2011	$—	$30,334	$30,334

Due primarily to the deterioration in the general economic environment and the resulting decline in the Company's share price and market capitalization, at March 31, 2009, the impairment analysis determined that the carrying value of the reporting unit was higher than the fair value of the reporting unit, which resulted in a non-cash goodwill impairment charge of $45.4 million, thus eliminating all goodwill in the Banking operating unit at that time. This impairment charge did not reduce the Company's regulatory capital or cash flows. The Company also tested the Banking reporting unit core deposit intangibles for impairment and determined there was no impairment.

The annual goodwill impairment evaluation in 2010 and 2011 did not identify any impairment at the Banking unit.

The table below presents a summary of the intangible assets for the years ended December 31, 2011, 2010 and 2009.

(in thousands)	Customer and Trade Name Intangibles	Core Deposit Intangible	Net Intangible
Balance at January 1, 2009	$1,379	$2,125	$3,504
Reclassification to assets held for sale	(783)	—	(783)
Amortization expense	(596)	(482)	(1,078)
Balance at December 31, 2009	—	1,643	1,643
Amortization expense	—	(420)	(420)
Balance at December 31, 2010	—	1,223	1,223
Intangibles from purchase of Legacy Bank	—	833	833
Intangibles from purchase of The First National Bank of Olathe	—	7,905	7,905
Intangibles from purchase of Bank Liberty	—	323	323
Amortization expense	—	(999)	(999)
Balance at December 31, 2011	$—	$9,285	$9,285

The following table reflects the expected amortization schedule for the core deposit intangible (in thousands) at December 31, 2011.

Year	Core Deposit Intangible
2012	$1,879
2013	1,653
2014	1,426
2015	1,199
2016	973
After 2016	2,155
	$9,285

NOTE 10 - MATURITY OF CERTIFICATES OF DEPOSIT

Following is a summary of certificates of deposit maturities at December 31, 2011:

(in thousands)	$100,000 and Over	Other	Total
Less than 1 year	$278,326	$153,035	$431,361
Greater than 1 year and less than 2 years	126,484	46,619	173,103
Greater than 2 years and less than 3 years	24,211	21,927	46,138
Greater than 3 years and less than 4 years	73,087	24,527	97,614
Greater than 4 years and less than 5 years	48,427	20,218	68,645
Over 5 years	—	60	60
	$550,535	$266,386	$816,921

NOTE 11 - SUBORDINATED DEBENTURES

The Corporation has nine unconsolidated statutory business trusts. These trusts issued preferred securities that were sold to third parties. The sole purpose of the trusts was to invest the proceeds in junior subordinated debentures of the Company that have terms identical to the trust preferred securities.

The amounts and terms of each respective issuance at December 31, 2011 and 2010 were as follows:

(in thousands)	Amount 2011	2010	Maturity Date	Call Date	Interest Rate
EFSC Clayco Statutory Trust I	$3,196	$3,196	December 17, 2033	December 17, 2008	Floats @ 3MO LIBOR + 2.85%
EFSC Capital Trust II	5,155	5,155	June 17, 2034	June 17, 2009	Floats @ 3MO LIBOR + 2.65%
EFSC Statutory Trust III	11,341	11,341	December 15, 2034	December 15, 2009	Floats @ 3MO LIBOR + 1.97%
EFSC Clayco Statutory Trust II	4,124	4,124	September 15, 2035	September 15, 2010	Floats @ 3MO LIBOR + 1.83%
EFSC Statutory Trust IV	10,310	10,310	December 15, 2035	December 15, 2010	Floats @ 3MO LIBOR + 1.44%
EFSC Statutory Trust V	4,124	4,124	September 15, 2036	September 15, 2011	Floats @ 3MO LIBOR + 1.60%
EFSC Capital Trust VI	14,433	14,433	March 30, 2037	March 30, 2012	Fixed for 5 years @ 6.573%(1)
EFSC Capital Trust VII	4,124	4,124	December 15, 2037	December 15, 2012	Floats @ 3MO LIBOR + 2.25%
EFSC Capital Trust VIII	25,774	25,774	December 15, 2038	December 15, 2013	Fixed @ 9%
Total trust preferred securities	82,581	82,581			
Bank Subordinated notes	2,500	2,500	October 1, 2018	October 1, 2013	Fixed @ 10%
Total Subordinated debentures	$85,081	$85,081			

(1) After the March 2012 payment, floats @ 3MO LIBOR + 1.60%

The subordinated debentures, which are the sole assets of the trusts, are subordinate and junior in right of payment to all present and future senior and subordinated indebtedness and certain other financial conditions of the Company. The Company fully and unconditionally guarantees each trust's securities obligations. The trust preferred securities are included in Tier 1 capital for regulatory capital purposes, subject to certain limitations.

The securities are redeemable in whole or in part on or after their respective call dates. Mandatory redemption dates may be shortened if certain conditions are met. The securities are classified as subordinated debentures in the Company's consolidated balance sheets. Interest on the subordinated debentures held by the trusts is recorded as interest expense in the Company's consolidated statements of operations. The Company's investment in these trusts is included in other investments in the consolidated balance sheets.

The trust preferred securities issued through EFSC Capital Trust VIII are convertible into 1,439,263 shares of the Company's common stock at a conversion price of $17.37. After December 15, 2010, if the Company's common stock price per share exceeds $22.58 for 20 consecutive trading days, upon written notice, the Company can force the holders to convert or lose their conversion rights. An entity managed and controlled by a former member of the Company's Board of Directors purchased $5.0 million of the convertible trust preferred securities of EFSC Capital Trust VIII on December 12, 2008. Certain current directors still have a nominal interest in this entity.

NOTE 12 - FEDERAL HOME LOAN BANK ADVANCES

FHLB advances are collateralized by 1-4 family residential real estate loans, business loans and certain commercial real estate loans. At December 31, 2011 and 2010, the carrying value of the loans pledged to the FHLB of Des Moines was $469.0 million and $434.0 million, respectively. The secured line of credit had availability of approximately $139.4 million at December 31, 2011.

Enterprise also has a $7.9 million investment in the capital stock of the FHLB of Des Moines and a $1.6 million investment in the capital stock of the FHLB of San Francisco at December 31, 2011.

The following table summarizes the type, maturity and rate of the Company's FHLB advances at December 31:

(in thousands)	Term	2011 Outstanding Balance	Weighted Rate		2010 Outstanding Balance	Weighted Rate	
Long term non-amortizing fixed advance	less than 1 year	$22,000	2.90	%	$5,300	2.04	%
Long term non-amortizing fixed advance	1 - 2 years	—	—	%	22,000	2.90	%
Long term non-amortizing fixed advance	3 - 4 years	10,000	4.53	%	—	—	%
Long term non-amortizing fixed advance	4 - 5 years	—	—	%	10,000	4.53	%
Long term non-amortizing fixed advance	5 - 10 years	70,000	3.37	%	70,000	3.37	%
Total Federal Home Loan Bank Advances		$102,000	3.38	%	$107,300	3.32	%

All FHLB advances have fixed interest rates. At December 31, 2011, all of the advances are pre-payable by the Company at anytime, subject to prepayment penalties. Of the advances with a term of five to ten years, $70.0 million were callable by the FHLB as of December 31, 2011. In addition to the above advances, at December 31, 2011, the Company also had used $24.7 million of collateral value to secure confirming letters of credit for public unit deposits and industrial development bonds.

NOTE 13 - OTHER BORROWINGS AND NOTES PAYABLE

A summary of other borrowings is as follows:

(in thousands)	December 31, 2011		2010	
Securities sold under repurchase agreements	$154,545		$119,333	
Average balance during the year	$103,392		$58,737	
Maximum balance outstanding at any month-end	154,545		119,333	
Weighted average interest rate during the year	0.42	%	0.45	%
Weighted average interest rate at December 31	0.45	%	0.44	%

Federal Reserve line
The Bank also has a line with the Federal Reserve Bank of St. Louis for back-up liquidity purposes. As of December 31, 2011, approximately $379.6 million was available under this line. This line is secured by a pledge of certain eligible loans aggregating approximately $622.3 million.

NOTE 14 - LITIGATION AND OTHER CLAIMS

The Company and its subsidiaries are, from time to time, parties to various legal proceedings arising out of their businesses. Other than those described below, management believes that there are no such proceedings pending or threatened against the Company or its subsidiaries which, if determined adversely, would have a material adverse effect on the business, consolidated financial condition, results of operations or cash flows of the Company or any of its subsidiaries.

Distinctive Notes
The Bank, along with other co-defendants has been named as a defendant in two lawsuits filed by persons alleging to be clients of the Bank’s Trust division who invested in promissory notes (the "Distinctive Notes") issued by Distinctive Properties (UK) Limited (“Distinctive Properties”), a company involved in the purchase and development of real estate in the United Kingdom. The Company is unable to estimate a reasonably possible loss for the cases described below because the proceedings are in early stages and there are significant factual issues to be determined and resolved in each case. The Company denies plaintiffs’ allegations and intends to vigorously defend the lawsuits.

Rosemann, et al. v. Martin Sigillito, et al.
In one of the lawsuits, the plaintiffs allege that the investments in the Distinctive Notes were part of a multi-million dollar Ponzi scheme. Plaintiffs allege to hold such promissory notes in accounts with the Trust division and that, among other things, the Bank was negligent, breached its fiduciary duties and breached its contracts. Plaintiffs also allege that the Bank violated the Racketeer Influenced and Corrupt Organizations Act (“RICO”). Plaintiffs, in the aggregate, are seeking damages from defendants, including the Bank, in excess of $25.0 million as well as their costs and attorneys’ fees and trebled damages under RICO.

On June 6, 2011, the Bank filed a Motion to Dismiss the Complaint. On July 1, 2011, the United States moved to intervene in the case for purposes of securing a stay of the case pending completion of it's criminal case against two of the individual defendants. The stay was granted on August 4, 2011. On October 31, 2011, the court granted the Bank's motion to dismiss the plaintiffs claims that the Bank violated RICO and that the Bank breached its fiduciary duties to the plaintiffs. The court granted the plaintiffs leave to amend the dismissed claims. However, the court denied the Bank's motion to dismiss the claims that the Bank conspired with others to violate RICO, breached its agreements with the plaintiffs and that the Bank was negligent in performing its duties as custodian of the IRAs that held the Distinctive Notes. As a result of the stay, all discovery in the case may be put on hold for the duration of the criminal proceedings; however, further procedural actions may continue to be ruled upon by the court. On January 2, 2012, the plaintiffs filed their second amended complaint which reasserts the claim that the Bank violated RICO, however the claim of breach of fiduciary duty was not reasserted. Criminal proceedings in the case began on March 19, 2012. After a four week trial, the jury found Sigillito guilty of 20 counts of wire fraud, mail fraud, and conspiracy and money laundering. Following the verdict, the Judge lifted the stay and has scheduled a Rule 16 conference in the civil case for May 31, 2012. The Court is expected to set the case for trial at the Rule 16 conference.

BJD, LLC and Barbara Dunning v. Enterprise Bank & Trust, et. al.
The Bank has also been named as a defendant in this case, relating to BJD’s investment in the Distinctive Notes. Plaintiffs allege that the Bank, and the other defendants breached their fiduciary duties and were negligent in allowing plaintiffs to invest in the Distinctive Notes because the loan program was allegedly never funded and the assets of the borrower did not exist or were overvalued. Plaintiffs are seeking approximately $800,000 in damages, 9% interest, punitive damages, attorneys’ fees and costs.

On June 16, 2011, the Bank filed a motion to compel arbitration and stay proceedings in the Circuit Court. On July 11, 2011, the U.S. Attorney's Office moved to intervene in this case as well for purposes of seeking a stay of certain discovery pending completion of the above described criminal proceedings. The Court never formally issued a stay order; however, the conclusion of the criminal trial on April 13, 2012, renders the U.S. Attorney's motion moot. The Court has granted the Bank's motion to compel arbitration and stay proceedings and has scheduled a Case Management Conference for May 10, 2012.

William Mark Scott v. Enterprise Financial Services Corp, et. al.
On April 10, 2012, a putative class action was filed in the United States District Court for the Eastern District of Missouri captioned William Mark Scott v. Enterprise Financial Services Corp, Peter F. Benoist, and Frank H. Sanfilippo. The complaint asserts claims for violation of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 on behalf of a putative class of purchasers of the Company's stock between April 20, 2010 and January 25, 2012, inclusive. The complaint alleges, among other things, that defendants allegedly made false and misleading statements and allegedly "failed to disclose that the Company was improperly recording income on loans covered under loss share agreements with the FDIC" and that, as a result, "the Company's financial statements were materially false and misleading at all relevant times." The action seeks unspecified damages and costs and expenses. The Company is unable to estimate a reasonably possible loss for the case because the proceeding is in an early stage and there are significant factual issues to be determined and resolved. The Company denies plaintiffs' allegations and intends to vigorously defend the lawsuit.

NOTE 15-REGULATORY MATTERS

The Company and the Bank are subject to various regulatory capital requirements administered by the Federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the financial statements of the Company and the Bank. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of 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 ratios (set forth in the following table) of total and Tier 1 capital to risk-weighted assets, and of Tier 1 capital to average assets. Management believes, as of December 31, 2011 and 2010, that the Bank met all capital adequacy requirements to which they are subject.

As of December 31, 2011 and 2010, the Bank was categorized as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized" the Bank must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table.

The actual capital amounts and ratios are also presented in the table below.

(in thousands)	Actual Amount	Actual Ratio		For Capital Adequacy Purposes Amount	For Capital Adequacy Purposes Ratio		To Be Well Capitalized Under Applicable Action Provisions Amount	To Be Well Capitalized Under Applicable Action Provisions Ratio	
As of December 31, 2011:									
Total Capital (to Risk Weighted Assets)									
Enterprise Financial Services Corp	$306,996	13.78	%	$178,237	8.00	%	$—	—	%
Enterprise Bank & Trust	267,717	12.06		177,565	8.00		221,956	10.00	
Tier 1 Capital (to Risk Weighted Assets)									
Enterprise Financial Services Corp	276,275	12.40		89,118	4.00		—	—	
Enterprise Bank & Trust	237,326	10.69		88,783	4.00		133,174	6.00	
Tier 1 Capital (to Average Assets)									
Enterprise Financial Services Corp	276,275	8.26		100,387	3.00		—	—	
Enterprise Bank & Trust	237,326	7.09		100,387	3.00		167,311	5.00	
As of December 31, 2010:									
Total Capital (to Risk Weighted Assets)									
Enterprise Financial Services Corp	$285,226	14.11	%	$161,691	8.00	%	$—	—	%
Enterprise Bank & Trust	251,149	12.51		160,642	8.00		200,802	10.00	
Tier 1 Capital (to Risk Weighted Assets)									
Enterprise Financial Services Corp	237,099	11.73		80,845	4.00		—	—	
Enterprise Bank & Trust	223,330	11.12		80,321	4.00		120,481	6.00	
Tier 1 Capital (to Average Assets)									
Enterprise Financial Services Corp	237,099	8.99		79,127	3.00		—	—	
Enterprise Bank & Trust	223,330	8.51		78,707	3.00		131,179	5.00	

NOTE 16 - COMPENSATION PLANS

The Company has adopted share-based compensation plans to reward and provide long-term incentive for directors and key employees of the Company. These plans provide for the granting of stock, stock options, stock-settled stock appreciation rights ("SSARs"), and restricted stock units (“RSUs”), as designated by the Company's Board of Directors upon the recommendation of the Compensation Committee. The Company uses authorized and unissued shares to satisfy share award exercises. During 2011, share-based compensation was issued in the form of restricted stock. There were no options or SSARs granted in 2011. At December 31, 2011, there were 637,241 shares available for grant under the various share-based compensation plans.

Total share-based compensation expense that was charged against income was $1.8 million, $2.3 million, and $2.2 million for the years ended December 31, 2011, 2010, and 2009 respectively. The total income tax expense recognized in Additional paid in capital for share-based compensation arrangements was $53,000, $494,000, and $338,000 for the years ended December 31, 2011, 2010, and 2009, respectively.

Employee Stock Options and Stock-settled Stock Appreciation Rights
In determining compensation cost for stock options and SSARs, the Black-Scholes option-pricing model is used to estimate the fair value on date of grant. The Black-Scholes model is a closed-end model that uses the assumptions in the following table. The risk-free rate for the expected term is based on the U.S. Treasury zero-coupon spot rates in effect at the time of grant. Expected volatility is based on historical volatility of the Company's common stock. The

Company uses historical exercise behavior and other factors to estimate the expected term of the options, which represents the period of time that the options granted are expected to be outstanding.

	2011	2010	2009
Risk-free interest rate	NA	2.1 %	2.5 %
Expected dividend rate	NA	0.6 %	0.6 %
Expected volatility	NA	56.8 %	54.8 %
Expected term	NA	6 years	6 years

Stock options have been granted to key employees with exercise prices equal to the market price of the Company's common stock at the date of grant and 10-year contractual terms. Stock options have a vesting schedule of three to five years. In 2007, the Company began granting SSARs to key employees. The SSARs are subject to continued employment, have a 10-year contractual term and vest ratably over five years. Neither stock options nor SSARs carry voting or dividend rights until exercised. At December 31, 2011, there was $898,000 of total unrecognized compensation cost related to SSARs which is expected to be recognized over a weighted average period of 2.3 years. Various information related to the stock options and SSARs is shown below.

(in thousands, except grant date fair value)	2011	2010	2009
Weighted average grant date fair value of options and SSARs	NA	$10.24	$8.99
Compensation expense	911	908	896
Intrinsic value of option exercises on date of exercise	132	—	1
Cash received from the exercise of stock options	889	—	15

Following is a summary of the employee stock option and SSAR activity for 2011.

(Dollars in thousands, except share data)	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2011	902,932	$15.71		
Granted	—	—		
Exercised	(75,112)	11.83		
Forfeited	(28,836)	14.31		
Outstanding at December 31, 2011	798,984	$16.13	4.9 years	$—
Exercisable at December 31, 2011	624,121	$16.85	4.1 years	$—
Vested and expected to vest at December 31, 2011	708,365	$15.67	4.9 years	$—

Restricted Stock Units (“RSU”)

As part of a long-term incentive plan, the Company awards nonvested stock, in the form of RSUs to employees. RSUs are subject to continued employment and vest ratably over five years. RSUs do not carry voting or dividend rights until vested. Sales of the units are restricted prior to vesting. Various information related to the RSUs is shown below.

(in thousands)	2011	2010	2009
Compensation expense	$555	$1,038	$1,138
Total fair value at vesting date	331	389	417
Total unrecognized compensation cost for nonvested stock units	273	827	1,879
Expected years to recognize unearned compensation	0.9 years	1.6 years	2.2 years

103

A summary of the status of the Company's RSU awards as of December 31, 2011 and changes during the year then ended is presented below.

	Shares	Weighted Average Grant Date Fair Value
Outstanding at January 1, 2011	36,173	$22.43
Granted	—	—
Vested	(22,111)	23.10
Forfeited	(1,512)	21.58
Outstanding at December 31, 2011	12,550	$21.38

Stock Plan for Non-Management Directors

In 2006, the Company adopted a Stock Plan for Non-Management Directors, which provides for issuing shares of common stock to non-employee directors as compensation in lieu of cash. The plan was approved by the shareholders and allows up to 100,000 shares to be awarded. At December 31, 2011, there were 19,622 shares of stock were available for issuance under the Stock Plan for Non-Management Directors. Shares are issued twice a year and compensation expense is recorded as the shares are earned, therefore, there is no unrecognized compensation cost related to this plan. In 2011, the Company issued 19,830 shares of stock at a weighted average fair value of $12.90 per share. In 2010, the Company issued 25,888 shares of stock at a weighted average fair value of $9.93 per share. In 2009, the Company issued 17,015 shares of stock at a weighted average fair value of $9.86 per share. The Company recognized $256,000, $257,000 and $168,000 of stock-based compensation expense for the shares issued to the directors in 2011, 2010 and 2009, respectively.

Employee Stock Issuance

Restricted stock was issued to certain key employees as part of their compensation. The restricted stock may be in a form of a one-time award or paid in pro rata installments. The stock is restricted for at least 2 years and upon issuance may be fully vested or vest over five years. The Company recognized $29,700 and $51,700 of stock-based compensation expense for the shares issued to the employees in 2011 and 2010, respectively. The Company issued 6,724 and 8,999 shares in 2011 and 2010, respectively.

In conjunction with the Company’s short-term incentive plan, the Company issued 14,329 and 13,660 restricted shares to certain key employees in 2011 and 2010, respectively. The compensation expense related to these shares was expensed in 2011 and 2010, respectively. For further information on the short-term incentive plan, refer to the Compensation Discussion and Analysis in the Company’s Proxy Statement for the 2012 Annual Meeting of Stockholders.

Moneta Plan

In 1997, the Company entered into a solicitation and referral agreement with Moneta Group, Inc. (“Moneta”), a nationally recognized firm in the financial planning industry. There have been no options granted to Moneta under the agreement since 2003. The fair value of each option granted to Moneta was estimated on the date of grant using the Black-Scholes option pricing model. The Company recognized the fair value of the options over the vesting period as expense. As of December 31, 2006, the fair value of all Moneta options had been recognized.

Following is a summary of the Moneta stock option activity for 2011.

(Dollars in thousands, except share data)	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2011	26,105	$13.58		
Granted	—	—		
Exercised	(9,217)	11.70		
Forfeited	(8,792)	15.50		
Outstanding at December 31, 2011	8,096	$13.65	0.5 years	$9
Exercisable at December 31, 2011	8,096	$13.65	0.5 years	$9

401(k) plans

Effective January 1, 1993, the Company adopted a 401(k) thrift plan which covers substantially all full-time employees over the age of 21. The amount charged to expense for the Company's contributions to the plan was $1.1 million, $468,000 and $349,000 for 2011, 2010, and 2009, respectively. Approximately $320,000 of the 2011 expense is related to an accrual for the Internal Revenue Service ("IRS") Voluntary Correction Program. Upon approval by the IRS, this payment will be made to the 401(k) plan participants.

NOTE 17-INCOME TAXES

The components of income tax (benefit) expense for the years ended December 31 are as follows:

	Years ended December 31,		
(in thousands)	2011	2010	2009
Current:			
Federal	$10,775	$(44)	$(383)
State and local	1,907	101	(433)
Deferred	(733)	766	(2,545)
Total income tax expense (benefit)	$11,949	$823	$(3,361)
Income tax expense (benefit) is included in the financial statements as follows:			
Continuing operations	$11,949	$823	$(2,650)
Discontinued operations	—	—	(711)
Total income tax expense (benefit)	$11,949	$823	$(3,361)

A reconciliation of expected income tax (benefit) expense, computed by applying the statutory federal income tax rate of 35% in 2011, 2010, and 2009 to income before income taxes and the amounts reflected in the consolidated statements of operations is as follows:

	Years ended December 31,		
(in thousands)	2011	2010	2009
Income tax expense (benefit) at statutory rate	$13,080	$2,239	$(17,961)
Increase (reduction) in income tax resulting from:			
Tax-exempt income, net	(717)	(527)	(597)
Goodwill write off	—	—	15,882
State and local income taxes, net	994	67	(282)
Non-deductible expenses	65	292	187
Federal income tax credits	(749)	(749)	—
Change in estimated rate for deferred taxes	(1,180)	—	—
Other, net	456	(499)	(590)
Total income tax expense (benefit)	$11,949	$823	$(3,361)

A net deferred income tax asset of $16.0 million and $17.7 million is included in other assets in the consolidated balance sheets at December 31, 2011 and 2010, respectively. The tax effect of temporary differences that gave rise to significant portions of the deferred tax assets and deferred tax liabilities is as follows:

	Years ended December 31,	
(in thousands)	2011	2010
Deferred tax assets:		
Allowance for loan losses	$15,414	$15,564
Asset purchase tax basis difference, net	52,881	32,751
Basis difference on other real estate	1,382	2,740
Deferred compensation	2,272	1,723
Goodwill and other intangible assets	18,341	227
Tax credit carryforwards	—	497
Unrealized losses on securities available for sale	—	223
Other, net	347	206
State valuation allowance	(320)	—
Total deferred tax assets	$90,317	$53,931
Deferred tax liabilities:		
FDIC loss guarantee receivable, net	$66,606	$33,812
Unrealized gains on securities available for sale	2,189	—
State tax credits held for sale, net of economic hedge	1,903	1,674
Core deposit intangibles	3,487	445
Office equipment and leasehold improvements	87	320
Total deferred tax liabilities	74,272	36,251
Net deferred tax asset	$16,045	$17,680

A valuation allowance is provided on deferred tax assets when it is more likely than not that some portion of the assets will not be realized. The Company did not have any valuation allowances for federal income taxes as of December 31, 2011 or December 31, 2010. Management believes it is more likely than not that the results of future operations will

generate sufficient federal taxable income to realize the deferred federal tax assets. The Company had a state valuation allowance of $320,000 as of December 31, 2011 and $0 as of December 31, 2010.

The Company, or one of its subsidiaries, files income tax returns in the federal jurisdiction and in six states. With few exceptions, the Company is no longer subject to federal, state or local income tax audits by tax authorities for years before 2008. The Company is not currently under audit by any taxing jurisdiction.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense and classifies such interest and penalties in the liability for unrecognized tax benefits. As of December 31, 2011, the Company had approximately $114,000 accrued for interest and penalties.

As of December 31, 2011, the gross amount of unrecognized tax benefits was $1.1 million and the total amount of net unrecognized tax benefits that would impact the effective tax rate, if recognized, was $741,000. As of December 31, 2010 and 2009, the total amount of the net unrecognized tax benefits that would impact the effective tax rate, if recognized, was $861,000 and $946,000, respectively. The Company believes it is reasonably possible that the gross amount of unrecognized benefits will be reduced by approximately $305,000 as a result of a lapse of statue of limitations.

The activity in the gross liability for unrecognized tax benefits was as follows:

(in thousands)	2011	2010	2009
Balance at beginning of year	$4,003	$1,337	$1,690
Additions based on tax positions related to the current year	311	270	142
Additions for tax positions of prior years	38	2,884	180
Reductions for tax positions of prior years	(2,849)	—	—
Settlements or lapse of statute of limitations	(446)	(488)	(675)
Balance at end of year	$1,057	$4,003	$1,337

NOTE 18 - COMMITMENTS AND CONTINGENCIES

The Company issues financial instruments with off balance sheet risk in the normal course of the business of meeting the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments may involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the consolidated balance sheets.

The Company’s extent of involvement and maximum potential exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of these instruments.

The Company uses the same credit policies in making commitments and conditional obligations as it does for financial instruments included on its consolidated balance sheets. At December 31, 2011 there were $1.3 million of unadvanced commitments on impaired loans. Other liabilities include approximately $257,000 for estimated losses attributable to the unadvanced commitments on impaired loans. At December 31, 2010 there were $1.4 million of unadvanced commitments on impaired loans. Other liabilities include approximately $280,000 for estimated losses attributable to the unadvanced commitments on impaired loans.

The contractual amounts of off-balance-sheet financial instruments as of December 31, 2011 and 2010 are as follows:

(in thousands)	December 31, 2011	December 31, 2010
Commitments to extend credit	$547,657	$429,411
Standby letters of credit	43,973	42,113

107

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 usually have fixed expiration dates or other termination clauses and may require payment of a fee. Of the total commitments to extend credit at December 31, 2011 and December 31, 2010, approximately $75.7 million and $67.0 million, respectively, represent fixed rate loan commitments. Since certain of the commitments may 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 borrower. Collateral held varies, but may include accounts receivable, inventory, premises and equipment, and real estate.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. These standby letters of credit are issued to support contractual obligations of the Company's customers. The credit risk involved in issuing letters of credit is essentially the same as the risk involved in extending loans to customers. The approximate remaining term of standby letters of credit range from 6 months to 5 years at December 31, 2011.

Contingencies
See Note 14 - Litigation and Other Claims for information on contingencies.

NOTE 19 - FAIR VALUE MEASUREMENTS

The fair value of an asset or liability is the price that would be received to sell that asset or paid to transfer that liability in an orderly transaction occurring in the principal market (or most advantageous market in the absence of a principal market) for such asset or liability. In estimating fair value, the Company utilizes valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Such valuation techniques are consistently applied. Inputs to valuation techniques include the assumptions that market participants would use in pricing an asset or liability. ASC Topic 820, "Fair Value Measurements and Disclosures," establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

- Level 1 Inputs - Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

- Level 2 Inputs - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.

- Level 3 Inputs - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

Fair value on a recurring basis

The following table summarizes financial instruments measured at fair value on a recurring basis as of December 31, 2011 and 2010, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value.

	December 31, 2011			
(in thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Assets				
Securities available for sale				
Obligations of U.S. Government sponsored enterprises	$—	$126,917	$—	$126,917
Obligations of states and political subdivisions	—	36,810	3,027	39,837
Residential mortgage-backed securities	—	422,692	3,736	426,428
Total securities available for sale	$—	$586,419	$6,763	$593,182
Portfolio loans	—	14,270	—	14,270
State tax credits held for sale	—	—	26,350	26,350
Derivative financial instruments	—	1,189	—	1,189
Total assets	$—	$601,878	$33,113	$634,991
Liabilities				
Derivative financial instruments	$—	$1,796	$—	$1,796
Total liabilities	$—	$1,796	$—	$1,796

	December 31, 2010			
(in thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Assets				
Securities available for sale				
Obligations of U.S. Government agencies	$—	$453	$—	$453
Obligations of U.S. Government sponsored enterprises	—	27,564	4,555	32,119
Obligations of states and political subdivisions	—	14,711	2,965	17,676
Residential mortgage-backed securities	—	311,298	—	311,298
Total securities available for sale	$—	$354,026	$7,520	$361,546
Portfolio loans	—	16,068	—	16,068
State tax credits held for sale	—	—	31,576	31,576
Derivative financial instruments	—	2,042	—	2,042
Total assets	$—	$372,136	$39,096	$411,232
Liabilities				

Derivative financial instruments	$—	$2,607	$—	$2,607
Total liabilities	$—	$2,607	$—	$2,607

- Securities available for sale. Securities classified as available for sale are reported at fair value utilizing Level 2 and Level 3 inputs. The Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions. At December 31, 2011, Level 3 securities available for sale include three Auction Rate Securities, a municipal bond issued by a school district and a newly issued residential mortgage-backed security.

- Portfolio Loans. Certain fixed rate portfolio loans are accounted for as trading instruments and reported at fair value. Fair value on these loans is determined using a third party valuation model with observable Level 2 market data inputs.
- State tax credits held for sale. At December 31, 2011, of the $50.4 million of state tax credits held for sale on the consolidated balance sheet, approximately $26.4 million were carried at fair value. The remaining $24.0 million of state tax credits were accounted for at cost. The Company elected not to account for the state tax credits purchased in 2010 and 2011 at fair value in order to limit the volatility of the fair value changes in our consolidated statements of operations.

The Company is not aware of an active market that exists for the 10-year streams of state tax credit financial instruments. However, the Company’s principal market for these tax credits consists of Missouri state residents who buy these credits and from local and regional accounting firms who broker them. As such, the Company employed a discounted cash flow analysis (income approach) to determine the fair value.

The fair value measurement is calculated using an internal valuation model with observable market data including discounted cash flows based upon the terms and conditions of the tax credits. Assuming that the underlying project remains in compliance with the various federal and state rules governing the tax credit program, each project will generate about 10 years of tax credits. The inputs to the fair value calculation include: the amount of tax credits generated each year, the anticipated sale price of the tax credit, the timing of the sale and a discount rate. The discount rate is defined as the LIBOR swap curve at a point equal to the remaining life in years of credits plus a 205 basis point spread. With the exception of the discount rate, the other inputs to the fair value calculation are observable and readily available. The discount rate is considered a Level 3 input because it is an “unobservable input” and is based on the Company’s assumptions. Given the significance of this input to the fair value calculation, the state tax credit assets are reported as Level 3 assets.

Economically, the Company equates the state tax credits to a fixed rate loan. After considering various risks, such as credit risk, compliance risk, and recapture risk, management concluded the state tax credits are equivalent to a fixed rate loan priced at Prime minus 75 basis points. When pricing a fixed rate loan, most banks utilize the Prime-based swap curve, which is based on the LIBOR swap curve plus a prime equivalent spread of 265 to 285 basis points depending on market pricing and the maturity of the underlying loan. The Prime-based swap curve is available daily on Bloomberg or other national pricing services. As a result, at December 31, 2011 and 2010, management concluded the spread of 205 basis points (prime equivalent spread of 285 basis points minus 75 basis points) to the LIBOR curve should be utilized in the fair value calculation.

At December 31, 2011, the discount rates utilized in our state tax credits fair value calculation ranged from 2.63% to 4.08%. Resulting changes in the fair value of the state tax credits held for sale increased Gain on state tax credits in the consolidated statement of operations by $436,000 for the year ended December 31, 2011.

- Derivatives. Derivatives are reported at fair value utilizing Level 2 inputs. The Company obtains counterparty quotations to value its interest rate swaps and caps. In addition, the Company validates the counterparty quotations with third party valuation sources. Derivatives with negative fair values are included in Other liabilities in the consolidated balance sheets. Derivatives with positive fair value are included in Other assets in the consolidated balance sheets.

Level 3 financial instruments

The following table presents the changes in Level 3 financial instruments measured at fair value as of December 31, 2011 and 2010.

- Purchases, sales, issuances and settlements, net. Purchases of Level 3 financial instruments during the year ended December 31, 2011 include a newly issued residential mortgage-backed security.

Transfers in and/or out of Level 3. The transfer out of Level 3 is related to two newly issued mortgage-backed securities purchased in the fourth quarter of 2010 which were originally priced using Level 3 assumptions. In the first quarter of 2011, a third party pricing service became available.

	Securities available for sale, at fair value	
	Years ended December 31,	
(in thousands)	2011	2010
Beginning balance	$7,520	$2,830
Total gains (losses):		
Included in other comprehensive income	(1,126)	(427)
Purchases, sales, issuances and settlements:		
Purchases	4,924	15,529
Transfer in and/or out of Level 3	(4,555)	(10,412)
Ending balance	$6,763	$7,520
Change in unrealized gains relating to assets still held at the reporting date	$(1,126)	$(427)

	State tax credits held for sale	
	Years ended December 31,	
(in thousands)	2011	2010
Beginning balance	$31,576	$32,485
Total gains:		
Included in earnings	2,292	2,544
Purchases, sales, issuances and settlements:		
Sales	(7,518)	(3,453)
Ending balance	$26,350	$31,576
Change in unrealized gains relating to assets still held at the reporting date	$436	$1,685

Fair value on a non-recurring basis

Certain financial assets and financial liabilities are measured at fair value on a non-recurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

Impaired loans. Impaired loans are included as Portfolio loans on the Company's consolidated balance sheets with amounts specifically reserved for credit impairment in the Allowance for loan losses. From time to time, fair value adjustments are recorded on impaired loans to reflect (1) partial write-downs that are based on the current appraised or market-quoted value of the underlying collateral or (2) the full charge-off of the loan carrying value. In some cases, the properties for which market quotes or appraised values have been obtained are located in areas where comparable sales data is limited, outdated, or unavailable. In addition, the Company may adjust the valuations based on other relevant market conditions or information. Accordingly, fair value estimates, including those obtained from real estate brokers or other third-party consultants, for collateral-dependent impaired loans are classified in Level 3 of the valuation hierarchy.

- Other Real Estate. These assets are reported at the lower of the loan carrying amount at foreclosure or fair value less estimated costs to sell. Fair value is based on third party appraisals of each property and the Company's

111

judgment of other relevant market conditions. These are considered Level 3 inputs.

The following table presents financial instruments and non-financial assets measured at fair value on a non-recurring basis as of December 31, 2011 and 2010.

	December 31, 2011				
	(1)	(1)	(1)	(1)	
(in thousands)	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total (losses) gains for the year ended December 31, 2011
Impaired loans	$15,927	$—	$—	$15,927	$(21,330)
Other real estate	14,382	—	—	14,382	(4,702)
Total	$30,309	$—	$—	$30,309	$(26,032)

	December 31, 2010				
	(1)	(1)	(1)	(1)	
(in thousands)	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total (losses) gains for the year ended December 31, 2010
Impaired loans	$14,542	$—	$—	$14,542	$(36,160)
Other real estate	14,886	—	—	14,886	(5,710)
Total	$29,428	$—	$—	$29,428	$(41,870)

(1) The amounts represent only balances measured at fair value during the period and still held as of the reporting date.

Carrying amount and fair value at December 31, 2011 and 2010

Following is a summary of the carrying amounts and fair values of the Company's financial instruments on the consolidated balance sheets at December 31, 2011 and 2010.

(in thousands)	December 31, 2011 Carrying Amount	December 31, 2011 Estimated fair value	December 31, 2010 Carrying Amount	December 31, 2010 Estimated fair value
Balance sheet assets				
Cash and due from banks	$20,791	$20,791	$23,413	$23,413
Federal funds sold	143	143	3,153	3,153
Interest-bearing deposits	168,711	168,711	268,853	268,853
Securities available for sale	593,182	593,182	361,546	361,546
Other investments, at cost	14,527	14,527	12,278	12,278
Loans held for sale	6,494	6,494	5,640	5,640
Derivative financial instruments	1,189	1,189	2,042	2,042
Portfolio loans, net	2,158,060	2,163,723	1,845,162	1,850,197
State tax credits, held for sale	50,446	50,446	61,148	61,148
Accrued interest receivable	9,193	9,193	7,464	7,464
Balance sheet liabilities				
Deposits	2,791,353	2,804,044	2,297,721	2,301,387
Subordinated debentures	85,081	42,252	85,081	44,866
Federal Home Loan Bank advances	102,000	110,575	107,300	118,602
Other borrowings	154,545	154,561	119,333	119,366
Derivative financial instruments	1,796	1,796	2,607	2,607
Accrued interest payable	1,762	1,762	1,488	1,488

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

Cash, Federal funds sold, and other short-term instruments

For cash and due from banks, federal funds purchased, interest-bearing deposits, and accrued interest receivable (payable), the carrying amount is a reasonable estimate of fair value, as such instruments reprice in a short time period.

Securities available for sale

The Company obtains fair value measurements for available for sale debt instruments from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions.

Other investments

Other investments, which primarily consists of membership stock in the FHLB is reported at cost, which approximates fair value.

Loans held for sale

These loans consist of mortgages that sold on the secondary market generally within three months of origination. They are reported at cost, which approximates fair value.

Portfolio loans, net

The fair value of adjustable-rate loans approximates cost. The fair value of fixed-rate loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers for the same remaining maturities. The fair value of the acquired loans are based on the present value of expected future cash flows. The method of estimating fair value does not incorporate the exit-price concept of fair value prescribed by ASC Topic 820.

State tax credits held for sale
The fair value of state tax credits held for sale is calculated using an internal valuation model with unobservable market data including discounted cash flows based upon the terms and conditions of the tax credits.

Derivative financial instruments
The fair value of derivative financial instruments is based on quoted market prices by the counterparty and verified by the Company using public pricing information.

Deposits
The fair value of demand deposits, interest-bearing transaction accounts, money market accounts and savings deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated by discounting the future cash flows using the rates currently offered for deposits of similar remaining maturities.

Subordinated debentures
Fair value of subordinated debentures is based on discounting the future cash flows using rates currently offered for financial instruments of similar remaining maturities.

Federal Home Loan Bank advances
The fair value of the FHLB advances is based on the discounted value of contractual cash flows. The discount rate is estimated using current rates on borrowed money with similar remaining maturities.

Other borrowed funds
Other borrowed funds include customer repurchase agreements, federal funds purchased, notes payable, and secured borrowings related to loan participations. The fair value of federal funds purchased, customer repurchase agreements and notes payable are assumed to be equal to their carrying amount since they have an adjustable interest rate.

Commitments to extend credit and standby letters of credit
The fair value of commitments to extend credit and standby letters of credit are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements, the likelihood of the counterparties drawing on such financial instruments, and the present creditworthiness of such counterparties. The Company believes such commitments have been made on terms which are competitive in the markets in which it operates; however, no premium or discount is offered thereon and accordingly, the Company has not assigned a value to such instruments for purposes of this disclosure.

Limitations
Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgment, and therefore, cannot be determined with precision. Such estimates include the valuation of loans, goodwill, intangible assets, and other long-lived assets, along with assumptions used in the calculation of income taxes, among others. These estimates and assumptions are based on management's best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes to be reasonable under the circumstances. We adjust such estimates and assumptions when facts and circumstances dictate. Decreasing real estate values, illiquid credit markets, volatile equity markets, and declines in consumer spending have combined to increase the uncertainty inherent in such estimates and assumptions. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates. Changes in estimates resulting from continuing changes in the economic environment will be reflected in the financial statement in future periods. In addition, these estimates

do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Fair value estimates are based on existing on-balance and off-balance-sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. In addition, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in many of the estimates.

NOTE 20 - SEGMENT REPORTING

The Company has two primary operating segments, Banking and Wealth Management, which are delineated by the products and services that each segment offers. The segments are evaluated separately on their individual performance, as well as, their contribution to the Company as a whole.

The Banking operating segment consists of a full-service commercial bank, with locations in St. Louis, Kansas City and Phoenix. The majority of the Company's assets and income result from the Banking segment. All banking locations have the same product and service offerings, have similar types and classes of customers and utilize similar service delivery methods. Pricing guidelines and operating policies for products and services are the same across all regions.

The Wealth Management segment includes the Trust division of the Bank and the state tax credit brokerage activities. The Trust division provides financial planning, advisory, private banking, investment management and trust services to businesses, individuals, institutions and non-profit organizations. State tax credits are part of a fee initiative designed to augment the Company's wealth management segment and banking lines of business. Also included in the Wealth Management segment are the discontinued operations of Millennium.

The Corporate segment's principal activities include the direct ownership of the Company's banking and non-banking subsidiaries and the issuance of debt and equity. Its principal sources of revenue are dividends from its subsidiaries and stock option exercises.

The financial information for each business segment reflects that information which is specifically identifiable or which is allocated based on an internal allocation method. There were no material intersegment revenues among the three segments. Management periodically makes changes to methods of assigning costs and income to its business segments to better reflect operating results. When appropriate, these changes are reflected in prior year information presented below.

Following are the financial results for the Company's operating segments.

	At or for the years ended December 31,			
	2011			
(in thousands)	Banking	Wealth Management	Corporate and Intercompany	Total
Net interest income (expense)	118,063	(1,245)	(4,133)	112,685
Provision for loan losses	16,103	—	—	16,103
Noninterest income	7,526	10,486	496	18,508
Noninterest expense	66,548	7,236	3,934	77,718
Income (loss) before income tax expense (benefit)	42,938	2,005	(7,571)	37,372
Income tax expense (benefit)	13,839	678	(2,568)	11,949
Net income (loss)	$29,099	$1,327	$(5,003)	$25,423
Portfolio loans	2,197,684	—	—	2,197,684
Goodwill	30,334	—	—	30,334
Intangibles, net	9,285	—	—	9,285
Deposits	2,773,482	39,440	(21,569)	2,791,353
Borrowings	213,480	45,565	82,581	341,626
Total assets	3,278,328	90,068	9,383	3,377,779
	2010			
	Banking	Wealth Management	Corporate and Intercompany	Total
Net interest income (expense)	89,972	(1,430)	(4,559)	83,983
Provision for loan losses	33,735	—	—	33,735
Noninterest income	9,528	8,664	168	18,360
Noninterest expense	50,877	7,516	3,819	62,212
Income (loss) before income tax expense (benefit)	14,888	(282)	(8,210)	6,396
Income tax expense (benefit)	4,450	(104)	(3,523)	823
Net income (loss)	$10,438	$(178)	$(4,687)	$5,573
Portfolio loans	1,887,921	—	—	1,887,921
Goodwill	2,064	—	—	2,064
Intangibles, net	1,223	—	—	1,223
Deposits	2,272,764	40,353	(15,396)	2,297,721
Borrowings	172,431	56,702	82,581	311,714
Total assets	2,683,937	102,122	14,140	2,800,199
	2009			
	Banking	Wealth Management	Corporate and Intercompany	Total
Net interest income (expense)	75,505	(1,095)	(4,769)	69,641
Provision for loan losses	40,412	—	—	40,412
Noninterest income	14,263	5,559	55	19,877
Noninterest expense	42,143	6,442	4,465	53,050
Goodwill impairment	45,377	—	—	45,377
Loss from continuing operations before income tax benefit	(38,164)	(1,978)	(9,179)	(49,321)

Income tax benefit	4,997	(1,370)	(6,277)	(2,650)
Net loss from continuing operations	(43,161)	(608)	(2,902)	(46,671)
Loss from discontinued operations before income tax	—	(1,995)	—	(1,995)
Income tax benefit	—	(711)	—	(711)
Net loss from discontinued operations	—	(1,284)	—	(1,284)
Total net loss	$(43,161)	$(1,892)	$(2,902)	$(47,955)
Portfolio loans	1,832,125	—	—	1,832,125
Goodwill	2,064	—	—	2,064
Intangibles, net	1,643	—	—	1,643
Deposits	1,914,098	46,844	(19,526)	1,941,416
Borrowings	121,442	48,496	82,581	252,519
Total assets	2,241,092	106,069	18,494	2,365,655

116

NOTE 21-PARENT COMPANY ONLY CONDENSED FINANCIAL STATEMENTS

Condensed Balance Sheets

	December 31,	
(in thousands)	2011	2010
Assets		
Cash	$21,247	$15,396
Investment in Enterprise Bank & Trust	280,620	226,116
Investment in Enterprise Financial CDE, LLC	248	—
Other assets	20,544	21,105
Total assets	$322,659	$262,617
Liabilities and Shareholders' Equity		
Subordinated debentures	$82,581	$82,581
Accounts payable and other liabilities	513	235
Shareholders' equity	239,565	179,801
Total liabilities and shareholders' equity	$322,659	$262,617

Condensed Statements of Operations

	Years ended December 31,		
(in thousands)	2011	2010	2009
Income:			
Dividends from subsidiaries	$—	$—	$800
Other	624	309	203
Total income	624	309	1,003
Expenses:			
Interest expense-subordinated debentures	4,262	4,701	4,918
Other expenses	3,935	3,819	4,465
Total expenses	8,197	8,520	9,383
Net loss before taxes and equity in undistributed earnings of subsidiaries	(7,573)	(8,211)	(8,380)
Income tax benefit	2,568	3,523	6,277
Net loss before equity in undistributed earnings of subsidiaries	(5,005)	(4,688)	(2,103)
Equity in undistributed earnings of subsidiaries	30,428	10,261	(45,852)
Net income (loss)	$25,423	$5,573	$(47,955)

Condensed Statements of Cash Flow

(in thousands)	Years Ended December 31, 2011	2010	2009
Cash flows from operating activities:			
Net income (loss)	$25,423	$5,573	$(47,955)
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Share-based compensation	1,466	1,947	2,202
Net (income) loss of subsidiaries	(30,428)	(10,261)	45,052
Dividends from subsidiaries	—	—	800
Excess tax expense (benefit) of share-based compensation	53	494	338
Other, net	1,207	(585)	587
Net cash (used in) provided by operating activities	(2,279)	(2,832)	1,024
Cash flows from investing activities:			
Cash contributions to subsidiaries	(20,150)	(15,000)	—
Purchases of other investments	(1,114)	(402)	(290)
Proceeds from the sale of other investments	—	93	—
Proceeds from distributions on other investments	694	188	3
Proceeds from business divestitures	—	4,000	—
Purchase of limited partnership interests	—	—	(512)
Net cash used in investing activities	(20,570)	(11,121)	(799)
Cash flows from financing activities:			
Cash dividends paid	(3,577)	(3,121)	(2,694)
Excess tax (expense) benefit of share-based compensation	(53)	(494)	(338)
Dividends paid on preferred stock	(1,750)	(1,750)	(1,585)
Preferred stock issuance cost	—	—	(130)
Issuance of common stock	32,612	14,883	—
Proceeds from the issuance of equity instruments	1,468	357	156
Net cash provided by (used in) financing activities	28,700	9,875	(4,591)
Net increase (decrease) in cash and cash equivalents	5,851	(4,078)	(4,366)
Cash and cash equivalents, beginning of year	15,396	19,474	23,840
Cash and cash equivalents, end of year	$21,247	$15,396	$19,474

NOTE 22-QUARTERLY CONDENSED FINANCIAL INFORMATION (Unaudited)

The following table presents the unaudited quarterly financial information for the years ended December 31, 2011 and 2010.

	2011			
		As Restated(1)	As Restated(1)	As Restated(1)
(in thousands, except per share data)	4th Quarter	3rd Quarter	2nd Quarter	1st Quarter
Interest income	$39,463	$34,285	$38,559	$30,533
Interest expense	7,259	7,516	7,555	7,825
Net interest income	32,204	26,769	31,004	22,708
Provision for loan losses not covered under FDIC loss share	—	5,400	4,300	3,600
Provision for loan losses covered under FDIC loss share	(144)	2,672	275	—
Net interest income after provision for loan losses	32,348	18,697	26,429	19,108
Noninterest income	601	8,726	4,218	4,963
Noninterest expense	23,427	18,302	18,024	17,965
Income before income tax expense	9,522	9,121	12,623	6,106
Income tax expense	2,316	3,289	4,350	1,994
Net income	$7,206	$5,832	$8,273	$4,112
Net income available to common shareholders	$6,570	$5,200	$7,643	$3,486
Earnings per common share:				
Basic	$0.37	$0.29	$0.45	$0.23
Diluted	0.36	0.29	0.43	0.23

	As Restated(1) 2010			
(in thousands, except per share data)	4th Quarter	3rd Quarter	2nd Quarter	1st Quarter
Interest income	$32,271	$30,574	$26,545	$27,004
Interest expense	7,909	7,742	8,108	8,652
Net interest income	24,362	22,832	18,437	18,352
Provision for loan losses not covered under FDIC loss share	3,325	7,650	8,960	13,800
Provision for loan losses covered under FDIC loss share	—	—	—	—
Net interest income after provision for loan losses	21,037	15,182	9,477	4,552
Noninterest income	3,881	4,895	5,287	4,297
Noninterest expense	18,231	15,693	14,392	13,896
Income (loss) before income tax (benefit) expense	6,687	4,384	372	(5,047)
Income tax expense (benefit)	1,701	1,183	(205)	(1,856)
Net income (loss)	$4,986	$3,201	$577	$(3,191)
Net income (loss) available to common shareholders	$4,364	$2,583	$(38)	$(3,803)
Earnings (loss) per common share:				
Basic	$0.29	$0.17	$—	$(0.26)

Diluted	0.29	0.17	—	(0.26)

(1) See Note 24 - Restatement of Consolidated Financial Statements for more information.

NOTE 23-NEW AUTHORITATIVE ACCOUNTING GUIDANCE

FASB ASU 2010-06, “Improving Disclosures about Fair Value Measurements” On January 1, 2011, the Company adopted new authoritative guidance under this ASU, which requires detailed Level 3 roll forward disclosure. The adoption of this guidance did not have a material impact on the Company’s consolidated financial statements.

FASB ASU 2010-29, “Business Combinations (Topic 805)—Disclosure of Supplementary Pro Forma Information for Business Combinations” On January 1, 2011, the Company adopted new authoritative guidance under this ASU which provides clarification regarding the acquisition date that should be used for reporting the pro forma financial information disclosures required by Topic 805 when comparative financial statements are presented. ASU 2010-29 also requires entities to provide a description of the nature and amount of material, nonrecurring pro forma adjustments that are directly attributable to the business combination. The adoption of this guidance did not have a material impact on the Company’s consolidated financial statements.

FASB ASU 2011-02, “Receivables (Topic 310) - A Creditor’s Determination of Whether a Restructuring Is a Troubled Debt Restructuring” On July 1, 2011, the Company adopted new authoritative guidance under this ASU which provides clarification on whether a restructuring constitutes a troubled debt restricting and also clarifies the guidance on a creditor’s evaluation of whether it has granted a concession to the debtor and if the debtor is experiencing financial difficulties. The adoption of this guidance did not have a material impact on the Company’s consolidated financial statements.

FASB ASU 2011-04, “Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS” In May 2011, the FASB issued ASU 2011-04. The ASU is the result of joint efforts by the FASB and IASB to develop a single, converged fair value framework on how (not when) to measure fair value and on what disclosures to provide about fair value measurements. The amended guidance changes several aspects of the fair value measurement guidance in FASB Accounting Standards Codification 820 “Fair Value Measurement” including the following provisions:

- Application of the concepts of highest and best use and valuation premise
- Introduction of a option to measure groups of offsetting assets and liabilities on a net basis
- Incorporation of certain premiums and discounts in fair value measurements
- Measurement of the fair value of certain instruments classified in shareholders' equity

In addition, the amended guidance includes several new fair value disclosure requirements, including information about valuation techniques and unobservable inputs used in Level 3 fair value measurements and a narrative description of Level 3 measurements' sensitivity to changes in unobservable inputs. This ASU is effective for the years beginning after December 15, 2011. The Company believes this ASU will not have a material impact on the Company's consolidated financial statements.

FASB ASU 2011-05, “Presentation of Comprehensive Income" In June 2011, the FASB issued ASU 2011-05 which amends Topic 220, Comprehensive Income by eliminating the option to present components of other comprehensive income (OCI) in the statement of stockholders' equity. This new guidance requires entities to present all nonowner changes in stockholders' equity either as a single continuous statement of comprehensive income or as two separate but consecutive statements. This ASU also requires entities to present all reclassification adjustments from OCI to net income on the face of the statement of comprehensive income. This ASU is effective for the years beginning after December 15, 2011. The Company believes this ASU will not have a material impact on the Company's consolidated financial statements.

FASB ASU 2011-08, "Testing Goodwill for Impairment" In September 2011, the FASB issued ASU 2011-08 which permits entities to first perform a qualitative assessment to determine whether it is more likely than not (a likelihood of more than 50 percent) that the fair value of a reporting unit is less than its carrying amount. If the entity determines that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, it would perform the first step of the goodwill impairment test; otherwise, no further impairment test would be required. This ASU is effective prospectively for annual and interim goodwill impairment tests performed for the years beginning after December 15, 2011. The Company believes this ASU will not have a material impact on the Company's consolidated financial statements.

FASB ASU 2011-11, "Disclosures about Offsetting Assets and Liabilities" In December 2011, the FASB issued ASU 2011-11 which requires entities with financial instruments and derivatives that are either offset on the balance sheet or subject to a master nettting or similar arrangement are required to disclose the following information separately for assets and liabilities in a tabular format:

- Gross amounts of recognized assets and liabilities
- Offsetting amounts that determine the net amount presented in the balance sheet
- Amounts subject to an enforceable master netting arrangement that were not already included in the disclosure required by (2) above, including
  - Amounts related to recognized financial instruments and other derivative instruments if either (a) management makes an accounting election not to offset the amounts, or (b) the amounts do not meet the right of setoff conditions in ASC 210-30-45, Balance Sheet: Offsetting, or in ASC 815-10-45, Derivatives and Hedging
  - Amounts related to financial collateral
- Net amounts after deducting the amounts in (4) from the amounts in (3) above

In addition to the tabular disclosure described above, entities are required to provide a description of the setoff rights associated with assets and liabilities subject to an enforceable master netting arrangement. This ASU is effective for the years beginning on or after January 1, 2013, and interim periods within those annual periods. The guidance must be applied retrospectively for any period presented that begins before an entity's date of initial application. The Company believes this ASU will not have a material impact on the Company's consolidated financial statements.

FASB ASU 2011-12, "Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05" In December, 2011 the FASB issued ASU 2011-12 which indefinitely defers the new provisions under ASU 2011-05 which required entities to present reclassification adjustments out of accumulated other comprehensive income by component in both the statement in which net income is presented and the statement in which other comprehensive income is presented for both interim and annual financial statements. This ASU is effective for the years beginning after December 15, 2011. The Company believes this ASU will not have a material impact on the Company's consolidated financial statements.

NOTE 24 - RESTATEMENT OF CONSOLIDATED FINANCIAL STATEMENTS

Background of the Restatement

In January 2012, while converting to a new system designed to address the complex accounting requirements of acquired loans under Accounting Standards Codification ("ASC") Topic 310-30, “Loans and Debt Securities Acquired with Deteriorated Credit Quality”, the Company discovered an error in its process used to record income on these loans. ASC 310-30 is utilized to account for the loans acquired by the Company under loss sharing agreements with the Federal Deposit Insurance Corporation (the “FDIC”). Under ASC 310-30, these acquired loans are initially recorded at fair value (as determined by the present value of expected future cash flows) with no valuation allowance. The difference between the undiscounted cash flows expected at acquisition and the investment in the loans, or the "accretable yield", is recognized as interest income on a level-yield method over the life of the loans. In accounting for income from the acquired loans, the Company recorded both the accretable yield and contractually required interest payments. The Company should not have recognized the contractually required interest payments. As a result, both interest income and the carrying value of the acquired loans were overstated. This affected income reported on the loans acquired in FDIC assisted transactions since December 2009.

Adjustments

In addition to the adjustments relating to the acquired loan contractual interest described above, the Company has corrected other errors that had been previously identified but not corrected because they were not material, individually

121

or in the aggregate, to the consolidated financial results. These items included changes in accrual estimates and financial statement reclassifications.

The following table presents the impact of the Restatement on the Company's previously issued audited Consolidated Statement of Operations and Consolidated Statement of Cash Flows for the year ended December 31, 2010 and its Consolidated Balance Sheet at December 31, 2010.

(in thousands, except per share data)	At or for the Year ended December 31, 2010 As Previously Reported	Restatement Adjustments	Other Adjustments	As Restated
Consolidated Statement of Operations				
Interest income:				
Interest and fees on loans	$114,041	$(5,141)	$(500)	$108,400
Total interest income	122,035	(5,141)	(500)	116,394
Total interest expenses	32,411	—	—	32,411
Net interest income	89,624	(5,141)	(500)	83,983
Provision for loan losses	33,735	—	—	33,735
Net interest income after provision for loan losses	55,889	(5,141)	(500)	50,248
Noninterest income:				
Wealth Management revenue	6,414	—	—	6,414
Miscellaneous income	1,763	—	—	1,763
Total noninterest income	18,360	—	—	18,360
Noninterest expense:				
Employee compensation and benefits	28,513	(196)	—	28,317
Other	12,128	—	(500)	11,628
Total noninterest expense	62,908	(196)	(500)	62,212
Income before income tax	11,341	(4,945)	—	6,396
Income tax expense (benefit)	2,221	(1,313)	(85)	823
Net income (loss)	9,120	(3,632)	85	5,573
Net income (loss) available to common shareholders	6,653	(3,632)	85	3,106
Basic earnings (loss) per share	$0.45	$(0.24)	$—	$0.21
Diluted earnings (loss) per share	0.45	(0.24)	—	0.21
Consolidated Balance Sheet				
Portfolio loans covered under FDIC loss share at fair value	$126,711	$(5,141)	$—	$121,570
Portfolio loans, net	1,850,303	(5,141)	—	1,845,162
FDIC loss share receivable	88,292	—	(500)	87,792
Total assets	2,805,840	(5,141)	(500)	2,800,199
Other liabilities	11,569	(1,594)	(500)	9,475
Total liabilities	2,622,492	(1,594)	(500)	2,620,398
Retained earnings	19,322	(3,547)	—	15,775
Total shareholders' equity	183,348	(3,632)	85	179,801
Total liabilities and shareholders' equity	2,805,840	(5,141)	(500)	2,800,199
Consolidated Statement of Cash Flows				
Net income (loss)	$9,120	$(3,632)	$85	$5,573
Net accretion of loan discount and indemnification asset	(10,793)	5,141	—	(5,652)
Other, net	3,213	(1,594)	—	1,619

122

The following tables present the impact of the Restatement on the unaudited quarterly financial information for each quarter in 2011.

(in thousands, except per share data)	For the Three months ended March 31, 2011 As Previously Reported	Restatement Adjustments	Other Adjustments	As Restated
Consolidated Statement of Operations				
Interest income:				
Interest and fees on loans	$31,661	$(4,030)	$—	$27,631
Total interest income	34,563	(4,030)	—	30,533
Total interest expenses	7,825	—	—	7,825
Net interest income	26,738	(4,030)	—	22,708
Provision for loan losses	3,600	—	—	3,600
Net interest income after provision for loan losses	23,138	(4,030)	—	19,108
Total Noninterest income	4,963	—	—	4,963
Noninterest expense:				
Other	3,000	—	500	3,500
Total noninterest expense	17,465	—	500	17,965
Income before income tax	10,636	(4,030)	(500)	6,106
Income tax expense	3,557	(1,316)	(247)	1,994
Net income	7,079	(2,714)	(253)	4,112
Net income available to common shareholders	6,453	(2,714)	(253)	3,486
Net income available to common shareholders and assumed conversions	6,824	(3,085)	(253)	3,486
Basic earnings per share	$0.43	$(0.18)	$(0.02)	$0.23
Diluted earnings per share	0.42	(0.18)	(0.01)	0.23

(in thousands, except per share data)	For the Three months ended June 30, 2011 As Previously Reported	Restatement Adjustments	Other Adjustments	As Restated
Consolidated Statement of Operations				
Interest income:				
Interest and fees on loans	$36,420	$(3,163)	$1,694	$34,951
Total interest income	40,028	(3,163)	1,694	38,559
Total interest expenses	7,555	—	—	7,555
Net interest income	32,473	(3,163)	1,694	31,004
Provision for loan losses	4,575	—	—	4,575
Net interest income after provision for loan losses	27,898	(3,163)	1,694	26,429
Noninterest income:				
Miscellaneous income	351	—	(908)	(557)
Total noninterest income	5,126	—	(908)	4,218
Noninterest expense:				
Other	3,195	—	—	3,195
Total noninterest expense	18,024	—	—	18,024
Income before income tax	15,000	(3,163)	786	12,623
Income tax expense	5,118	(1,090)	322	4,350

Net income	9,882	(2,073	) 464	8,273
Net income available to common shareholders	9,252	(2,073	) 464	7,643
Net income available to common shareholders and assumed conversions	9,623	(2,073	) 464	8,014
Basic earnings per share	$0.54	$ (0.12	) $0.03	$0.45
Diluted earnings per share	0.52	(0.11	) 0.02	0.43

123

(in thousands, except per share data)	For the Three months ended September 30, 2011 As Previously Reported	Restatement Adjustments	Other Adjustments	As Restated
Consolidated Statement of Operations				
Interest income:				
Interest and fees on loans	$36,748	$(4,522)	$(1,243)	$30,983
Total interest income	40,050	(4,522)	(1,243)	34,285
Total interest expenses	7,658	—	(142)	7,516
Net interest income	32,392	(4,522)	(1,101)	26,769
Provision for loan losses	5,557	2,515	—	8,072
Net interest income after provision for loan losses	26,835	(7,037)	(1,101)	18,697
Noninterest income:				
Miscellaneous income	281	1,287	877	2,445
Total noninterest income	6,562	1,287	877	8,726
Noninterest expense:				
Total noninterest expense	18,302	—	—	18,302
Income before income tax	15,095	(5,750)	(224)	9,121
Income tax expense	5,394	(2,073)	(32)	3,289
Net income	9,701	(3,677)	(192)	5,832
Net income available to common shareholders	9,069	(3,677)	(192)	5,200
Net income available to common shareholders and assumed conversions	9,440	(3,677)	(192)	5,571
Basic earnings per share	$0.51	$(0.21)	$(0.01)	$0.29
Diluted earnings per share	0.49	(0.19)	(0.01)	0.29

124

ITEM 9: CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

a) Dismissal of independent registered accounting firm.

On May 28, 2010, KPMG LLP (“KPMG”) was dismissed as the independent registered public accounting firm of Enterprise Financial Services Corp (the “Company”).

KPMG's report on the Company's consolidated financial statements for the past two years ended December 31, 2009 and 2008 did not contain an adverse opinion or a disclaimer of opinion, and was not qualified or modified as to uncertainty, audit scope, or accounting principles, except that KPMG's report on the Company's consolidated financial statements as of and for the years ended December 31, 2009 and 2008 contained an explanatory paragraph stating that “As discussed in Note 2 to the consolidated financial statements, the 2008 and 2007 consolidated financial statements have been restated to correct a misstatement.”

The audit reports of KPMG on the effectiveness of internal control over financial reporting as of December 31, 2009 and 2008 did not contain any adverse opinion or disclaimer of opinion, nor were they qualified or modified as to uncertainty, audit scope or accounting principles.

The Audit Committee of the Board of Directors of the Company approved the termination, which was effective as of May 28, 2010.

During the Company's two most recent fiscal years ended December 31, 2009 and 2008 and the subsequent period through May 28, 2010, the Company did not have any disagreements (as defined in Item 304(a)(1)(iv) of Regulation S-K and the related instructions to Item 304 of Regulation S-K) with KPMG on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of KPMG, would have caused it to make reference to the subject matter of the disagreements in connection with its report. Also during this period, there have been no reportable events as that term is described in Item 304(a)(1)(v) of Regulation S-K, except for the material weakness as set forth in the following paragraph:

In connection with the identification of the loan participation accounting error described in Item 7, Management Discussion & Analysis and in Item 8, Note 2 of the consolidated financial statements and elsewhere in the Form 10-K dated March 16, 2010, the Company also determined that a material weakness in its internal controls over financial reporting existed during the periods affected by the error, including as of December 31, 2008. The Company's management concluded that the material weakness was the Company's lack of a formal process to periodically review existing contracts and agreements with continuing accounting significance. To remediate this material weakness, during the fourth quarter of 2009 the Company implemented a formal process to review all contracts and agreements with continuing accounting significance on an annual basis. As a result of the review conducted in the fourth quarter, management did not identify any other errors in its previous accounting for such contracts or agreements. Management believes that this new process has remediated the material weakness in the Company's internal control over financial reporting.

The Company provided KPMG with a copy of the disclosures it is making in response to Item 304(a) of Regulation S-K and requested that KPMG furnish the Company with a letter addressed to the Securities Exchange Commission stating whether it agreed with the statements made by the Company in response to Item 304(a) of Regulation S-K and, if not, stating the respects in which it did not agree. The letter from KPMG was attached as Exhibit 16 to the current report on Form 8-K filed by the Company with the SEC on May 28, 2010.

(b) Engagement of new independent registered accounting firm.

As a result of a competitive request for proposal process undertaken by the Audit Committee of the Board of Directors of the Company, the Audit Committee on May 28, 2010, approved the appointment of Deloitte & Touche LLP ("Deloitte") as the Company's independent registered accounting firm for the year ending December 31, 2010. In deciding to select Deloitte, the Audit Committee reviewed auditor independence issues and existing commercial relationships with Deloitte and concluded that Deloitte has no commercial relationship with the Company that would impair its independence. The Company did not engage Deloitte in any prior consultations during the Company's fiscal years ended December 31, 2009 and 2008 or its subsequent period through the date of the engagement of Deloitte regarding either: (i) the application of accounting principles to a specified transaction, either completed or proposed, or the type of audit opinion that might be rendered on the Company's consolidated financial statements, and neither a written report was provided to the Company nor oral advice was provided that Deloitte concluded was an important factor considered by the Company in reaching a decision as to the accounting, auditing, or financial reporting issue; or (ii) any matter that was the subject of either a disagreement (as defined in Item 304(a)(1)(iv) of Regulation S-K and the related instructions to Item 304 of Regulation S-K) or a reportable event (as defined in Item 304(a)(1)(v) of Regulation S-K).

ITEM 9A: CONTROLS AND PROCEDURES

Restatement of Prior Period Financial Statements

In January 2012, while converting to a new system designed to address the complex accounting requirements of acquired loans under ASC 310-30, “Loans and Debt Securities Acquired with Deteriorated Credit Quality”, the Company discovered an error in its process used to record income on these loans. Both interest income and the carrying value of the acquired loans were overstated. The error affects income reported on all loans acquired in FDIC assisted transactions since December 2009. On January 20, 2012, the Audit Committee of the Board of Directors of the Company and management determined that previously issued consolidated financial statements for the fiscal year 2010 and the interim quarters of 2011 should no longer be relied upon and should be restated.

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of the Company's Chief Executive Officer (“CEO”) and the Chief Financial Officer (“CFO”), management evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15, as of December 31, 2011. Management concluded that, because of the material weakness in our internal controls over financial reporting of the Company's acquired loan portfolio (as discussed below), the Company's disclosure controls and procedures surrounding the Company's acquired loan portfolio were not effective as of December 31, 2011. Notwithstanding the material weakness described below, management has concluded that the consolidated financial statements included in this Form 10K present fairly, in all material respects, the Company's financial position, results of operations and cash flows for the periods presented in conformity with accounting principles generally accepted in the United States.

Management's Assessment of Internal Control Over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting. The Company's internal control over financial reporting is a process designed under the supervision of the Company's CEO and CFO to provide reasonable assurance regarding reliability of financial reporting and preparation of the Company's financial statements for external reporting purposes in accordance with U.S. GAAP.

For the year ended December 31, 2011, management, including our CEO and CFO assessed the effectiveness of the Company’s internal control over financial reporting as of December 31, 2011. 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. As permitted by SEC guidance, management excluded from its assessment the FDIC-assisted transaction of the First National Bank of Olathe described in Note 2 - Acquisitions to the Consolidated Financial Statements. The assets acquired in this acquisition consist primarily of "covered assets" which comprised approximately 6% of total consolidated assets at December 31, 2011. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company’s annual or interim financial statements will not be prevented or detected on a timely basis. Based on management’s assessment, including consideration of the control deficiencies discussed below, management has concluded that the company’s internal control over financial reporting surrounding the Company's acquired loan portfolio was not effective as of December 31, 2011, due to the fact that there was a material weakness in its internal control over financial reporting. Specifically, management identified: (i) control deficiencies in its internal controls associated with the accounting for acquired loans under ASC 310-30 that constitute a material weakness, and (ii) the need to restate prior period financial statements. The material weakness in internal control over financial reporting identified is as follows:

Accounting for Acquired Loans under ASC 310-30, "Loans & Debt Securities Acquired with Deteriorated Credit Quality" - The controls over the accounting entries of acquired loans were improperly designed and were not effective in capturing the accuracy of the resulting yield related to these loans. The controls that had been in place focused primarily on the calculation and accounting of the accretable and non-accretable yields under ASC 310-30. The controls were not effective in recording the accounting entry required to reverse the contractual interest calculated by the Company's loan servicing subsystem.

The effectiveness of the Company's internal control over financial reporting as of December 31, 2011, has been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report which appears herein.

Changes to Internal Control Over Financial Reporting

There have not been any changes in our internal control over financial reporting for the quarter ended December 31, 2011 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Remediation Plan

Management has been actively engaged in developing remediation plans to address the above material weakness. The remediation efforts include, bur are not limited to, the following:

- Implemented a commercially available system specifically designed to address the accounting requirements under ASC 310-30, "Loans & Debt Securities Acquired with Deteriorated Credit Quality";
- Implemented additional reconciliation and other procedures surrounding the calculation of the effective yield for acquired loans;
- Hired additional personnel in the Loss Share accounting department;
- Utilization of an accounting firm to consult in the analysis and preparation of accounting entries required under ASC 310-30; and
- Reversed contractual interest related to the acquired loans.

In addition, under the direction of the Audit Committee, management will continue to review and make necessary changes to the overall design of the company’s internal control environment, as well as to policies and procedures to improve the overall effectiveness of internal control over financial reporting.

If not remediated, these control deficiencies could result in further material misstatements to the Company’s financial statements.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders
Enterprise Financial Services Corp
St. Louis, Missouri

We have audited the internal control over financial reporting of Enterprise Financial Services Corp and subsidiaries (the "Company") as of December 31, 2011, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis. The following material weakness has been identified and included in management's assessment: the controls over accounting for acquired loans under ASC 310-30, “Loans & Debt Securities Acquired with Deteriorated Credit Quality”. This material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the consolidated financial statements as of and for the year ended December 31, 2011, of the Company and this report does not affect our report on such financial statements.

In our opinion, because of the effect of the material weakness identified above on the achievement of the objectives of the control criteria, the Company has not maintained effective internal control over financial reporting as of December 31, 2011, based on the criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial as of and for the year ended December 31, 2011, of the Company and our report dated April 23, 2012 expressed an unqualified opinion on those financial statements and included an explanatory paragraph regarding the restatement of the 2010 financial statements as described in Note 24.

/s/ Deloitte & Touche LLP

St. Louis, MO
April 23, 2012

ITEM 9B: OTHER INFORMATION

2011 Short Term Incentive Awards
On April 20, 2012, the Compensation Committee (the “Committee”) of Enterprise Financial Services Corp (the “Company”) approved awards for the Company's named executive officers under the Company's 2011 Short-Term Incentive Plan (the “2011 STIP”).

Under the 2011 STIP, each of the Company's Named Executive Officers were eligible to receive awards as follows: 40% of the award was based on an earnings per share goal, 20% of the award was based on an asset quality goal, 20% of the award was based on a dependency ratio goal and 20% of the award was based on a leadership rating for the individual named executive officer. The asset quality goal is measured by calculating the “classified assets” of the Company's banking subsidiary (excluding covered assets) as a percent of equity capital and reserves. The dependency ratio goal is measured by the degree to which the Company's banking subsidiary funds longer-term assets (such as loans and securities that mature in more than one year) with non-core funding (such as brokered accounts, as defined by the Bank's call reports to federal banking regulators, including certificates of deposit, and large deposits, as defined by the Bank's Asset Liability Committee).

Based on performance of the Company and each named executive officer measured against each of these four goals, the Committee determined the amount of STIP awards to be paid to the named executive officers for the year ended December 31, 2011, as follows:

Named Executive Officer	STIP Award (1)
Peter F. Benoist, President and Chief Executive Officer	$185,925
Frank H. Sanfilippo, Executive Vice President and Chief Financial Officer	68,175
Stephen P. Marsh, Executive Vice President; Chairman and Chief Executive Officer - Enterprise Bank & Trust	104,063
Robert J. Witterschein, Executive Vice President, Enterprise Bank & Trust	99,825
John G. Barry, Executive Vice President, Enterprise Bank & Trust	86,213

(1) In order to comply with the regulations under the United States Treasury's Capital Purchase Program (the “CPP”), the top five most highly compensated employees of the Company are prohibited from receiving cash bonuses, and are only permitted to receive incentive compensation in the form of “long-term restricted stock.” Pursuant to these regulations, Mr. Benoist, Mr. Marsh, Mr. Witterschein and Mr. Barry received their 2011 STIP awards in the form of shares of restricted stock of the Company. Mr. Sanfilippo was not prohibited from receiving a cash award and thus the Committee determined to pay his 2011 STIP awards in cash. Grants are denominated in dollars. The number of shares of long-term restricted stock issued pursuant to any award is determined by dividing the dollar value of the award by the market value of the Company's common stock on the date of the award.

For more information concerning awards pursuant to the 2011 STIP, see the Compensation Discussion and Analysis section of the Company's Proxy Statement for its annual meeting to be held on June 4, 2012.

Clawback of 2010 Incentive Compensation
In connection with the Restatement and pursuant to the Company's clawback policy, the Compensation Committee reviewed variable compensation awarded with respect to the Company's performance during the 2010 fiscal year. The Company's clawback policy states that any variable compensation paid to its Named Executive Officers and top twenty other most highly compensated employees (the “Covered Employees”) is subject to recovery or “clawback” if the variable compensation is based on materially inaccurate financial statements. In its review, the Committee examined all components of variable compensation and determined that the restatement affected awards under the Company's

2010 Short-Term Incentive Plan made to Named Executive Officers and other Covered Employees for the performance

130

goal based on the Company's earnings per share (the “EPS Goal”).

The aggregate amounts subject to recovery consisted of $79,800 in cash payments and 8,313 shares of long-term restricted stock. At the direction of the Committee, all of this cash and stock has been recovered by the Company. The Named Executive Officers of the Company for the 2010 fiscal year, in aggregate forfeited 7,449 shares of long-term restricted stock to the Company.

For more information concerning the Company's recovery of 2010 short-term incentive awards pursuant to the clawback policy, see the Compensation Discussion and Analysis section of the Company's Proxy Statement for its annual meeting to be held on June 4, 2012.

PART III

ITEM 10: DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this item is incorporated herein by reference to the Company's Proxy Statement for its annual meeting to be held on Monday, June 4, 2012. The Company's executive officers consist of the named executive officers disclosed in the Compensation Discussion and Analysis Section of the Proxy Statement.

ITEM 11: EXECUTIVE COMPENSATION

The information required by this item is incorporated herein by reference to the Company's Proxy Statement for its annual meeting to be held on Monday, June 4, 2012.

ITEM 12: SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this item is incorporated herein by reference to the Company's Proxy Statement for its annual meeting to be held on Monday, June 4, 2012.

ITEM 13: CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

The information required by this item is incorporated herein by reference to the Company's Proxy Statement for its annual meeting to be held on Monday, June 4, 2012.

ITEM 14: PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this item is incorporated by reference to the Company's Proxy Statement for its annual meeting to be held on Monday, June 4, 2012.

PART IV

ITEM 15: EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) 1. Financial Statements

The consolidated financial statements of Enterprise Financial Services Corp and its subsidiaries and independent auditors' reports are included in Part II (Item 8) of this Form 10-K.

2. Financial Statement Schedules

All financial statement schedules have been omitted, as they are either inapplicable or included in the Notes to Consolidated Financial Statements.

3. Exhibits

Exhibit No.	Description
3.1	Certificate of Incorporation of Registrant, (incorporated herein by reference to Exhibit 3.1 of Registrant's Registration Statement on Form S-1 filed on December 19, 1996 (File No. 333-14737)).
3.2	Amendment to the Certificates of Incorporation of Registrant (incorporated herein by reference to Exhibit 4.2 to Registrant's Registration Statement on Form S-8 filed on July 1, 1999 (File No. 333-82087)).
3.3	Amendment to the Certificate of Incorporation of Registrant (incorporated herein by reference to Exhibit 3.1 to Registrant's Quarterly Report on Form 10-Q for the period ending September 30, 1999).
3.4	Amendment to the Certificate of Incorporation of Registrant (incorporated herein by reference to Exhibit 99.2 to Registrant's Current Report on Form 8-K filed on April 30, 2002).
3.5	Amendment to the Certificate of Incorporation of Registrant (incorporated herein by reference to Appendix A to Registrant's Proxy Statement on Form 14-A filed on November 20, 2008).
3.6	Certificate of Designations of Registrant for Fixed Rate Cumulative Perpetual Preferred Stock, Series A, dated December 17, 2008 (incorporated herein by reference to Exhibit 3.1 to Registrant's Current Report on Form 8-K filed on December 23, 2008).
3.7	Bylaws of Registrant, as amended, (incorporated herein by reference to Exhibit 3.1 to Registrant's Current Report on Form 8-K filed on October 2, 2007).
10.1.1*	Key Executive Employment Agreement dated effective as of July 1, 2008 by and between Registrant and Stephen P. Marsh (incorporated herein by reference to Exhibit 99.1 to Registrant's Current Report on Form 8-K filed on November 25, 2008), and amended by that First Amendment of Executive Employment Agreement dated as of December 19, 2008 (incorporated herein by reference to Exhibit 99.6 to Registrant's Current Report on Form 8-K filed on December 23, 2008).
10.1.2*	Key Executive Employment Agreement dated effective as of December 1, 2004 by and between Registrant and Frank H. Sanfilippo (incorporated herein by reference to Exhibit 10.1 to Registrant's Current Report on

Form 8-K filed on December 1, 2004), and amended by that First Amendment of Executive Employment Agreement dated as of December 19, 2008 (incorporated herein by reference to Exhibit 99.5 to Registrant's Current Report on Form 8-K filed on December 23, 2008).

10.1.3*	Key Executive Employment Agreement dated effective as of September 24, 2008, by and between Registrant and Peter F. Benoist (incorporated herein by reference to Exhibit 10.1 to Registrant's Current Report on Form 8-K filed on September 30, 2008), and amended by that First Amendment of Executive Employment Agreement dated as of December 19, 2008 (incorporated herein by reference to Exhibit 99.3 to Registrant's Current Report on Form 8-K filed on December 23, 2008).
10.1.4*	Executive Employment Agreement dated effective as of March 29, 2010, by and between Registrant and Robert J. Witterschein (filed herewith).
10.1.5*	Amended and Restated Key Executive Employment Agreement dated effective as of February 17, 2010, by and among Registrant, Enterprise Bank & Trust, and John G. Barry (incorporated herein by reference to Exhibit 99.2 to Registrant's Current Report on Form 8-K filed on February 19, 2010).
10.1.6*	Waiver executed by each of Peter F. Benoist, Frank H. Sanfilippo, Linda M. Hanson, Stephen P. Marsh and John G. Barry (incorporated herein by reference to Exhibit 99.2 to Registrant's Current Report on Form 8-K filed on December 23, 2008).
10.1.7*	Enterprise Financial Services Corp Deferred Compensation Plan I (incorporated herein by reference to Exhibit 10.1 of Registrant's Quarterly Report on Form 10-Q for the period ended March 31, 2000).
10.1.8*	Enterprise Financial Services Corp Amended and Restated Deferred Compensation Plan I dated effective as of December 31, 2008 (incorporated by reference to Exhibit 10.9 to Registrant's Report on Form 10-K for the year ended December 31, 2008).
10.1.9*	Enterprise Financial Services Corp, Third Incentive Stock Option Plan (incorporated herein by reference to Exhibit 4.5 to Registrant's Registration Statement on Form S-8 filed on December 29, 1997 (File No. 333-43365)).
10.1.10*	Enterprise Financial Services Corp, Fourth Incentive Stock Option Plan (incorporated herein by reference to Registrant's 1998 Proxy Statement on Form 14-A).
10.1.11*	Enterprise Financial Services Corp, Stock Plan for Non-Management Directors (incorporated herein by reference to Registrant's Proxy Statement on Form 14-A filed on March 7, 2006).
10.1.12*	Enterprise Financial Services Corp, 2002 Stock Incentive Plan, as amended (incorporated herein by reference to Registrant's Proxy Statement on Form 14-A, filed on March 17, 2008).
10.1.13*	Enterprise Financial Services Corp, Annual Incentive Plan (incorporated herein by reference to Registrant's Proxy Statement on Form 14-A, filed on March 7, 2006).
10.1.14*	Enterprise Financial Services Corp, Incentive Stock Purchase Plan (incorporated herein by reference to Exhibit 4.6 to Registrant's Registration Statement on Form S-8 filed on November 1, 2002 (File No. 333-100928)).
10.1.15*	Form of Enterprise Financial Services Corp Restricted Stock Award Agreement (incorporated herein by reference to Exhibit 99.1 to Registrant's Current Report on Form 8-K filed on February 19, 2010);
10.1.16*	Form of Restricted Stock Award Agreement with John G. Barry (incorporated herein by reference to Exhibit 99.3 to Registrant's Current Report on Form 8-K filed on February 19, 2010.)

10.2	Indenture dated December 12, 2008, by and between Registrant and Wilmington Trust Company (incorporated herein by reference to Exhibit 4.1 to Registrant's Current Report on Form 8-K filed on December 15, 2008).
10.3	Amended and Restated Declaration of Trust dated December 12, 2008, by and among Registrant, Wilmington Trust Company, and each of the Administrators named therein (incorporated herein by reference to Exhibit 4.2 to Registrant's Current Report on Form 8-K filed on December 15, 2008).

133

10.4	Guarantee dated December 12, 2008, by and between Registrant and Wilmington Trust Company (incorporated herein by reference to Exhibit 4.3 to Registrant's Current Report on Form 8-K filed on December 15, 2008).
10.5	First Amendment to Amended and Restated Declaration of Trust No. 2 dated January 9, 2009 by and among Registrant, Wilmington Trust Company and each of the Administrators named therein (incorporated herein by reference to Exhibit 10.23 to Registrant's Report on Form 10-K for the year ended December 31, 2008).
10.6	Warrant to Purchase Shares of Common Stock dated December 19, 2008, by Registrant in favor of the United States Department of the Treasury (incorporated herein by reference to Exhibit 4.1 to Registrant's Current Report on Form 8-K filed on December 23, 2008).
10.7	Letter Agreement dated December 19, 2008, including Securities Purchase Agreement - Standard Terms incorporated by reference therein, by and between Registrant and the United States Department of the Treasury (incorporated herein by reference to Exhibit 99.1 to Registrant's Current Report on Form 8-K filed on December 23, 2008).
10.8	Loan Sale Agreement dated July 9, 2010 by and between the Federal Deposit Insurance Corporation, as Receiver for Home National Bank, Blackwell, Oklahoma and Enterprise Bank & Trust (incorporated by reference to Exhibit 10.1 to Registrant's Quarterly Report on Form 10-Q filed on August 6, 2010.)
10.9	Purchase and Assumption Agreement dated January 7, 2011, by and between Enterprise Bank & Trust and the Federal Deposit Insurance Corporation as Receiver for Legacy Bank (incorporated by reference to Exhibit 10.1 to Registrant's Quarterly Report on Form 10-Q filed on May 10, 2011).
10.10	Purchase and Assumption Agreement dated August 12, 2011, by and between Enterprise Bank & Trust and the Federal Deposit Insurance Corporation as Receiver for The First National Bank of Olathe (incorporated by reference to Exhibit 10.1 to Registrant's Current Report on Form 8-K/A filed on October 28, 2011).
12.1	Computation of Ratio of Earnings to Fixed Charges and Preferred Dividends
16.1	Letter Regarding Change in Certifying Accountant (incorporated herein by reference to Exhibit 16 to Registrant's Current Report on Form 8-K filed on June 4, 2010.)
21.1	Subsidiaries of Registrant.
23.1	Consent of KPMG LLP.
23.2	Consent of Deloitte & Touche LLP.
24.1	Power of Attorney.
31.1	Chief Executive Officer's Certification required by Rule 13(a)-14(a).
31.2	Chief Financial Officer's Certification required by Rule 13(a)-14(a).
32.1	

	Chief Executive Officer Certification pursuant to 18 U.S.C. § 1350, as adopted pursuant to section § 906 of the Sarbanes-Oxley Act of 2002.
32.2	Chief Financial Officer Certification pursuant to 18 U.S.C. § 1350, as adopted pursuant to section § 906 of the Sarbanes-Oxley Act of 2002.

99.1	Certification of Chief Executive Officer pursuant to Section III(b)(4) of the Emergency Economic Stabilization Act of 2008.
99.2	Certification of Chief Financial Officer pursuant to Section III(b)(4) of the Emergency Economic Stabilization Act of 2008.

* Management contract or compensatory plan or arrangement.

Note:
In accordance with Item 601 (b) (4) (iii) of Regulation S-K, Registrant hereby agrees to furnish to the SEC, upon its request, a copy of any instrument that defines the rights of holders of each issue of long-term debt of Registrant and its consolidated subsidiaries for which consolidated and unconsolidated financial statements are required to be filed and that authorizes a total amount of securities not in excess of ten percent of the total assets of the Registrant on a consolidated basis.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on April 23, 2012.

ENTERPRISE FINANCIAL SERVICES CORP

/s/ Peter F. Benoist	/s/ Frank H. Sanfilippo
Peter F. Benoist	Frank H. Sanfilippo
Chief Executive Officer	Chief Financial Officer

Pursuant to the requirements of the Securities Act of 1934, this Report on Form 10-K has been signed by the following persons in the capacities indicated on April 23, 2012.

Signatures	Title
/s/ Peter F. Benoist* Peter F. Benoist	President and Chief Executive Officer and Director
/s/ James J. Murphy, Jr.* James J. Murphy, Jr.	Chairman of the Board of Directors
/s/ Michael A. DeCola* Michael A. DeCola	Director
/s/ William H. Downey* William H. Downey	Director
/s/ John S. Eulich* John S. Eulich	Director
/s/ Robert E. Guest, Jr.* Robert E. Guest, Jr.	Director
/s/ Lewis A. Levey* Lewis A. Levey	Director
/s/ Birch M. Mullins* Birch M. Mullins	Director
/s/ Brenda D. Newberry* Brenda D. Newberry	Director
/s/ John M. Tracy* John M. Tracy	Director
/s/ Sandra A. Van Trease* Sandra A. Van Trease	Director

*Signed by Power of Attorney.